THE NEED FOR EFFECTIVE PROMPT PAYMENT SOLUTIONS IN UK SUBPRIME VEHICLE FINANCE

A PERSPECTIVE FOR LENDERS

A White Paper from Global Telemetrics Ltd.

Contents

About this white paper

This paper outlines how UK vehicle finance companies can widen their market; whilst at the same time reduce the costs of servicing delinquent payers with the adoption of new payment protection technologies and collection strategies. It provides a guide to understanding the opportunity and what qualities to look for in a solution provider.

Who should read it

CFOs in UK vehicle finance companies and operators of dealer franchise networks wanting to convert the top layer of sub-prime applicants into sales without increasing their exposure to added risk.

The problem in the UK

More and more consumers want to buy used cars on finance but there are fewer and fewer lenders able to take advantage of the opportunity. The used car market is fundamental to the UK's economic recovery if only lenders could find a way to reduce their risk and lend more. This comes at a time when the consumer credit market contributes £260bn to the UK economy of which about £30 billion is from used car sales.

Growth is in the sub £10k Used Car

There is significant latent profit to be squeezed from sub-prime vehicle lending in the UK with the adoption of new payment protection technologies which greatly reduce risk and radically alter payment behaviours.

In spite of the growth in new car registrations, the market for used car credit is rising. At the time of writing (2013) the number of used cars purchased with car finance is growing consistently every month, with over 70,000 used cars financed in January 2013 (a 6% increase on the previous year). Similar growth was reported every month in the previous quarter too.[1]

Mintel's 2013 report shows the relative importance of used cars over new cars, revealing that 40% of car owners possess a second-hand car compared to 27% who purchased their last car from new. Strikingly, two-thirds of cars owned currently were purchased for less than £10,000 (Car Purchasing Process - UK - April 2013, by Mintel).

It's not just the sub-prime lending specialists who can capitalise on this growing demand for car credit in the UK: **with the right risk reduction strategies mainstream lenders can benefit too.**

Growth is in sub-prime

Yet at the same time, the base of subprime borrowers in the UK is expanding, with more and more applicants showing poorer credit scores.

Car purchasers, who were once in the mainstream, are now increasingly turning out poor credit scores. They can only find loans from sub-prime specialists and fewer lenders want to take on the risk of sub-prime.

The sub-prime sector is bulging both upward as well as downward and there is a significant opportunity for enlightened lenders to mine the top layer of sub-prime without lowering risks.

Understandably, recession-bashed CFOs of vehicle finance companies have been risk averse, having faced shortages of credit supply, reticent consumers and riskier applicants. Added to this, sub-prime lending comes with very high delinquency rates, late payments, costly repossessions and expensive skips.

The climate is changing

Credit availability is at its highest level in five and a half years[2]. And it needs to find a good home. Deloitte's *CFO Survey 2013*3 shows a sharp fall in uncertainty and rising optimism and risk appetite among UK corporates. Perceptions of economic and financial uncertainty have fallen to the lowest level since early 2010.

There is a valid case that investors should look to the UK sub-prime vehicle credit market for good returns, now that payment delinquencies can be better controlled, collection costs reduced and assets secured.

New prompt payment technologies are unlocking hitherto untapped potential and changing the game. Consumer payment behaviour is being influenced remotely and vehicles securely tracked. Well documented in USA and Canada, such technologies are only just surfacing in Europe. However, there's an added barrier to adoption in the UK as technologies need to comply with the stringent consumer credit regulations, satisfy the OFT and be desirable to end-user drivers.

Payment Protection Technologies in the UK

Payment protection technologies are relatively new in the UK. Typically they range from simple pre-programmed stand-alone starter interrupt devices (SIDs), to more sophisticated command and control GPS systems integrated with lenders' and dealers' back offices, designed to manage driver needs as well as lenders' interests.

