Loan Remediation

The complexities of redress schemes
for secured and unsecured lenders

May 2017

With the regulation of consumer credit firms now the responsibility of the FCA and increased expectations and scrutiny being placed on the mortgage sector, loan remediation exercises have become commonplace in recent years.

In the secured lending space, capitalisation of arrears, payment allocation, early redemption charges and mis-calculation of interest are just some of the issues we have encountered. In the consumer credit sector, we have seen overcharged fees, irresponsible lending and unenforceability issues affecting firms. An additional common theme across all lenders is that loan administration systems have not always treated customers in line with products' terms and conditions.

Loan remediation is often more challenging than other forms of remediation due to the potential need for account reconstitution, which is often the only way to ensure that all affected customers are identified and offered fair redress. Even for superficially basic breaches, these exercises can be fraught with complexity and require lenders to demonstrate a deep understanding of the workings of their products and systems, often going back many years for long-term products.

Loans typically involve many interdependent transactions over long periods of time, which are frequently administered across many sub-accounts using complex payment waterfalls. This means that even a single breach such as an interest calculation error might result in inaccurate repayments, overstated or understated arrears, inappropriately applied fees and charges, unfounded litigation activity and so on.

To tackle this complexity, we believe that the following steps are critical to making a success of loan remediation:

- **Customer journey:** An early and sufficiently detailed exercise to assess how the issue has affected a representative sample of individual accounts is essential in planning your remediation project. This will help to frame many aspects of the project including data validation, redress methodology, consequential loss, regulatory liaison and customer contact.
- **Limit future detriment:** Where accounts have potentially been affected, consider putting any fees, charges and/or litigation activity on hold while remediation takes place. If the system or process underlying the issue can be fixed prior to redress, this should be undertaken as soon as possible to limit future detriment.
- **Pilot:** Whether you are testing your full end-to-end remediation process or looking for a high-level view of the overall impact for provisioning, a pilot exercise is highly valuable. Being able to see the tangible effects of remediation on an account can help to flush out any issues which may not have been anticipated when drafting your redress methodology or constructing your redress calculator.

The key questions that you may need to consider when embarking on a remediation exercise include:

Data

- Can data from legacy systems be easily acquired and trusted? How do previous system migrations affect the data? What steps will you need to take to validate this data?
- How well are historical manual adjustments recorded? Is their rationale clear and documented?
- Can the impacted population be easily identified within the administration system?
- How can you choose a pilot sample to best flush out any issues?

Calculation methodology

- How far back in time should you go to calculate redress? Can the origin of the issue be easily identified?
- Might the issue have had a knock-on impact on:
  - the application of historical payment allocation waterfalls?
  - the application of historical arrears-related fees and charges?
  - the enforceability of the loan contract (eg CCA-regulated loans)?
  - the date on which the loan was settled?
  - the level of historical redemption charges and early settlement calculations?
- How might redressing this issue interact or overlap with other current or past redress issues?
- Can you assess the potential complexity of the redress calculation based on what you know about the affected population (eg overstatements of monthly instalments are likely to have a greater impact on loan books with heavy arrears)?
- Has the impact of any recent FOS adjudications been considered in determining how to calculate redress? Is an appropriate level of compensatory interest being applied?
- How will you determine any de minimis level for redress? How will this be affected by regulatory expectations and tracing costs?
- How will you apply redress to customers with written-off or shortfall balances?
- Have the trade-offs between prudence and accuracy been considered and applied consistently across the methodology? Is a two-speed approach prioritising certain groups of accounts and highlighting certain cases for manual review more efficient?
- Will the complexity of redress calculation for certain cohorts affect the order in which customers are redressed?
- Can redress be offset for customers with multiple affected accounts?
- When will the redress be administered in the payment cycle?
- How will you ensure that learnings from any pilot are appropriately implemented when you move to full execution?

Consequential loss

- Has reasonable consideration been given to consequential loss beyond any redress calculated through account reconstitution?
- Has the issue caused any credit reference agency submissions to be misstated?
- Have litigation decisions that were made under false pretences been revised?
- Is any redress for Distress and Inconvenience required?
- Have other consequential losses been considered, for example the cost of borrowing elsewhere or the costs of moving house?
- Have you considered wider personal impact on customers?
- How will you deal with the knock on impact on tax liabilities and benefit entitlement?

Customer contact

- Can customers with closed accounts be traced? At what cost?
- Are sufficient call centre staff available and trained to handle complaints and clearly explain redress to customers?
- How will the redress be communicated to customers with multiple accounts or accounts with multiple issues?
- What level of detail will communications with customers go into?
- What and when does the regulator expect you to communicate to customers?
- How proactive will you be in ensuring customers understand the issue, particularly for customers in vulnerable circumstances?
- What will you do if you get no response?

How we can help

Grant Thornton has extensive experience of assisting lenders with all aspects of loan remediation projects and is uniquely placed to advise on the challenges encountered and the critical factors for success.

Our team of experts in regulatory compliance, complex redress calculation modelling, project management, and assurance can provide independent challenge and oversight to your loan remediation project, helping you to make sure that the project is delivered efficiently to regulatory deadlines and standards and to ensure that customers are treated fairly.

We have assisted firms with loan remediation exercises ranging from populations of only a few hundred customers to large-scale projects that involve populations of hundreds of thousands of customers, taking years, rather than months to complete.

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