Personal Loans Market in Poland

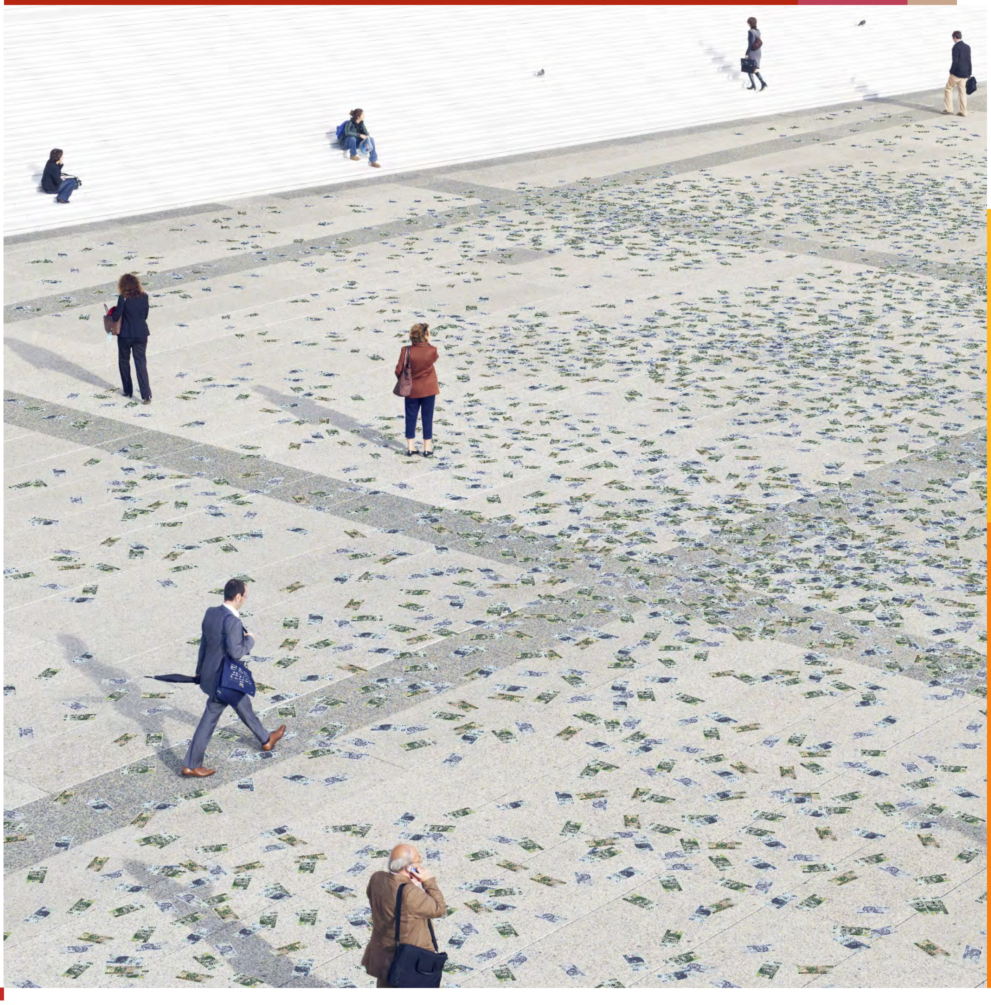


Table of Contents

Foreword by Professor Witold M. Orłowski, PwC's Chief Economic Advisor in Poland 04

1. Introduction 06

1.1. Background 06

1.2. Objective scope of the report 08

2. Market and its participants 11

2.1. Personal loans market in Poland 11

2.2. Personal loans market: customer profile 14

2.3. Business model of a personal loan company 19

2.4. Segmentation of personal loan companies 20

2.5. Amount and structure of loan costs 25

3. Consumer practices 30

3.1. Practices of personal loan companies with regard to customers based on the Mystery Shopper study 30

3.2. Company's responsibility: formalities, processes and procedures 32

3.3. Customer's responsibility: awareness and knowledge 36

3.4. Service quality: providing information about the product and customer service standards 38

4. Analysis of the systems regulating operation of personal loan companies in Poland and abroad: best practices 44

4.1. Licencing and supervision 44

4.2. Annual Percentage Rate limits 48

4.3. Regulations concerning liability to consumers 50

4.4. Debt recovery 52

4.5. Withdrawal from the agreement 55

5. Summary: key findings for the personal loans market in Poland 56

6. Glossary of terms 60

Foreword
– by Professor Witold M. Orłowski, PwC's Chief Economic Advisor in Poland

It is with pleasure that we present the readers with this report on the activities of personal loan companies in Poland. Despite the mixed feelings of the public, the sector is an important participant of Poland's financial market. It provides access to financial services to those consumers that for various reasons cannot take advantage of banking services because of their limitations or lack of appropriate products.

High costs of loans provided by the personal lending companies are often the reason for their negative public perception. The reasons for applying such costs are usually the same reasons for which the customers of personal lenders are overlooked by the banking sector. The borrowed amounts are usually small, which translates into relatively high overhead costs, and the customer group is often associated with higher risk. Since banks have to protect the value of deposits entrusted to them by customers, they cannot engage themselves in such activities. On the other hand, the personal loan companies described in this report risk the funds of their shareholders, who are conscious of the higher risk as it is an imminent part of their business model.

In this study, we conduct a multifaceted analysis of the personal loan companies operating in Poland. The objective of the analysis is, firstly, to describe the operations of the sector with as much precision as possible; secondly, to identify potential effects of various regulatory measures. Thus, the analytical part of the report contains a description of the market in which personal lenders operate, as well as a description of regulatory solutions applied in other countries and planned in Poland.

As part of the description of the market, we also included a description of the customers of personal lenders as well as their current business models; furthermore, thanks to the Mystery Shopper study conducted for the purpose of this report, it was possible to describe the real interactions between the lenders and their customers. The description of regulatory measures includes not only the information about the existing and planned measures, but also the opinions of the interested parties on the planned amendments.

The analysis led to several important conclusions:

- There are three segments of companies operating in the personal loans market, each representing companies of a different business model determining the cost and availability of the loan to the customer and therefore the product and services offered to the market.
- Most of the companies covered by the report strive to provide its customers with fair and clear information on the costs and other terms and conditions of the loans; this however does not mean that all customers are able to fully understand the meaning of the signed contractual provisions.
- Any potential changes in regulations should take into account the aforementioned conclusions to ensure that the amended regulations protect the rights of customers and fair competition on the one hand, while avoiding liquidation of the market on the other.
- Besides the potential changes in legislation, self-regulation of personal loan companies may also play an important part in the personal loan market, with such measures as establishing a code of conduct in dealing with the customer to be adopted by the whole sector, or education campaigns among the customers.

We hope that the results of the analysis presented in this report, as well as the conclusions and recommendations, will make a valid contribution to the current debate about the best solutions regulating personal lenders' operations in Poland.

1. Introduction

1.1. Background

Background and context of the report

Operations of personal loan agencies and other entities operating – legally or illegally – in the Polish financial market has been a popular topic with media and government authorities since the collapse of the infamous Amber Gold. On the other hand, another hot topic in public debate is households' difficulties in obtaining financing due to the global financial crisis.

There have been a lot of publications and reports issued recently by public authorities and NGOs. However, the description of the market contained in such publications usually focuses on a selected thematic aspect, such as advertising practices, or selected market participants and segments. The most often raised subjects related to the industry include statutory limits on interest rates, client profile and their financial situation, methods and costs of debt collection, charges applied by personal loan companies, as well as violation of other provisions or good practice in the lender-borrower relationship.

