
OFT's action on credit card default charges

5 April 2006

The OFT wrote to eight major credit card issuers last year to inform them of our provisional view that the amount they charged consumers for missing/late payments (default charges), or for going over their credit limit, was too high. We invited the credit card issuers to consult with us on this issue.

Following discussions with the eight issuers, and after consideration of complaints, we have produced a statement of the principles we think card issuers should follow in order to set fair default charges. This is intended to protect consumers from being charged unfair amounts, but also to enable banks to compete vigorously and fairly. For the full statement see www.offt.gov.uk/Business/Legal/UTCC/guidance.htm

We consider that a contract term is likely to be unfair if it requires consumers to pay more as a result of a default than the court would order them to pay if they were sued for breach of contract. This means that a default charge should not exceed a reasonable pre-estimate of the administrative costs that the consumer ought to have realised would be likely to be incurred by his or her card issuer in dealing with defaults. What costs were in the reasonable contemplation of the consumer would be a question for the court to decide. We think that in general terms a default charge may include postage and stationery costs, and also a proportionate share of the costs of employing staff and of maintaining premises and IT systems in order to deal with defaults of the same kind. The precise level of any particular fair default fee, however, would depend on the business circumstances of the particular credit card issuer.

Please be aware that only a court can decide whether a term is unfair and what is stated here is just our view.

What happens now?

We expect card issuers to recalculate their default charges in line with the principles in our statement to achieve consistency with unfair contract terms legislation. We have decided that, as a provisional step, it is appropriate to give priority to addressing default charges which exceed a simple monetary threshold of £12, in line with our duty to use our resources to tackle contract terms that have the potential to cause the most serious harm to consumers. We are not suggesting that default fees should be set at £12, and a court will certainly not consider that a default fee is fair just because it is below the threshold.

Our presumption will be that credit card default charges set above this level are unfair unless there are exceptional business factors (relevant factors are set out in paragraphs 5.9 -5.11 of the Statement). Where we conclude that a fee above the threshold is unfair we are likely to challenge the charge but will take into account all the circumstances in deciding whether to do so or not. On the other hand, in line with our priorities, we do not propose at present to consider legal action where charges are set below £12.

Why not take enforcement action?

We do not think it is in the overall interests of consumers for us to start court proceedings at present. One reason for this is that it would not be practicable for us to take action against the whole body of card issuers at once, and any court action against even one issuer could be expected to be lengthy as well as costly to both sides. We expect our current approach to bring about a significant change in the whole market which will bring a swifter benefit to consumers. We are not ruling out the possibility of taking legal action in future if we feel it appropriate. We will consider further action if trends in the market suggest that our approach is not achieving an appropriate and early change in the market.

We have given credit card issuers a short time to respond to this statement and tell us whether they are willing to make changes to their default charges.

We accept that changes will require IT system and other business changes by the credit card issuers which may take some time to fully implement but we think that steps to reduce charges should be taken as a matter of exceptional priority even if this means that consequential changes occur at a later date.

We or our co-enforcers will investigate further and will take appropriate action if change does not occur within a reasonable timescale.

There is also a read across of the general principles in this work to other default charges in consumer contracts such as bank overdrafts, store cards and mortgages. We are inviting the banks and other financial services businesses to review such charges accordingly.

What can consumers do?

An unfair term in a consumer contract is not binding on the consumer. However, a number of credit card issuers have disputed our view on how to calculate fair default charges and only a court can finally decide the issue. If you want further advice about your rights and obligations under your credit card agreement, you should seek independent legal advice

The OFT statement sets out in detail our view of the law and what costs can and cannot be taken into account. Individual consumers are certainly free to take account of the statement in deciding whether to question default fees that they have been charged but should take their own legal advice before mounting a challenge or refusing to pay.

We would also strongly recommend that anyone who is struggling to pay debts of any kind seeks early help and advice from one of the free advice agencies such as Citizens Advice, Citizens Advice Scotland, Advice UK or Consumer Credit Counselling Service.

In certain circumstances you may be able to reduce the likelihood of being required to pay default charges by taking various steps to ensure you pay on time such as setting up a direct debit to the lender to pay at least the minimum sum required each month. However, this may not be suitable for all consumers. For help on deciding what is right for you, you should seek advice from free independent advice agencies.

The Financial Ombudsman Service can help settle individual disputes between businesses providing financial services and their customers. Its service is free to consumers but they must have first complained to the business concerned, before it can look at the case. FOS can be contacted at: The Financial Ombudsman Service, South Quay Plaza, 183 Marsh Wall, London, E14 9SR. The consumer helpline number is 0845 080 1800.

