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**Validation Orders (VO) Application Forms – Notes**

**Stage 2 – Consumer Harm Assessment**

**What is a Consumer Harm Assessment?**

Stage 2 (5-6) of the VO application will require you to complete a consumer harm assessment. The purpose of this assessment is to identify any actual or potential consumer harm that may have occurred or may occur in the future in connection with the relevant agreements into which affected consumers have entered.

The assessment will involve four steps (full details outlined below). These are:

1. Customer journey walkthrough
2. Customer contact exercise
3. Report setting out your consumer harm assessment
4. Request from FCA for clarification and/or to discuss your findings

**IMPORTANT**: The applicant must undertake a robust and comprehensive consumer contact exercise and provide a robust and comprehensive assessment of consumer harm. If the applicant does not do so, the likelihood is that the FCA will not be able to reach the positive conclusion that it is “just and equitable” to grant a validation order – and so the validation order will not be granted.

**Why do we require a Consumer Harm assessment to be completed?**

The FCA may only grant a VO if it is “satisfied that it is just and equitable to do so in the circumstances of the case”.

When considering if it is just and equitable, we will consider any actual or potential consumer harm that has occurred (or may occur) in connection with the relevant agreements into which affected consumers have entered.

**Important information regarding the Consumer Harm assessment**

* Pre-application service: Firms are encouraged to reach out to the FCA before submitting an application for a Validation Order. This will enable the firm to understand what is required of it when applying for a VO, including what is involved in the consumer harm assessment (of which the customer contact exercise plays an important part).
* Impartial, fair and transparent: Firms must ensure that the customer contact exercise and consumer harm assessment have been carried out in an impartial, fair and transparent manner.

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* Costs: In addition to the application fees that are payable to the FCA, firms must fund all costs involved in undertaking the Consumer Harm Assessment (including the customer contact exercise) to the requisite high standard.
* External support: Firm’s may wish to consider partnering with a consultant with suitable experience as determined by the firm. This could be a consultant with experience of being a skilled person that prepares reports assessing consumer harm / conducting contact exercises. If so, you must tell us who they are; we will expect the consultant to confirm to us that they are satisfied that the consumer harm exercise has been undertaken (and its results presented) in an impartial, fair and transparent manner. You must also provide the terms of engagement with the consultant and confirm that you have reviewed, approved and taken responsibility for their findings.

Step-by-step process

Step 1: Customer journey walkthrough

After we have reviewed Stage 1 of your application (ie. Section 2 of the form) and confirmed in writing that the relevant agreements are unenforceable and that the Authority has jurisdiction to determine the application, you will be asked to complete the Consumer Harm Assessment. The first stage of this is the ‘customer journey walkthrough’.

You must provide full details the end-to-end customer journey for the relevant loans during the period in which they were entered into that customers would have experienced. This includes an outline of what the customer experienced and what actions were completed internally at each stage of this customer journey. Please note, you are required to provide details of what customers as a whole experienced and the process(es) that were in place at the relevant period, rather than a record of each individual customer/agreement. The steps which you must outline include:

* Distribution channels and customer onboarding including:
  + Examples of advertising/financial promotions used to invite or induce customers
  + Things said and done by any Credit Brokers, ARs and IARs used (if applicable) along with copies of the agreements that were in place.
* Decision making process in respect of the lending decision including:
  + Information obtained from the customer (such as income/expenditure)
  + Information obtained from third parties such as CRAs
  + AML/Financial Crime checks completed
  + Creditworthiness/Affordability assessments completed (including by who and when)
  + Copies of the Credit Agreements/Pre-contact information used
* Collections/Arrears/Forbearance processes including:
  + How collections were made
  + Actions undertaken for contacting customers in arrears
  + Forbearance options used and how decisions were made to offer/not offer forbearance
* Defaults including
  + Actions undertaken for customers who defaulted
  + Actions undertaken by any third-party debt collectors (if applicable)
* Vulnerable customers
  + Actions you completed to identify vulnerable and/or potentially vulnerable customers
  + Actions taken to cater for vulnerable customers’ needs

You may be required to present this customer journey to your case-officer (either in person at the FCA’s office or via a video conference).