The purpose of this report is to contribute to the public debate in Poland concerning the future of the personal loan companies. It also aims at providing explanations and enriching the discussion continued in EU countries in the area of regulation of activities of personal loan companies. The Polish government, market regulation authorities and other stakeholders active in the broadly understood financial market have been holding for over a year a discussion about new regulations connected with activities of companies who lend money using their own funds. Such companies are not covered by the comprehensive system of regulations and prudential supervision exercised by Komisja Nadzoru Finansowego, the Polish Financial Supervision Authority (hereinafter "FSA"), such as banks, payment institutions or społeczne kasy oszczędnościowo-kredytowe (social credit unions, hereinafter "SKOKs"). On the other hand, they are subject to regulations issued by consumer protection authorities such as Urząd Ochrony Konkurencji i Konsumentów (Consumer and Competition Protection Authority), the bodies protecting personal data such as Generalny Inspektor Ochrony Danych Osobowych (General Inspector for Personal Data Protection) and institutions supervising implementation of regulations on preventing money laundering and terrorism financing, such as Generalny Inspektor Informacji Finansowej (General Inspector for Financial Information).

Thus, the objective of this report is to describe the sector of personal loans and provide to the reader:

- A description and context of operation of the personal loan market;
- A description of the main segments of entities operating in the market and pointing out their chief characteristics;
- A profile of the average customer of a personal loan company;
- Selected aspects of the lending practices applied by companies from selected segments with reference to current regulations and communications directed by such companies to the market;
- Results of the analysis of selected aspects of operations of the industry in Poland and other selected countries;
- Results of the analysis of the key areas of potential regulations for the personal loan sector in Poland.

The thematic scope of the report as well as the adopted approach enables us to present to the key readers of this publication a clear picture of the personal loan market and possible areas requiring regulation or supervision. The report has been developed for representatives of public authorities (government, supervisory authorities such as FSA, Consumer and Competition Protection Authority, and the National Bank of Poland as an institution responsible for financial stability) which make decisions about the future of that part of the financial market, as well as for other entities, such as commercial chambers or business associations. We do hope that this document will contribute to the discussions around the currently developed regulatory measures, which will allow the companies in the industry to operate in a competitive manner, while ensuring protection to their customers and promoting stability of the financial system as well as minimising financial exclusion in the society over a long term perspective.

Report objectives

To ensure reliability of the presented data and analyses, certain rules were adopted during development of this report. The aim was to ensure that the report is:

- Independent – the report is prepared by an entity independent of the personal loans market, that is PwC;
- Impartial – the report presents the situation in the market without evaluating or judging any of the market participants;
- Constructive – the study identifies significant thematic areas which may be valuable from the point of view of potential regulatory solutions in the personal loans sector in Poland.

Certain assumptions used for the purpose of this report were consulted with selected stakeholders concerned with operation of the personal loan market and its future regulation. Nevertheless, the final form of the report is a result of an independent decision made by PwC, and the purpose of consultations was to verify whether the report covers major business, social and regulatory issues which are important from the stakeholder's point of view. When preparing the report, PwC used a number of market research techniques, which are discussed in detail in subsequent sections. For the purpose of the report, PwC analysed the publicly available data, conducted an independent study of market practices used by companies from the personal loans sector using the Mystery Shopper technique, conducted a survey among personal loan companies and performed qualitative and quantitative analyses on that basis, which contributed to the development of individual parts of the report.

To maintain a broad and balanced perspective on the subject of this report, PwC designed and conducted the following studies for the purpose of this report:

- Qualitative and quantitative study of the Polish personal loan sector using a specially designed survey addressed to tens of companies representing an important part of the personal loan market and operating in three segments discussed in the report (see Chapter 2.4). PwC received a dozen or so responses, including 7 completed questionnaires (one questionnaire was completed by an industry organisation on behalf of several companies);
- Qualitative and quantitative survey addressed to experts from PwC's network of companies, concerning, among other things, selected aspects of regulations applying to personal loan companies in selected countries (see Chapter 4);
- Mystery Shopper study conducted by a third party company for two personal lender profiles in three market segments defined in the report. The study consisted in applying for a personal loan by individuals, reviewing the loan process and eventually withdrawing from the loan agreement (see Chapter 3). This enabled us to make a detailed analysis of the process in such areas as communication concerning the offer, terms and conditions of the loan, and the current law.

The subsequent parts of the introduction to the report focus on a description of the market and market characteristics.

1.2. Objective scope of the report

Lack of one common definition of the non-banking financial services market often leads to confusion and incorrect classification of personal lenders. In public debate, personal loan companies are often classified under the same category of enterprises as the so-called shadow banks. On the other hand, lack of precise and accepted term of a shadow bank in the market and in the literature on the subject results in misinterpretations of how the lending companies operate. Therefore, for the purpose of further analysis, a detailed definition of the personal loans market against a broad category of financial services is especially important.

The problem becomes more complex when we examine international regulations which apply to the personal loans market. The term "shadow banking", which is often used in discussions concerning the non-regulated segment of personal loan companies, or more broadly, the non-regulated financial market, means different things for different countries. ("shadow banking" is often translated into Polish as *bankowość równoległa*). For instance, in the Anglo-Saxon culture, and to a large extent in European Commission's publications (Green Paper on Shadow Banking[1]), the segment is defined as "the system of credit intermediation" that involves entities and activities outside the regular banking system (including credit intermediaries, hedge funds or SPVs). In countries with developed financial markets (especially Anglo-Saxon), the term very rarely applies to companies from the non-banking financial services market, limited to non-regulated companies providing loans to private individuals.

In the public debate in Poland, the terms "shadow banking", *bankowość równoległa* and *parabanki* are used as synonyms, often in an inconsistent and imprecise manner. Thus, "shadow banking" is sometimes used to refer to non-regulated entities (but often with high internal credit standards) operating in Poland and being members of international banking groups. Such companies – which provide loans using funds provided by the international parent rather than deposits obtained from Polish customers – were often the target of critical comments (and actions) of some institutions, being referred to as "grey banking area companies" or "*shadow banks*", allegedly pursuing regulatory arbitrage[2]. These labels are also used with regard to non-banking lenders, which are classified as shadow banks, or *parabanki*. The definitions of both terms in the public debate are vague and have generally negative connotations.