Early adopters caught the imagination with crude system

The ‘stand-alone’ prompt payment solution, initially the only technology of its type available, requires the driver/borrower to enter a receipt code each month into a visible dash mounted keypad which prevents the device from immobilising the vehicle. The borrower is supplied the code from the lender after having made the payment. If the driver fails to enter the code into the dash system, they are given a series of on-board visual alerts, typically a three day countdown clock, prior to the vehicle being automatically immobilised. This type of system has no GPS nor data connection and once fitted has no flexibility to be re-configured. It has limitations, not only for the customer with a stigma attached to the visible dash mounted device, but it does not meet UK credit regulations[4]. Lenders need to be certain that any such solution fully conforms to UK consumer credit legislation which in this context requires a due process of notification.

As the initial market entrant in the UK, the ‘stand-alone’ prompt payment solution has gained some traction in the industry which is beginning to recognise the enormous potential benefits of changing the dynamics of the collection process in this way.

New innovative end-to-end solutions

The next generation solutions utilise ‘connected’ on-board tracking devices. These are GPS immobilisers securely fitted within the vehicle. When a driver defaults on their payment, after appropriate legal notice to the customer, the technology can remotely immobilise the vehicle. Using smart technology, a good ‘next gen’ solution can issue alerts when they detect the device is being tampered with, or if the vehicle is moving with low or no power (i.e. indicating it is being towed). A range of GPS devices is available in the UK, but lenders looking for a supplier should look at providers who control the whole ‘end to end solution’, from managing their own ‘walled garden’ secure wireless network to their own accredited fitters and managing the default notice issuance and notifications. By giving the responsibility for the whole process to a specialist provider, such as Global Telemetrics with their end-to-end VTSiM® solution, the lender is less exposed to any liability.

A more holistic dedicated solution combines GPS tracking features with a CRM (customer relationship management) system to result in added benefits to both lender and driver.

(Find out about VTSiM® at http://vtsim.globaltelemetrics.eu/ or call 0800 279 5702.)

Lender, dealer, driver: a new relationship

For lenders to succeed in reducing their exposure to defaulters, a new symbiotic partnership needs to form between lender, dealer and borrower.

Do petrol retailers suffer delinquent payments from their customers? No! If the consumer wants the use of their vehicle, they need fuel and they need to pay for it or no fuel, no car. Car finance can now have the same binary dynamic. If the consumer wants the use of their vehicle, they need to keep up the payments or their vehicle will cease to operate. No payment, no car.

With the threat of immobilisation, making the monthly car loan payment now becomes as necessary as buying the fuel.

Whereas collection agencies usually have to track down the defaulter, initiate the phone calls etc, the onus now changes and the borrower is contacting the collection agent. This saves significant costs.

In time, intelligent payment protection systems may become standard and the opportunity to ‘duck and dive’ to avoid payment becomes a thing of the past. Why should lenders tolerate it when they don’t need to? What is evident is that it is very rare that the ultimate step of immobilisation occurs.

Drivers become conditioned to pay on time and their behaviour becomes automatic.

Quantifying the benefit for collections

Historically, very few finance companies have used payment protection technologies. This low adoption is largely due to lack of information about what is possible with new developments in technology and emerging business models.

A recent survey of lenders in Canada demonstrated how deployment of GPS style payment protection technology can have game-changing impacts on the bottom line.

The survey found 27.21% of subprime loans are delinquent. However, where payment protection technology is used there was a 21% improvement in delinquent accounts. They survey found only 17% of subprime car loan companies use payment protection technology to accompany their collection processes. Part of the reason for this narrow adoption rate was attributed to a lack of education in the marketplace on the range of features of newer systems. The 17% that adopted the new technology however saw a significant improvement in consumer payments and collection efficiency.
A recent report by Canada's National Independent Automobile Dealers Association on the Used Car Industry indicated that of the car loan lending firms surveyed, 27.21% of subprime loans are delinquent. Overlay the industry average with the statistics based on the deployment of 72,000 devices with a midsized subprime lender over a 44 month period the areas of profit improvement are significant as shown in Table 1.