If the customer journey was different (eg for a subset of the relevant loans and/or as it changed over time), you should provide separate documents that walkthrough each of those different customer journeys. You should ensure you make clear which journey applies to each of the relevant agreements.

Step 2: Customer contact exercise

After you have completed Step 1 (customer journey walkthrough), you will need to undertake a customer contact exercise. This will involve you preparing and sending to each affected customer a questionnaire that aims to understand the customer journey that they experienced and any actual or potential consumer harm that may have occurred (or may occur in the future) in connection with the relevant agreements into which affected consumers have entered.

When you send your questionnaire to affected consumers, you must ensure that you provide them with a clear explanation (in writing) of the following:

* that their agreement is currently unenforceable (and why)
* of the order you are seeking from the FCA and what it will mean for them if it is granted
* that it is important they respond to the customer contact exercise, as it is their opportunity to make representations to the FCA on whether it should grant the validation order sought (either unconditionally or subject to conditions) and why.

This is to ensure that each customer is clear as to why they are being approached (which will help them understand what information they should provide in reply) and of the importance that they respond to you with their views.

**How should I contact affected customers?**

You should send the questionnaire in writing to each affected consumer. Where you are unable to contact a relevant consumer, you must exhaust all reasonable means to identify accurate contact details.

You should also consider what an appropriate communication strategy looks like. You will also need to consider an appropriate method of making initial contact (outlining why you are contacting them and why they should respond), chasing customers who do not initially respond and concluding your contact and providing ongoing updates. For example, you may decide to send chasers through a variety of means (e.g. text message; letter; email; telephone) in such a way that you reasonably consider is most likely to maximise the prospect of each affected consumer responding to the questionnaire.

**What is the process for preparing/finalising the questionnaire?**

**Responsibility for ensuring that the exercise is sufficiently robust rests solely with the applicant; you will therefore need to identify all additional questions that affected consumers should be asked to ensure consumer detriment is properly identified on the specific facts.**

Without detracting from that responsibility, before you send your questionnaire to affected consumers, you should submit both the questionnaire and your proposed strategy for contact customers to your case-officer for their review. They may have recommendations on additional matters you should incorporate into your questionnaire and/or on your proposed approach for contacting affected consumers.

**What questions should I include in my questionnaire?**

As noted above, responsibility for ensuring that the exercise is sufficiently robust rests solely with the applicant; you will therefore need to identify all additional questions that affected consumers should be asked to ensure consumer detriment is properly identified on the specific facts.

In preparing your questionnaire you should consider the following:

* The purpose of the questionnaire is to elicit the information required to give a robust and comprehensive view on the extent of any actual/potential consumer detriment that may have occurred (or may occur in the future) in connection with the relevant agreements into which affected consumers have entered. Your questions should be designed with this essential objective in mind.
* When preparing your questions, you must bear in mind the difference between ‘closed’ questions (eg Yes/No or multiple choice questions) and ‘open’ questions (i.e. asking the consumer to set out their response in a free text field). You will likely need to use a combination of these question types.
* Your questions must be relevant to understanding the consumer journey as experienced by the affected consumer and identifying actual and/or potential harm that has occurred or may occur.
* Neutral/unloaded ie not encouraging or leading the customer to a specific response.
* Written in plain and easy to understand language for the customer, with each question drafted as succinctly as possible.
* You must ask all questions necessary to identify actual/potential consumer detriment, but avoid the risk of overloading the affected consumer with unnecessary or repetitive questions.
* In a format that is suitable/accessible to the customer so that they have equal opportunity to respond.