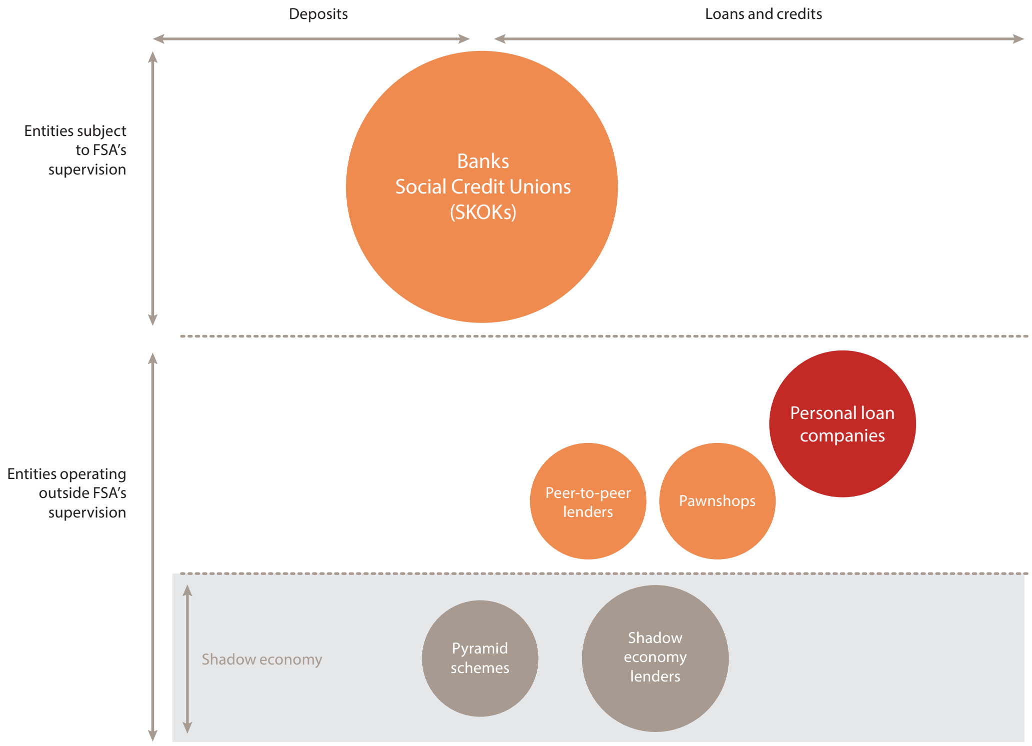
According to the European Commission's Green Paper on Shadow Banking, the term "shadow banking" also refers to (beside other entities such as hedge funds, SPVs etc.) entities which provide loans or credits and operate outside the regulated banking sector, which in practice means that the broadly understood shadow banking can also refer to personal loan companies.

This report focuses on entities providing personal loans, which operate as partnerships or companies, funded under the provisions of the Commercial Companies Code, and which do not finance their operations through customer deposits.

1. http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2012:0102:FIN:PL:PDF

2. The arguments which are often used in public debate are somewhat logically contradictory – entities referred to as shadow banks did not circumvent banking regulations as they did not perform activities that were restricted to banks operating on the basis of a banking licence; therefore, their activities did not violate the provisions of the Banking Act (they did not collect deposits).

Chart 1. Financial services for private individuals in Poland



Source: Own work, PwC

Chart 1 illustrates the objective scope of the report from the regulatory point of view. Activities in the sector of financial services addressed to consumers were divided into two main segments: deposit taking and extending loans and credits using own funds.

"Banking activities" are understood as performing banking operations which may expose to risks the funds collected from broadly understood customers[3], entrusted to the bank on a repayable basis, which implicates the need for strict regulation and supervision of such activities. In the current legal circumstances, the categories of entities subject to FSA's supervision include banks, SKOKs and cooperative banks as well as capital, insurance and pension market operators and companies providing payment services.

Entities that provide loans outside FSA's supervision include pawnshops, peer-to-peer lenders and personal loan companies, which are the main focus of interest of this report.

Due to significant differences between both the pawnshop and peer-to-peer lender business models and the loan provider model (the former provides a loan against a pledge, while the latter relies on loans granted between peers without any intermediaries), both these categories were excluded from further analysis.

3. According to the definition included in Article 4 of the Regulation of the European Parliament on Capital Requirements (CRR), which shall apply to all countries from the European Economic Area, "credit institution" is "an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account".

4. The Consumer Credit Directive refers to assessing the credit status of a consumer, while the Polish transposition of the directive introduced the concept of assessing the customer's credit risk.

The resulting scope of the study allows for focusing on entities that conduct legitimate activities consisting in provision of consumer loans, regulated by the civil law, including in particular the Act on Consumer Credit, but not regulated by FSA or the Banking Act.

In addition, the scope of this analysis includes companies offering loans that are used by consumers to meet their current needs or cover one-off expenses. Such instruments are usually of small value (compared to long-term loans extended by banks) and represent a small percentage of financial services for consumers. They are not subject to the Banking Act or regulated by FSA, therefore they do not have to meet the detailed and strict credit risk assessment and credit rating requirements (including those recommended by FSA in Recommendation T); as a result, creditworthiness of their customers may, but need not be lower than the creditworthiness of banking clients.

However, personal loan companies have to adhere to the provisions of the Act on Consumer Credit (including the general requirement for credit risk assessment[4]) as well as comply with the rules of conducting business, including the requirements defined in regulations applied specifically to business operators, such as the Act on Personal Data Protection or the Act on Preventing Money Laundering and Terrorism Financing. All those laws have an influence on the customer service process and are a form of regulation.

To sum up, the objective scope of this report includes only personal loan companies, i.e. entities extending consumer loans which do not take deposits and operate outside FSA's supervision in Poland.

2. Market and its participants

2.1. Personal loans market in Poland

Unlike banks, companies that offer consumer loans are not subject to financial supervision. Moreover, they are not required to publish information other than required by law and concerning their core business as business operators, e.g. they do not have to publish statistics on the number and value of loans. Only some of the companies operating in the market are members of industry organisations; other companies provide their services on a local scale and do not take part in such initiatives. As a consequence, it is impossible to obtain full information on the size of the market. The range of operations of the companies can only be estimated.

When comparing the banking market with the market of personal lenders, one must be aware of certain natural information limitations and differences in business models. First of all, data concerning banks as regulated entities are monitored and published on an ongoing basis. Personal loan companies, on the other hand, are not subject to special reporting requirements, and therefore have a high degree of freedom in that respect. The banking sector's statistics include, among other things, detailed information on the total debt of households resulting from consumer loans at the end of each month, while personal loan companies that publish reports on their activities usually focus on presenting the value of the extended loans in a certain period, often on an annual basis. Moreover, any comparison is made difficult by differences in the average loan term and average value of a single contract. All comparisons between the two markets are only estimations, and the results depend on the adopted approach, i.e. focusing on the sales value or on the debt level.

According to the Social Diagnosis 2013 study[5], ca. 0.7% of the total liabilities of Poles are due to personal loan companies, while 97.0% are liabilities due to banks. The total value of household liabilities due to banks for the first three quarters of 2013 was ca. PLN 534-554 bn according to FSA's data. Based on those data, the total debt to non-banking companies in 2013 may be estimated at PLN 3.0-4.0 bn. According to our analyses, the companies included in this publication contribute to ca. 80% of the estimated loan value. The result is a proof of a huge gap between banks and personal loan companies in terms of the range of lending operations in Poland. This was also noted by the authors of the Social Diagnosis, who wrote about exaggerated media reports suggesting high indebtedness of the households to non-banking sector. The dominant role of banks in the consumer loans market is also stressed by the Financial Supervision Authority[6]. At the same time, loans provided by personal lenders as one of the methods of household funding have become a complementary and important part of the financial services market from the point of view of economic growth.

The market size estimated above is close to the values presented by FSA in 2013, which estimated the total scale of operations of personal loan companies at PLN 3-4 bn p.a.[7]

The analysis of the value of loans extended by companies which are members of the Conference of Polish Financial Companies *(Konferencja Przedsiębiorstw Finansowych w Polsce*, KPF) during the recent few years leads to a conclusion that the personal loan market is characterised with a stable growth, interrupted only in 2009.

By the end of 2008, the Polish market of consumer loans for private individuals (an area of the financial service market operated by banks) developed in a dynamic way. Between 2008 and 2009, structural changes were made in the sources of consumer financing: consumer spending which had been financed through loans was now funded from savings. This results in a lower demand for loans and credits.

5. J. Czapiński, T. Panek (ed.), Diagnoza Społeczna 2013 (Social Diagnosis 2013), Warsaw 2013 – a national panel study of the living conditions and quality of lives of Poles, conducted by a team of scientists headed by Professors Janusz Czapiński and Tomasz Panek for over 10 years.

