

Regulator Assessment: Qualifying Regulatory Provisions

Title of proposal: CP18/35: Rent-to-own: Extended Warranties

Lead regulator: FCA

Date of assessment: 15/11/2018

Commencement date: 22/02/2019

Origin: Domestic

Does this include implementation of a Cutting Red Tape review? No

Which areas of the UK will be affected? Whole of UK

Brief outline of proposed new or amended regulatory activity

We are introducing new rules on the sale of extended warranties by rent-to-own firms. We consulted on these measures in May 2018 (CP 18/12) and announced we would make these rules in November 2018 (CP 18/35).

The rules introduce the following requirements:

- a. A point of sale ban on the sale of extended warranties alongside the sale of the RTO agreement ('the point-of-sale ban'). Firms will be required to allow two full days before consumers can actively opt-in to buy these.
- b. New requirements on RTO firms to provide information to consumers to help them decide whether to buy the extended warranty. This information will include the price in terms of weekly, annual and length of contract cost, as well as how the extended warranty relates to the manufacturer's warranty and any theft and accidental damage insurance.

These rules are intended to address the point of sale advantage held by RTO firms in selling these products which may be of limited value to some consumers, particularly where a manufacturer's warranty is in place. We expect to see a reduction in unnecessary purchases of extended warranties for products subject to rent-to-own agreements and consumers being able to make more informed and less pressured decisions on whether they do want to buy them.

Which type of business will be affected? How many are estimated to be affected?

Firms providing rent-to-own agreements i.e. hire-purchase or conditional sale agreements which provide for repayments to be made at intervals of less than one month, excluding those

for business purposes or motor vehicles. Three firms will be affected – the three largest firms in the RTO market. However, the third largest of these sells a very small number of extended warranties. We have not identified any small firms selling extended warranties.

Price base year	Implementation date	Duration of policy (years)	Business Net Present Value	Net cost to business (EANDCB)	BIT score
2018	2019	10	-51.5	6.0	29.9

Please set out the impact to business clearly with a breakdown of costs and benefits

To estimate the costs of these rule changes we collected cost and sales information from firms. We updated these costs following additional information we received during our consultation.

Our proposals entail costs in terms of:

Transitional costs: One-off costs to RTO firms of compliance with new requirements including provision of additional information

These will be broken into the following:

Updating systems - £280,000-£300,000

The most significant of these costs will be setting up a centralised sales team and amending IT systems to enable post-sale addition of extended warranties to contracts. This is estimated at £260K

We also require firms to provide key information about the costs, benefits and limitations of the extended warranty product and its interaction with the manufacturer's warranty and any insurance products sold alongside the RTO agreement. Surveyed firms indicate that IT changes to incorporate the need to check coverage and revisions to disclosure and advertising materials sum up to 30 to 50 days. Standard FCA salary assumptions on IT costs for small firms, including overheads, includes £266 daily costs to small firms, and £346 for medium firms. Considering that the market consists of small to medium firms, we assume £306 average costs.

The combined impact on the small number of firms operating in the market should then be in the £280,000 – £300,000 range

Training - £0.6m-£0.9m

RTO firms will need to train employees on how to process the offering of extended warranties to customers, both in terms of information provided and how to engage outside the point of sale. We estimate that 1,100 RTO staff will require training for 1 to 4.5 days. Combining opportunity costs of staff time and internal providers of training, payments to external providers, and costs of preparing materials, we estimate this cost to be £0.6m to 0.9m.

Familiarisation – Minimal¹

Minimal costs associated with familiarisation with new policy documentation.

Reviewing and updating information to consumers - £25,000-£50,000

RTO firms will need to review and update information they provide to consumers following our interventions. The time spent on these tasks varies depending on existing practices and the

¹ Please see page 66 of CP18/12 for further information

size of the firms involved. Indications from survey outcomes on the one-off impact of time to prepare disclosures point to 30 to 70 days, mostly spent by managers and directors with salaries. We estimate one-off costs to the industry to be in the £25,000-£50,000 range.

Total one-off costs: £0.9m - £1.3m

Ongoing costs

Reduction in profits from extended warranties sales

Firms may see a reduction in profits, following a reduction in sales of warranties, when consumers have more time to consider whether to buy them as a separate decision from the purchase of the underlying products. As the impact of a point of sale ban depends on behavioural reactions, the magnitude is inherently subject to uncertainty. We have therefore applied ranges to the impacts estimated and assume a 10% to 20% decrease in the number of consumers purchasing extended warranties, and an equivalent reduction in the value of those sales from RTO firms.

Accounting data show total revenues from sales of extended warranties around £40m-£45m per year, and costs of service cover around £10m-£15m, indicating profits in the £25m-£35m range. If revenues decrease by 10% to 20%², and assuming the costs of cover declines proportionately to revenue, RTO firms suffer a reduction in profits between **£2.5m and £8m per annum**.

Selling extended warranties after the point-of-sale

Some firms will need a new dedicated sales team to follow up on agreements with consumers, as the warranty sale can only be done after two clear days. This would be most likely to only apply to those consumers who said they were interested at the point of sale. Only around 60% -70% of consumers took out these products, so it is unlikely that the firm would need to follow up on every consumer. There will also be some time cost savings from in-store staff, as they cannot complete the sale of extended warranties at the point when consumers buy the RTO product and these staff can undertake other activities. This cost saving should be offset against any increased costs from selling extended warranties after the point of sale. We also expect firms to develop low cost ways to finalise sales using technology. For these reasons, we have assumed that the additional ongoing costs of selling extended warranties are **£1.3m per annum**. We believe this is the upper limit of the potential costs.

Please provide any additional information (if required) that may assist the RPC to validate the BIT Score.

High-cost Credit Review: consultation on rent-to-own, home-collected credit, catalogue credit and store cards, and alternatives to high-cost credit; and discussion on rent-to-own pricing (<https://www.fca.org.uk/publication/consultation/cp18-12.pdf>) - see chapter 2

CP18/35: Rent-to-own and alternatives to high-cost credit – feedback on CP18/12 and consultation on a price cap (<https://www.fca.org.uk/publication/consultation/cp18-35.pdf>) - see chapter 5
<https://www.fca.org.uk/publication/policy/ps19-11.pdf>

² This range was informed by our findings in 'An evaluation of our guaranteed asset protection insurance intervention' (see <https://www.fca.org.uk/publications/corporate-documents/evaluation-guaranteed-asset-protection-insurance-intervention>). Guaranteed Asset Protection insurance is a product with similar features to RTO extended warranties. The evaluation assessed the impact of a similar intervention to those imposed through this policy.