Collection Areas	Without devices	With devices	% Improvement
Current Accounts	**72.7 %**	**78.6 %.**	**+8.0 %**
Delinquent Accounts	**27.2 %**	**21.3 %**	**-21.0 %**
Late payment	9.2%	6.2 %	-33.0 %
Repossession	15.0 %	12.0 %	-13.0 %
Skips	3.0 %	2.0 %	-33.0 %
Seizure costs	$450/vehicle	$150/vehicle	-66.0 %
Agent to Accounts Ratio	1:300	1:235	+8.0%

Increase in on time payments
The mid-sized lender experienced an8% improvement in on time payments to improve current accounts, 13% reduction in repossessions and an astonishing 33% in skips. Like their response to the ding of the low fuel indicator, many consumers respond positively to the warning beep from the payment protection device and would call their collection agent to arrange payment.

Source: IMETRIK.

For UK lenders wanting a belt and braces solution, they need to triangulate three key criteria: security, legal compliance and responsibility for the whole process.

Choosing your technology solution has distinct legal ramifications

Lenders need to be sure that the solution they are using, whether remote immobilisation or pre-programmed starter-interrupt, not only produces prompt payments, but does so without falling foul of the Consumer Credit Act 1974 nor of the Unfair Contract Terms Act 1977.

As a lender considering the use of payment protection technology, you need to be sure that your provider can provide cast iron compliance to the Consumer Credit Act (CCA) and not jeopardise your position with the Office of Fair Trading.

In fact, given the nature of the CCA, it would be sensible to ask any provider for evidence of their compliance, and whether it meets the essential requirements as interpreted by David Waters QC in his opinion to Global Telemetrics 28th of January 2013.

Immobilisation of a car is a serious act with drastic consequences for the customer and amounts to a restriction of the customer's right to possess the car. As such, a creditor is bound to issue a default notice before threatening immobilisation.

Does your solution allow for the correct and appropriate issuance of a default notice?

Immobilisation is triggered by the customer failing to pay on time, and being in breach of the agreement. Whilst a breach alone may not require issuing a notice, the restriction on the customer's right to possess the car would. A creditor does not become entitled to restrict this right *until after a default notice is issued, and the notice period (14 days) has expired*. Merely activating a countdown clock to alert the driver is not the same thing at all. **In fact, by immobilising a vehicle in this way the creditor effectively risks committing a 'trespass'.**

"But we've got it covered in our terms and conditions in the consumer agreement."
This is not sufficient to comply with the CCA requirements.

"The device serves notice with its on-board dash countdown alert system".
This is not a default notice.

"We will send the customer a default notice before the countdown clock activates immobilisation". This would require a notice being issued in sufficient time for the 14 days to expire before the immobilisation takes effect. Where the device is pre-programmed to immobilise unless a code is entered, this does not seem practical. A notice would have to be served every month in anticipation of the customer defaulting… it gets messy!

Satisfying security requirements

Lenders reviewing which technology to use should consider solutions with robust security standards.

As a minimum, in order to be effective in the recovery of a vehicle, a solution should be accredited to Thatcham Category 5 standards ('CAT5'). This includes the use of remote immobilisation (interrupter) in the event of a theft with 'Police Authority'. Having CAT5 as a minimum standard will ensure the very best quality in product, service, criteria and approvals, such as:

- BS7858
- ISO 9000
- VCA compliance

All CAT5 Systems Operating Centres (SOCs) are required to have secure operating centres (a bunker type control room) providing the highest level of security, adding resilience to the tracking and monitoring service.

Future applications of the technology

'Next gen' GPS trackers will have benefits far beyond asset tracking.

Dealer benefits

Dealers can currently benefit from selling more vehicles as they turn away fewer buyers who fail on credit checks. But looking ahead, they can develop a longer term relationship with their customer. They will be able to track their customers' actual mileage and advise them when their tyres need changing, or when their service is due. This advice will be delivered automatically by a mobile app branded with the dealer's livery creating unprecedented advertising and marketing opportunities. At the point of purchase, the dealer can input MOT, insurance and tax deadlines, thus providing a special dependency for the customer.