6. Situation of Banks in 2012. The Report. Polish Financial Supervision Authority, Warsaw, 2013.

7. Ibidem

Table 1. Debts of private individuals due to banks and personal loan companies in 2013 (in PLN bn)

Total household debts due to banks*	543.2
Household debts due to banks from consumer loans*	122.7
Household debts due to personal loan companies**	4.0

** Average value for Q3 2013 based on FSA's data - aggregated monthly data for the banking sector.*
*** PwC's estimation's based on the Social Diagnosis 2013 report and FSA's data.*

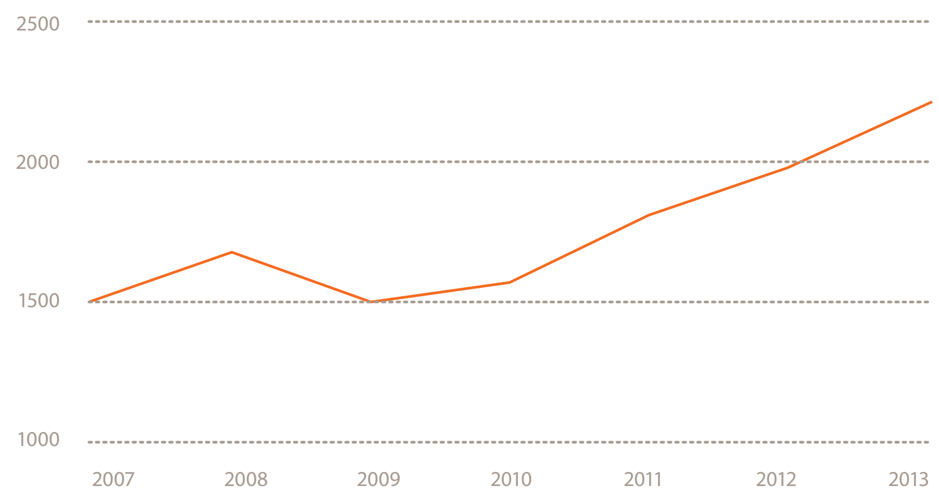
The increase in the value of loans in the non-regulated market after 2009 may be the effect of self-regulation activities of banks, which had to tighten their procedure and restrict the supply of credits in the face of the global financial crisis. Additionally, FSA's Recommendation T adopted in 2011 introduced stricter credit rating criteria (limiting the DtI ratio), which may have caused migration of clients of the lowest financial standing from banks to companies operating in the non-regulated market. However, most probably the increase in the value of loans provided by personal lenders is less connected to the new regulations than the organic growth of the market.

The number of loans granted by KPF members grew in a similar way as the value of the loans and was estimated at ca. 1 million loan agreements in the recent years. The number fell slightly in 2009 but has continued to grow ever since. Charts 2 and 4 show that the average value of a single loan in the reported period ranged from PLN 1,500 to PLN 1,700 PLN and show a small growing trend.

For the sake of comparison, over 90% of cash loans granted by banks are loans for over PLN 3,000[8].

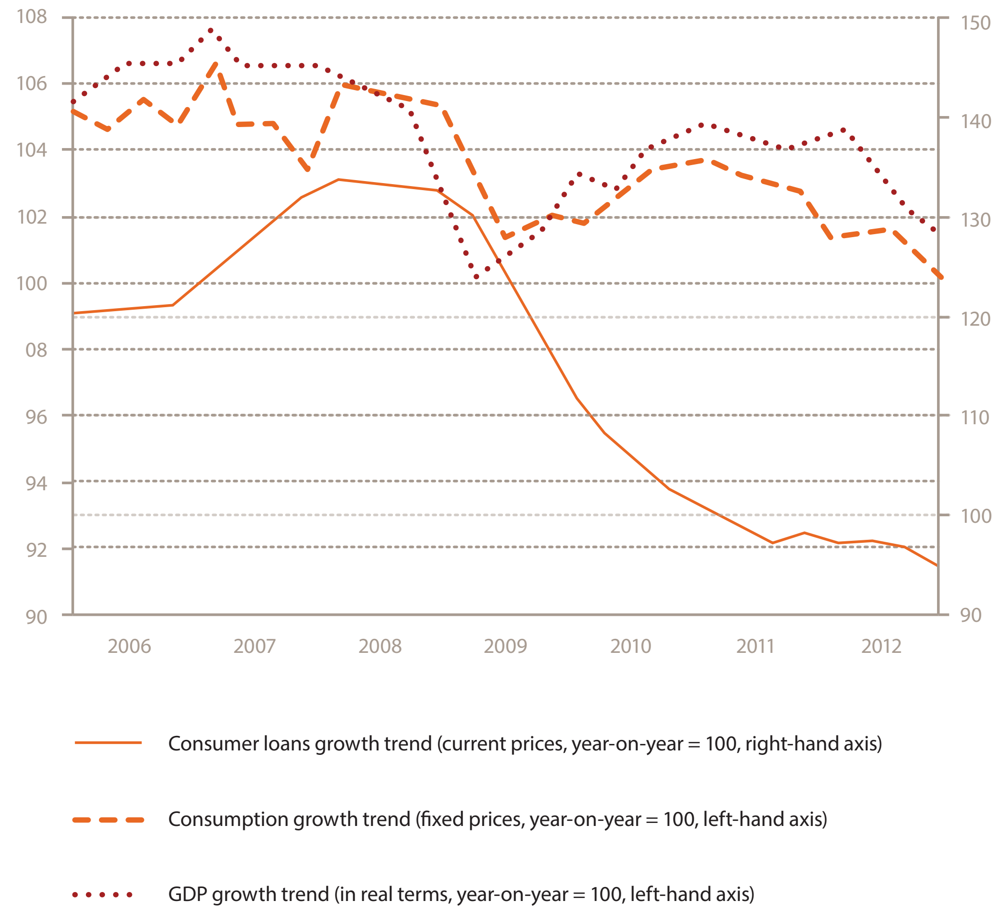
8. Report on Consumer Finance Market in Poland 2013, PwC

Chart 2. Value of loans provided by companies – members of KPF (in PLN m)



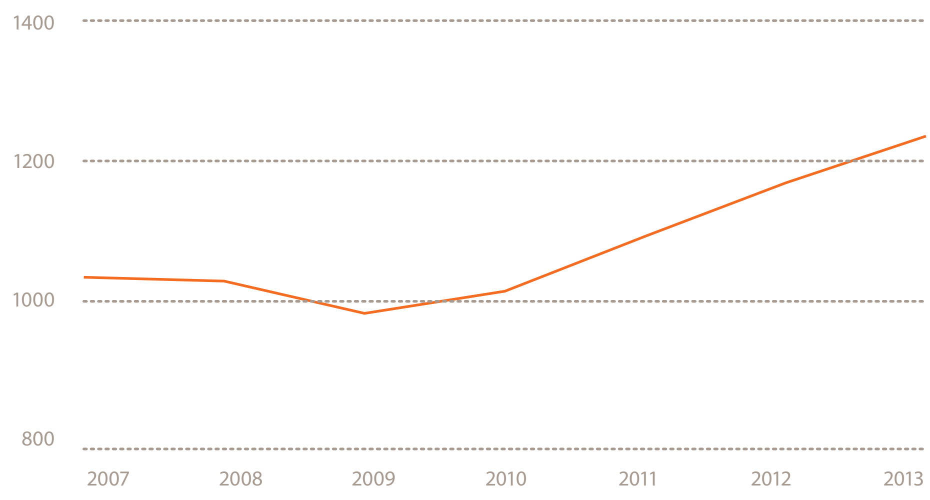
Source: Years 2007-2011: Rynek pożyczek niebankowych w Polsce (Non-banking loans market in Poland), KPF's report; years 2012-2013: PwC's estimates.