Example questions that you should consider including in your questionnaire are set out below (but on the proviso these are intended simply as a starting point for firms preparing their questionnaires):

1. How many loans have you taken out with “enter firm name here”?
2. What were the dates of each loan you took out with “enter firm name here”?
3. Please provide an overview of your journey, including:
   1. how you found out about the loan/lender
   2. who you approached (or were approached by)
   3. what you were told at each stage of the journey and by whom
   4. what was involved in you signing the loan documentation
   5. your correspondence in relation to the loan after entering into it.
4. Were you given documentation or anything in writing that explained the following:
   1. the terms and conditions of the loan?
   2. your obligations under the loan?
   3. how long the loan would last?
   4. what the total cost of the loan would be?
   5. what the APR rate of the loan was?
   6. what action the lender could take if you failed to repay?
   7. how you could raise a complaint if you felt dissatisfied?
5. Was anything said orally (and if so when and by whom) on any of the matters in [4]?
6. Overall, were you made aware of the full terms and conditions of the loan before you entered into the agreement? If so, how, when and by whom? If not, what were you not told about?
   1. Did you provide any details of your income/expenditure? If so, what did this involve – for example, what were you asked to provide, when and by whom?
7. Did you feel at any time pressured into taking out a loan with “enter firm name here”? If so, please explain why.
8. Did you struggle to keep up with repayments? If so, please explain in what way and the impact this had on you.
9. Did the loan repayments impact your ability to keep up with other bills? If so, please explain in what way and the impact this had on you.
10. Did you fall into arrears? If so:
    1. Did you raise your difficulties with the lender?
    2. If so, what did the lender say and were you given any forbearance options?
    3. What forbearance options were you given and what conclusion was reached in relation to them?
11. Did you default?
    1. If so, did this impact your ability to gain other forms of credit?
    2. If yes, please explain what impact this had.
12. Did you make a complaint in relation to your lending product? If so:
    1. Why did you complain, when, how and to whom?
    2. What was the response to the complaint?
    3. Were you satisfied with the way in which “enter applicant firm name here” handled your complaint? If not, please explain why not.
13. If the loan was used to purchase a product or service:
    1. What product or service did you buy?
    2. Was the product or service suggested to you by the lender or their agent? If so, what were you told, when, how and by whom?
    3. Were you satisfied with the quality of the product or service? If not, please provide details.
14. Overall, how satisfied were you with the service received from “enter applicant firm here”?
15. Overall, do you have any concerns with your lending product and/or the way in which it was sold to you?
16. Do you feel the FCA should grant “applicant firm” a Validation Order for the relevant agreements? Please explain the reasons for your view in as much detail as possible.
17. Is there any other information you consider that the FCA should take into account when determining whether to grant a Validation Order for the relevant agreements? If there is, please set it out in as much detail as possible.
18. Do you have any written correspondence or other documents relevant to any of your answers in this questionnaire? If so, please provide copies.

As noted above, these questions are intended as a starting point for firms to use when designing their individual questionnaire. Each firm must identify the questions they should ask to ensure they undertake a robust and comprehensive consumer contact exercise and provide a robust and comprehensive assessment of consumer harm.

Once we have reviewed your proposed questionnaire and contact strategy, we will provide you with any recommendations on it (And we may ask to see a revised version). Once the questionnaire is finalised, you should proceed with issuing it to all affected customers.

**What happens if I do not carry out a customer contact exercise to the required high standard?**

The FCA may only grant a validation order if it is positively satisfied that it is “just and equitable in the circumstances of the case” to do so.

Given that consumer detriment is a relevant factor when the FCA is deciding whether to grant a validation order, the applicant must ensure that it can demonstrate to the FCA what (if any) consumer detriment has occurred or may occur in connection with the relevant agreements and how it is being mitigated.

To do this, the applicant must undertake a robust and comprehensive consumer contact exercise and provide a robust and comprehensive assessment of consumer harm. If the applicant does not do so, the likelihood is that the FCA will not be able to reach the positive conclusion that it is “just and equitable” to grant a validation order – and so the validation order will not be granted.