Driver benefits

For the driver, a mobile app connected to their vehicle's tracker will be invaluable for 'managing' their vehicle. In addition to the current stolen vehicle recovery service it will have mileage-based servicing and tyre renewal alerts; warn them of MOT, insurance and vehicle tax deadlines; and hold their insurance details in case of an accident. This will be a 'done for you' service, with the data set up by the dealer when they purchase the vehicle. With compatible insurance providers, they can (literally) have 'pay as you go' motor insurance. The same app could manage their mileage expenses and sync with a web portal for ease of use.

Lender benefits

Lenders too can develop a deeper relationship with the finance buyer beyond the immediate transaction and leverage this to cross sell and upsell other finance products.

Conclusion: what to look for in a technology solution

Far sighted lenders and dealers will be wise to adopt a payment protection system which is both legally and technically future-proof and which can deliver a range of added value services to enhance their customer offerings and enable them to build long term relationships with their customers.

About Global Telemetrics

Global Telemetrics is the systems platform behind award winning Midlands-based SmartTrack, which designs and manufactures a range of advanced UK built vehicle tracking systems. Established in 2006, the business has grown rapidly with annual sales across Europe in excess of £2m. It specialises in providing holistic, dedicated end-to-end solutions and systems, highly secure and confidential, to service specific industry needs, such as VTSiM® for Finance, as well as products for the Stolen Vehicle and Fleet Management sectors.

The company is committed to developing advanced technologies, innovation and customer service in all its products as evidenced in its 21 coveted Mobile Electronics News Awards over the last 7 years. Global Telemetrics has invested in flexible, future-proof back office technology, such as Salesforce CRM (which it integrates with the DVLA portal) and an adaptive Avaya CTI phone system, to enable Global Telemetrics to provide scalable and enhanced customer service provision and to operate in new overseas markets many of which require multilingual SMS/voice.

All marketing and sales material is designed in-house by its own graphic designers/editors.

SmarTrack's latest compact web based product has been designed around the Thatcham TQA-CAT5 leisure criteria (improved battery life technology) making the device unique. All SmarTrack products are recognised by major insurance companies and have saved several million pounds on 'Total Loss' by theft.

SmarTrack is accredited to ISO9001-2008 and Thatcham Security standards and has passed the SGS Class One VCA-EMC testing procedure gaining full E-mark[1] Conformity of Production status.

All SmarTrack secure control room staff are Police liaison trained and BS7858 approved.

[1] An E-mark signifies that an automotive product complies both with the international UNECE regulations and the European vehicle legislation.

Further information

To find out how the VTSiM® solution can help your business contact Jim Mather below.

Global Telemetrics Limited
Telemetrics House
35 London Road
Coalville
Leicestershire LE67 3JB

e info@globaltelemetrics.eu
w www.globaltelemetrics.eu
t 0845 833 6971 or International +44 (0)1530 275920
All calls to the Global Telemetrics switchboard are recorded for training and monitoring purposes

Registered office: 63 Fosse Way, Syston, Leicestershire, LE7 1NF. Company No 6965076

VTSiM® is a registered trade mark of Global Telemetrics Ltd

ENDNOTES:

[1] Finance and Leasing Association as reported in Motor Trade Insight http://motortradesinsight.co.uk/article_page.asp?id=199
[2] The Deloitte CFO Survey Q1 2013: "CFOs say credit is more available and cheaper than at any time since the survey started in September 2007"
[3] The Deloitte CFO Survey Q1 2013 http://www.deloitte.com/view/en_GB/uk/research-and-intelligence/deloitte-research-uk/the-deloitte-cfo-survey/index.htm
[4] David Waters QC Opinion given to Global Telemetrics 28th of January 2013