Chart 3. Growth trends of consumer loans against growth of consumption and GDP



Source: Report on Consumer Finance Market in Poland, PwC, 2013

Chart 4. Number of loans provided by companies – members of KPF (in 1,000 loans)



Source: Years 2007-2011: Rynek pożyczek niebankowych w Polsce (Non-banking loans market in Poland), KPF's report; years 2012-2013: PwC's estimates

The value and number of consumer loans provided by personal loan companies represent a small portion of the total borrowing market. According to the estimates, both the value and number of the loans granted during years 2012 and 2013 showed a growing trend.

2.2. Personal loans market: customer profile

According to the Social Diagnosis data, the total number of Polish households having any type of debt has increased to 37%. As many as 88% of individuals (see Chart 5) declare having a debt with a bank. According to the declarations, personal loan companies are last in the ranking of the most popular lenders, covering only 4% of the total borrowers.

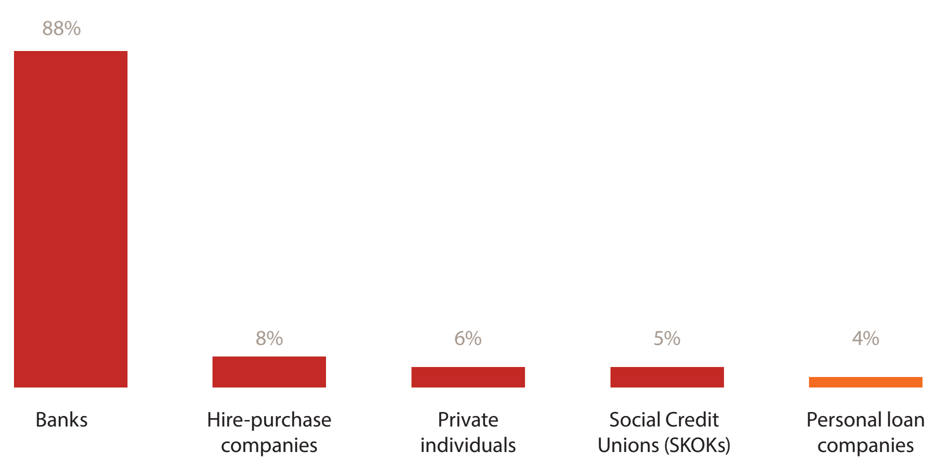
Considering the number of households in Poland (ca. 13.5 m), the overall percentage of indebted households (37%) and personal lenders' share in the household debt (4%), we may calculate the number of households indebted to personal loan companies, which is ca. 200,000. This is not a lot, considering that other market sources[9] talk about ca. 1.5 m – 2 m loans granted by such companies per year. This means that either the average loan term is very short, e.g. 1-2 months (one household may take several to more than ten such loans in a year), or there is a strong tendency among the respondents to conceal the fact that they are indebted to such companies in social studies.

When we look at the basic characteristics of households with debts to personal lenders and those indebted to other institutions, the differences are not really significant. They have similar structure of education of their chief income earners and their places of residence. The only difference is that fewer borrowers who are indebted personal loan companies (11% vs. 16%) live in the largest Polish cities (over 500,000 inhabitants).

However, members of households indebted to personal lenders estimate their financial situation to be much worse than those who have debts with other institutions – approximately 50% report that they can barely make ends meet (such a question was posed in the Social Diagnosis), while among other debtors the percentage is only 17%. This is obviously connected with the actual financial condition of such debtors, which will be presented later in this document.

_9. Cf. e.g.:_
1. "Problematyka Regulacji Rynku Firm Pożyczkowych w Polsce" (Regulation of the Personal Loans Market in Poland), Fundacja Republikańska, 2013.04.23
2. Białowolski P., "Rynek Firm Pożyczkowych w Polsce" (Personal loans market in Poland), KPF, Warsaw, 2012
3. Biuro Informacji Kredytowej (BIK), "Kredyty Konsumpcyjne – spadki i migracje" (Consumer loans: falls and migrations), Warsaw, 2013

Chart 5. Percentage of the total number of individuals with loans and credits from various types of lending institutions based on the Social Diagnosis 2013 data



Sources: Panek, T., Białowolski, P., Kotowska, I.E., Czapiński, J. (2013). Warunki życia gospodarstw domowych. Zasobność materialna. Diagnoza Społeczna 2013 Warunki i Jakość Życia Polaków – Raport (Living Conditions. Affluence. Social Diagnosis 2013 of Living Conditions and Quality of Life of Poles – a Report). [Special issue]. Contemporary Economics, 7, 59-82 DOI: 10.5709/ce.1897-9254.99 and own calculations based on the Social Diagnosis 2013 data available on: www.diagnoza.com

The ratio of households with debts to personal loan companies to the total number of borrowers is only 4%.

Income of customers of personal loan companies and percentage of income used for repayments

There is a widespread view that customers of personal loan companies have lower average income than customers of banks or other institutions providing loans and credits.

The results of the analysis of the Social Diagnosis 2013 data seem to confirm this proposition (see Table 2). The average income of households indebted to institutions other than personal lenders (mainly banks, but also SKOKs, hire-purchase companies and private individuals) was on average 50% higher than the income earned by households indebted to such lenders.

Information about the income of personal loan companies is also confirmed through the results of a survey conducted for the purpose of this report. Most of the respondents participating in the survey declared that average income of their customers are in line with the values presented in the table below.

Chart 6 presents an average percentage of monthly income appropriated to repayment of the debts. It seems that the households that are indebted to personal lenders have to allocate a higher percentage of their net income to repayment of their liabilities compared to those who have loans with other institutions (banks, SKOKs, hire-purchase agencies, or private individuals).

An average household indebted to a personal loan company has to assign approximately 24% of its monthly net income to repayments.

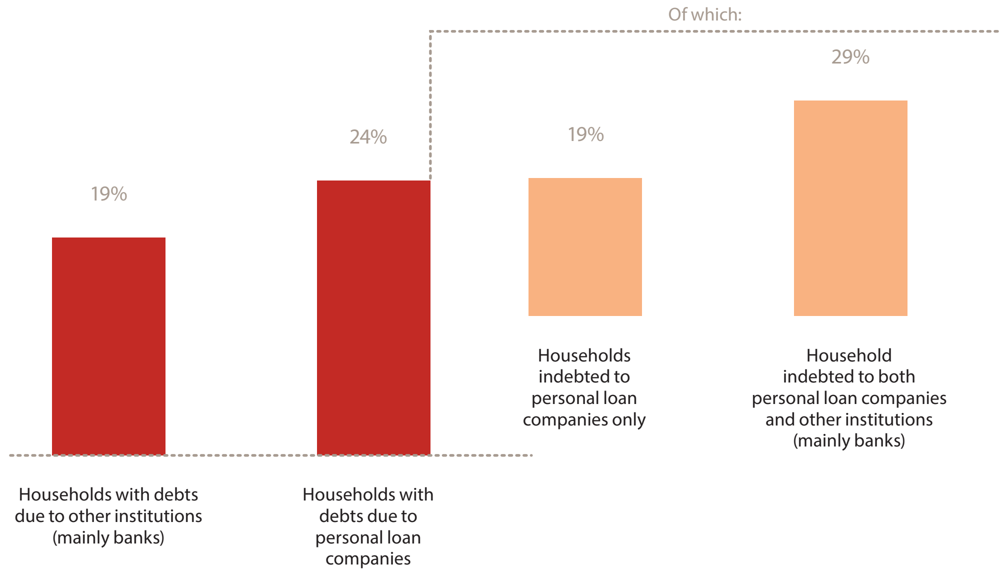
A similar situation is revealed in Table 3, which presents what percentage of customers assign what part of their net income for repayment of debts. As many as 27% customers of personal loan companies assign over 30% of their monthly income for repayments, whereas 9% have to assign more than 50% of their net income for that purpose. For customers

Table 2. Average income of households by sources of debt

	Average net monthly income of a household for the preceding month	Average income of a household for the preceding year	Average monthly income per person for the preceding month	Average monthly income per person for the preceding year
Households with debts due to other institutions (mainly banks)	PLN 3,967	PLN 3,967	PLN 1,415	PLN 1,423
Households with debts due to personal loan companies	PLN 2,520	PLN 2,588	PLN 967	PLN 995
Households with no debts	PLN 3,100	PLN 3,130	PLN 1,322	PLN 1,334

Source: PwC's calculations based on the Social Diagnosis 2013 data

Chart 6. Average estimated percentage of monthly income used for repayment of loans and credits



Source: PwC's calculations based on the Social Diagnosis 2013 data

indebted to other institutions, the figures are 15% and 3%, respectively.