Step 3: Report setting out your consumer harm assessment

Once the exercise has been completed the applicant will be required to provide the following as part of Stage 2 of its application. In terms of the structure of your assessment, it must comprise:

1. the underlying evidence from the consumer contact exercise (including copies of the applicant’s correspondence as sent to each affected consumer and their responses)
2. Management Information (MI) data on, for example, complaints, arrears/defaults, forbearance, affordability and enforcement (see further below)
3. evidence from any additional investigations and enquiries that the applicant has conducted in order to identify the extent of any consumer harm that has occurred or may occur in connection with the relevant agreements
4. a summary of:
   1. how the consumer contact exercise was conducted (including when and how each of the affected consumers was contacted and the response rate); and
   2. the results of the exercise, insofar as informs an assessment of actual and potential consumer detriment
5. detailed analysis of:
   1. the underlying evidence at (1) and (2) above
   2. to the extent the customer contact exercise and wider enquires have evidenced any actual or potential harm, the steps the applicant has taken and/or will take to mitigate it
   3. whether the applicant proposes to leave any actual or potential detriment unmitigated and, if so, what specifically and why
6. a detailed explanation of why the applicant considers that the results of its consumer contact exercise (and any wider investigations and enquiries) allow a sufficiently robust and reliable view to be reached on the actual and potential detriment suffered by all affected customers
7. a detailed explanation from the applicant as to why, in light of the analysis at (4) and (5) above and your responses in Stage 1 of the application, the applicant considers that it is “just and equitable” for the FCA to grant the validation order sought.

**What MI should I be obtaining, reviewing and providing?**

You should consider carefully what MI you should gather and review in order to form a robust view on consumer harm.

Examples of types of MI include:

* Complaints (number of complaints, themes, upheld rate and referrals to FOS)
* Arrears/default data (overall numbers and percentages of customers falling into arrears/default and at what stage of the loan these happened
* Forbearance (broken down into number of customers who have been offered different forbearance options and the number of customers who have/have not successfully cleared arrears through forbearance options)
* Affordability (overall numbers and percentage of customers approved/rejected)
* Enforcement (overall numbers and percentage of customers enforced against and when these were enforced against)
* Survey responses (unfiltered)

**How should I set out the findings from the consumer contact exercise?**

You must ensure that the results of your consumer contact exercise are set out in a clear and impartial manner.

As part of doing this, you must provide:

* a summary of the consumer contact exercise (see (4) above)
* your detailed analysis of the results of that exercise (see (5) above)
* all of the underlying evidence (see (1) and (2) above).

When setting out the responses you have received from consumers, please do this by way of a simple table, in excel format, with each survey question having its own column and each customer’s response having their own row.

**How should I approach and set out the assessment of harm?**

Ultimately the responsibility for conducting a robust and reliable assessment of actual/potential consumer detriment rests with the applicant firm. The onus is therefore on the applicant to ensure that it presents its assessment in a clear, comprehensive and impartial manner.

We have set out below the steps that we expect applicants to take to ensure they meet that standard.

This report should have separate sections/headings which identify the different types of harm to which consumers might be exposed (see list below). For each type of harm:

* You should outline if you have identified the harm has occurred or could have potentially occurred.
* If you determine the harm has not occurred and is unlikely to occur in the future, you should explain how you have determined this (referring to the customer contact exercise responses and/or your customer journey walkthrough to evidence your reasoning).
* Where you identify the harm has occurred or may occur in the future, you should:
  + explain how you have determined this (referring to the customer contact exercise responses and/or your customer journey walkthrough to evidence your reasoning).
  + which of the affected consumers have suffered this harm or are at risk of doing so (and why)
  + what actions you have undertaken or propose to undertake (if any) to mitigate the harm caused/potentially caused
  + to the extent any harm (or risk of harm) will be left unremedied, why you consider the FCA can nonetheless conclude that the ‘just and equitable’ test for granting the VO is positively satisfied.