The higher burden ratio shown in Chart 6 and Table 3 for customers of personal loan companies is mainly due to the fact that according to the Social Diagnosis data approximately 50% of such borrowers combine such debt with the loans due to other institutions. On average, those households use nearly 30% of their monthly income to repay the debts (see Chart 6), and the percentage of households that use over half of their monthly budget for such purpose is 16% (see Table 3).

On the other hand, the analysis results prove that the debt burden ratio of households indebted to personal loan companies only is

Table 3. Percentage of households with various levels of debt burden ratio by sources of debt

	Percentage of indebted households assigning a specific part of monthly income towards repayment of credits and loans			
	Less than 10%	10%-30%	30%-50%	Over 50%
Households with debts due to other institutions (mainly banks)	25%	60%	12%	3%
Households with debts due to personal loan companies	24%	49%	18%	9%
Of which:				
Households indebted to personal loan companies only	29%	51%	18%	2%
Household indebted to both personal loan companies and other institutions (mainly banks)	19%	47%	18%	16%

Source: PwC's calculations based on the Social Diagnosis 2013 data not much higher than in the case of households with other debt types. Almost 30% assign less than 10% of their income to repay the debts (see Table 3), and their average debt burden ratio is lower than 20% (see Chart 6) – the same as in the case of individuals indebted to other institutions (banks, SKOKs, hire-purchase agencies, private individuals).

The households indebted to personal loan companies assign a larger portion of their net monthly income to repay their debt than the households with debts to other institutions (banks, SKOKs, hire-purchase companies, and private individuals). On the other hand, the mere fact that a household is indebted to a personal lender does not necessarily mean an excessive debt burden to the household budget. The real danger appears when households combine several liabilities, borrowing funds from many sources. Such households are exposed to the risk of being caught in a debt spiral, which requires special caution on the part of lenders.

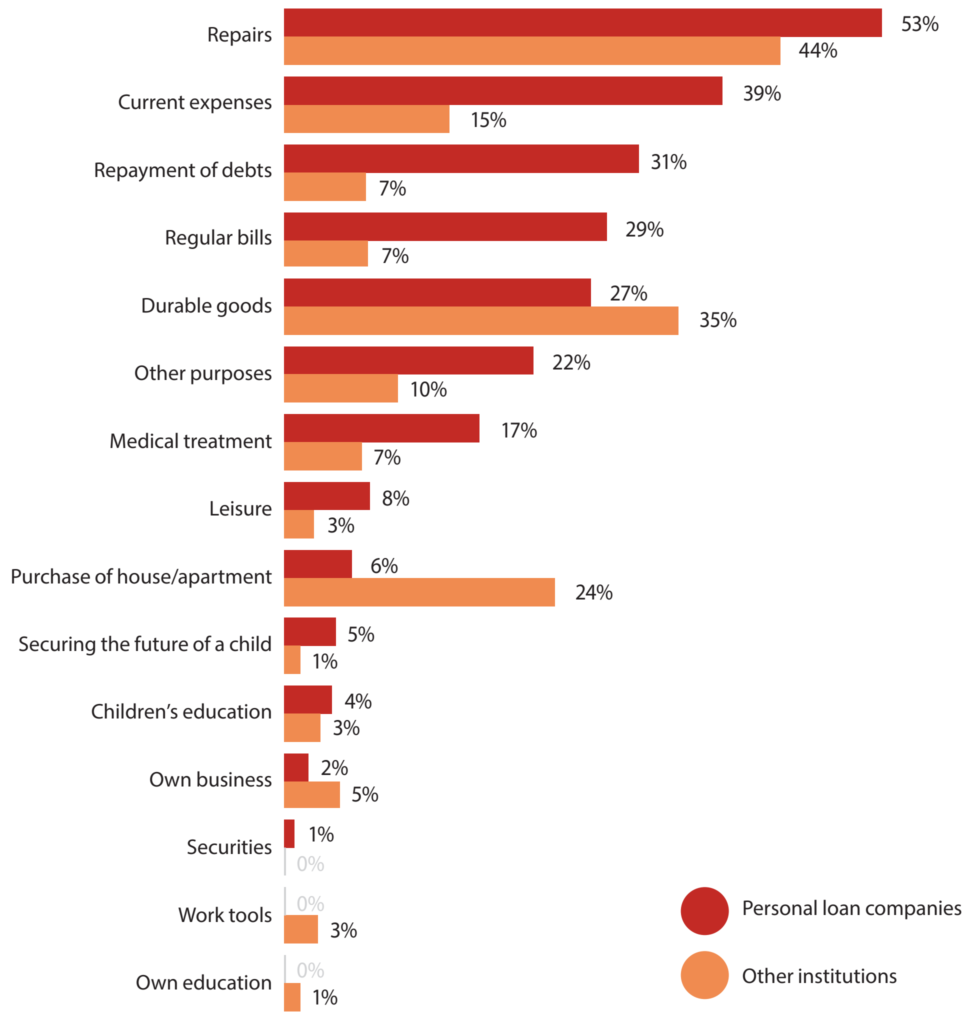
Purpose of loans taken from personal loan companies

The fact that 50% of households with debts to personal lenders combine the debt with loans and credits to other institutions suggests that a lot of the borrowers are people who due to the need to repay their loans with other institutions have to seek offers from personal loan companies. This is only partially true (see Chart 7).

Households with debts to personal loan companies use the loans mainly to make house repairs (53%) and cover the current spending needs (39%). Similar reasons are identified by the banking sector customers. Repayment of other debts is ranked as the third most frequent reason (31%). Other factors that prompt the customers to seek funding from personal lenders include: regular bills, purchase of durable goods and special occasions such as weddings or funerals.

The results also reveal that for ca. 60% of households that are indebted to both other institutions (banks, SKOKs, hire-purchase companies, private individuals) and personal loan companies, the main reason for seeking the services of the latter was the need to repay other liabilities; other households (ca. 40%) used services of personal lenders for other needs (as listed in Chart 7).

Chart 7. Purpose of loans taken from personal loan companies and other institutions



Source: PwC's calculations based on the Social Diagnosis 2013 data

Loans taken from personal loan companies are used mainly for consumption. On the other hand, 30% of the borrowers use the loans to repay other debts. This reinforces our earlier comment on the need to apply special caution by lenders when assessing the creditworthiness of such customers.

2.3. Business model of a personal loan company

The model of funding the personal lending business in Poland is similar for most companies active in the market. The lenders are usually joint stock or limited liability companies, which, and this must be stressed, **do not finance their lending operations through customer deposits** (do not conduct banking operations) but use sources of funding that are typical for business enterprises.

Personal loan companies grant loans for the term of one week to tens of weeks. The loan amount may vary depending on the lender, ranging from PLN 50 to as much as PLN 25,000. However, the average amount of the loan does not exceed PLN 1,000.
Revenues of a personal loan company are generated through:

- Loan interest;
- Loan commission;
- Insurance;
- Repayment commission;
- Other contractual costs.

In addition, in the event of delays in repayments, additional sources of income are generated, such as:

- Penalty interest;
- Costs of reminders (phone calls, letters, personal visits);
- Other contractual penalties.

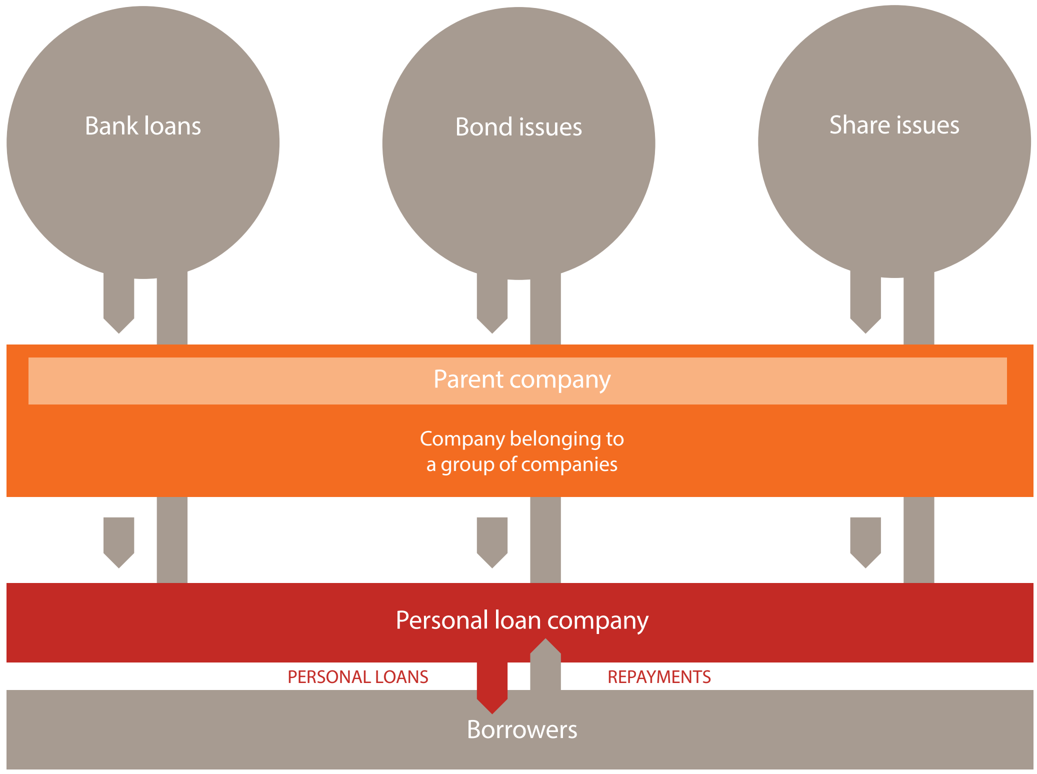
As a standard, personal loan companies finance their operations with their own capital, funds provided by the parent company, or bank loans. Larger entities may issue corporate bonds, and those listed in the stock exchange may obtain capital by means of share issues.

The results of the survey conducted among personal loan companies confirm the above facts. Most of the companies that decided to answer the question about main funding sources pointed to own funds or group funds. For some lenders, bank loans are an important source of funding, as well as bonds, although the latter were quoted less frequently.

For companies belonging to a group, the aforementioned sources of funding may be used by the parent company or dedicated companies that focus on obtaining funds for the whole group using the economies of scale and diversified sources of capital in various countries. The largest players in the Polish market are members of groups of companies; therefore they are able to obtain attractive terms of funding in form of syndicated loans or issue of bonds in various countries. Such personal loan companies may also sell impaired loan portfolios to their parents or to other entities, improving in this way their liquidity.

The personal loan companies discussed in this report are funded through standard instruments. They do not obtain deposits from private individuals. Therefore, the risks related to their business are not identical in that respect to the risks appearing in the banking sector, but are more similar to risks of any other business activity. On the other hand, personal loan companies must comply with the regulations applicable to the lending business.

Chart 8. Sources of funding operations of personal loan companies



Source: Own work

2.4. Segmentation of personal loan companies

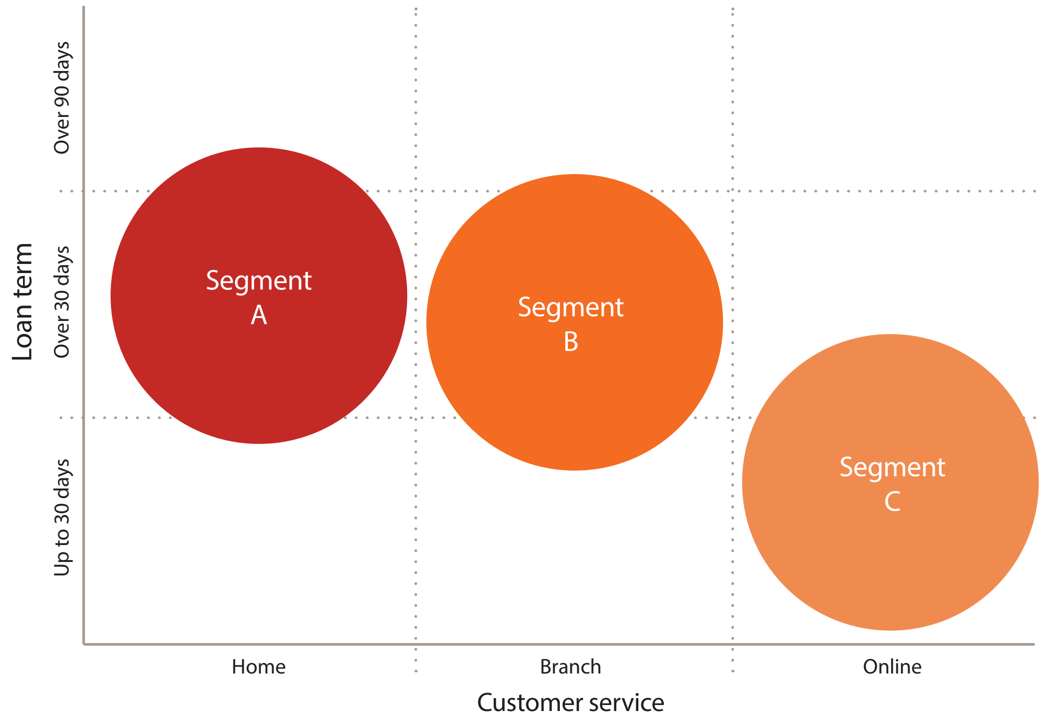
One of the major aspects influencing the business model of a personal loan company is the approach to customer service. It influences the procedure of applying for the loan and the place and method of signing the loan agreement, and defines the method of verification of the potential borrower – his/her personal details, address or living conditions. In this vein, personal loan companies were divided into three segments (each segment containing at least several companies from the personal loans market based on the conducted analysis):

- Segment A – Home credit companies;
- Segment B – Lending companies with branches/outlets;
- Segment C – Online lending companies.