The types of harms which that should be addressed in your Consumer Harm Assessment include:

* **Poor customer understanding:** This harm is caused when a customer does not understand the product/service they are buying and the potential consequences for them. It may be caused by:
  + The overall cost and monthly payments of the loan not being explained to the customer prior to entering into the agreement.
  + The duration of the loan not being explained to the customer prior to entering into the agreement.
  + What will happen should they fail to keep up with repayments not being explained to the customer prior to entering into the agreement.
  + Customers not being given adequate time to consider the terms of proposed agreements before entering into them.
  + Failure to issue Credit Agreements and other legal documentation compliant with the CCA.
  + Poor training of sales and/or customer support staff.
* **Unaffordable lending**: This harm is where customers are provided with loans that they cannot afford to repay. It may be caused by:
  + Insufficient credit checks being performed to assess the customer’s creditworthiness prior to entering into the agreement with the customer.
  + Failure to obtain enough information to assess the customers ability to repay the loan. This includes not gathering enough information on the customer’s income and expenditure (or savings/assets where these are being used to repay the loan) and/or not verifying this information to ensure it is accurate.
  + Failure to use data gathered/verified in a suitable way to determine the customer’s ability to repay the loan.
  + Poor training of underwriters.
  + Where affordability assessments are undertaken within the distribution chain, poor oversight of those carrying out the assessments.
* **Mistreatment of borrowers in financial difficulty:** This harm is where customers in financial difficulty are treated poorly. It may be caused by:
  + Inability for customers to notify the lender of any financial difficulty they are experiencing.
  + Customers who fall into arrears being harassed and/or pressured into making a payment.
  + Insufficient or unsuitable forbearance options offered.
  + Customers moved from arrears to default too quicky.
  + Customers threatened with enforcement inappropriately.
  + Customers enforced against after you became aware that the loans were unenforceable.
  + Failure to issue the statutory notices such as Notice of Sums in Arrears and Default Notice compliant with the CCA.
* **Excessive and/or unfair prices/charges:** This harm is where the price of loan (or the product/service purchased with the loan if applicable) does not represent fair value for the customer (or did not result in customers being treated fairly). This harm may be caused by:
  + Excessive interest rates, fees or other charges associated with the loan.
  + The price of the product/service purchased with the loan being excessive.
* **Unsuitable products and/or services:** This harm is where the loan (or the product/service purchased with the loan if applicable) is not fit for purpose and/or does not meet the needs of the customer. This may be caused by:
  + The type of the loan not being suitable for the customer.
  + Commission arrangements incentivising brokers to recommend products/services not in the customer’s interest.
* **Poor treatment of customers (in particular vulnerable customers):** This harm is where the customer is not given the required support they need. This may be caused by:
  + Lack of controls to identify and sufficiently cater for vulnerable consumers.
  + Lack of controls to identify and handle customer complaints.
  + Poor services standards for customers.
* **Other harm:** if you identify other types of actual/potential detriment that have occurred or may occur, you should identify these clearly and explain the evidence on which they are based. An example may be the consumer losing FOS and FSCS rights where unenforceability arises under s26 FSMA or S40, 148 and 149 of CCA.

You should also set out your assessment of the impact on you and affected customers should a VO (i) be granted and (ii) not be granted.

Following your assessment of each of the harms above, you should set out a detailed explanation from of why (in light of the results of your customer contact exercise and your responses in Stage 1 of the application) you consider that it is “just and equitable” for the FCA to grant the validation order sought.

You should also explain:

* How you will assess claims from affected consumers for compensation under Section 28A(2)(a) of FSMA (for post-2014 agreements only), in the period prior to the FCA determining your VO application.
* How you will handle claims to recover money/property transferred under the agreement, in the period prior to the FCA determining your VO application.

**Note: The prevalence of harm will be dependent on the relevant protections to which a customer was entitled to under standards at the relevant time. The consumer harm assessment will therefore require a consideration of not only what harm occurred but when that harm occurred and if the customer did not receive the protections they were entitled to at that time.**

Step 4: Request from FCA for clarification and/or to discuss your findings

After you have submitted your consumer harm report in Step 3, we may ask you to clarify aspects of your Consumer Harm Assessment (and possibly that you talk us through some or all of your assessment at a meeting or on a call).

If a consultant has been used to assist in the customer contact exercise and/or Consumer Harm Assessment, they will be expected to attend any such meeting/call.