It is worth noting that some companies operating in the Polish market are hybrids combining the characteristic features of more than one sector, which offer a possibility to sign the loan agreement at the branch office as well as at home. There are also online companies which collaborate with credit intermediaries. Such companies were classified within appropriate segment based on their most typical products and services.

Another criterion of segmentation, often derived from the company's business model, is the term of the loan, which to a large extent influences the costs paid by the borrower. The chart below positions the personal lender segments depending on the length of the loan term. It is clear that most of the companies from segment A focus on loans with repayment terms of more than 30 days, while segment C companies on payday loans (up to 30 days).

Chart 9. Segmentation of personal loan companies



Source: Own work

Segment A – Home collection credits

Customer communication

A customer who wants to borrow money from a company belonging to segment A may apply for a loan online; he or she may also contact the Call Centre or send a text message. After the initial review of the application or phone interview, the lender's representative contacts the potential borrower by phone to make an appointment at the customer's home. At home, the representative checks the appropriate documents and fills in the required form. Depending on the lender and the loan amount, the representative may extend the loan on the spot or request the loan company to make a transfer to the borrower's account.

Products

Personal loan companies from Segment A address their offering to individual as well as business clients. According to the information published on their websites, the amount of the extended loan may range from PLN 200 to PLN 10,000. Loans for higher amounts are available to regular customers.

Loan may be repaid over various terms, from 18 to 62 weeks. In most cases, repayments are made on a weekly basis.

An important aspect of Segment A companies business model is the so called **home collection** service. The home service is an optional form of repayment, where the sales representatives visit the customer at home every week to collect repayments. This option significantly increases the loan costs, but gives the customer more flexibility in terms of repayment as he or she may consult the lender's representative on an ongoing basis.

Business model

Definitely the most important aspect of Segment A company business model is the home visit of the sales representative at the borrower's, during which the representative gathers and verifies the information necessary to make the lending decision.

Verification of a potential customer during filling in the application form and during a phone interview with the consultant depends mainly on the amount of the expected loan and the credit history. A mandatory element of the scoring process is confirming the borrower's identity and permanent place of residence, which occurs at the borrower's home.

The home visit is a part of the customer scoring process, during which the lender's representative confirms the customer's identity and permanent place of residence, and makes an individual assessment of the customer's standards of living through a visual inspection and interview.

In the case of a positive lending decision, the customer may choose whether the weekly repayments will be collected by a representative visiting the customer at home, or transferred through a bank account. Despite significantly higher costs in this segment, customers often choose the home collection service, on which the business model of segment A companies is based.

Theoretically, the customer may choose between the types of service; however, if he or she decides to make repayments through a bank transfer, more discipline is required as the customer needs to remember about the weekly repayment regime and any penalty interests or other charges for late payment reminders.

Home service is an element of collection of repayments on a weekly basis, and also an element of the debt recovery process: a sales representative of the home credit company may remind the customer about the payment but also negotiate prolongation of the payment term.

Successful repayment of loans relies not only on the benefits of the home collection model but also on small repayment amount payable on a weekly basis. From a psychological point of view, it is easier to make frequent repayments of smaller amounts than make a large single repayment. The average amount of loans provided by Segment A companies is less than PLN 1,000, and the typical customer is a private individual.

Segment B – Loans granted through a branch/outlet

Customer communication

In the case of segment B lenders, loan requests may be submitted by phone, website or at the physical branch or credit outlet. The potential customer must provide all necessary documents to the branch where the documents are checked and a formal loan application is filled in.

Products

Lenders from segment B have also a broad range of products and services. The lower limit of the loan is set much lower than in the case of segment A lenders, and the upper limit is much higher as it reaches PLN 25,000. Loans of higher amounts are addressed to business entities to start up and develop business or make repayments. The biggest market players are able to offer special loans of PLN 200,000 to 300,000 with relatively long repayment terms and a possibility to use mortgage as a security.

Usually the higher the loan (for a longer term), the more documents have to be provided by the potential borrower.

Loans offered by segment B companies may be repaid over a period of one week in case of payday loans to 48 weeks for loans of higher value. When the loan amount granted to a business customer amounts to PLN 150,000 to 200,000, the repayment term may be even 150 weeks.

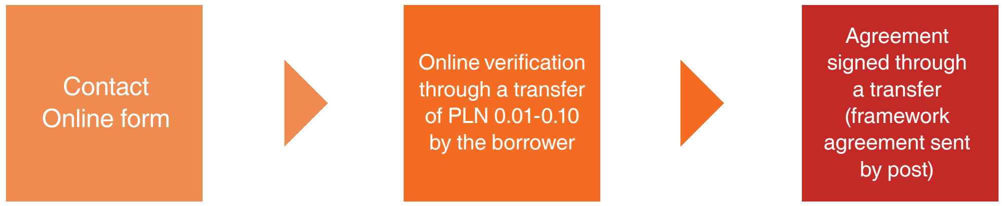
Business model

The business model of a segment B lender is based on a network of branches or outlets where the customer finalises all the formal requirements. Customer verification depends also on the product type. For smaller amounts with shorter repayment terms a simplified process is used, whereas in the case of higher loans with longer repayment terms the customer verification process is similar to that used in banks, where all types of documents and income statements must be provided, including clearance certificates or utility bills.

Segment B has a different cost structure and scoring methods than segment A: in this case, home visits have to be replaced with other tools to verify the customer's creditworthiness.

Segment C – Online loans

Customer communication



In segment C, the customer finalises all formal requirements on the lending company's website. When the potential borrower fills in an online form, the loan company will request the customer to make a bank transfer for a minimum amount, usually PLN 0.01 or 0.10; in this way, the company is able to verify the customer's details. If all requirements are met and a positive credit decision is issued, the money is paid to the borrower, which may even happen on the same day.

Products

Loan companies from segment C offer one product only: a payday loan of a relatively small value, granted for a short period of time. In the case of most lenders the maximum loan amount is PLN 2,000. Some lenders offer loans of a maximum amount of PLN 500.

A standard loan term of a typical online lender does not exceed 30 days.

Business model

The success of the business model of a segment C lender depends primarily on a high volume of loans of relatively low value. Loans are granted for a very short term, usually not more than 30 days. Because the customer signs a framework agreement with the loan company, high turnover is ensured as the framework agreement speeds up the lending process and allows the customers to contract quickly new loans (or prolong the repayment term of the existing debt). All those operations are subject to commissions. Quick processing of loans and formal arrangements reduced to a minimum is a significant competitive advantage of the lenders in this segment.

Because the companies do not have to maintain as large as staff to handle the Call Centre services, or sales representatives as in segment A, or branch offices/outlets as in segment B, the business model is assumed to be very cost effective. However, because customer credit scoring methods used by lenders from other segments cannot be applied in the case of segment C companies, they are forced to introduce more rigid and automatic scoring methods, which result in a higher application rejection rate.

High efficiency of segment C companies is also manifested in debt recovery. The non-paying customers are quickly reminded about the repayment through and charged with a reminder fee, and subsequently with penalty interest and other charges; ultimately, their debt is sold to a debt recovery company which subsequently handles the liability.

2.5. Amount and structure of loan costs

The costs of a personal loan are strictly dependent on the loan term. The channel through which the service is provided is of less importance. One should remember, however, that loans with the term longer than 30 days are typically provided by Segment A companies, while shorter-term loans are provided by Segment C companies (Segment B varies in this respect). Differences between the segments appear in particular with regard to the loan cost structures. In addition, efficiency of a given business models also depends on the cost of funding and cost of credit risk.

The following analysis is based on the results of the Mystery Shopper study conducted for the purpose of this report. A detailed description of the methodology of the study is presented in Chapter 3.1.

Costs of personal loans

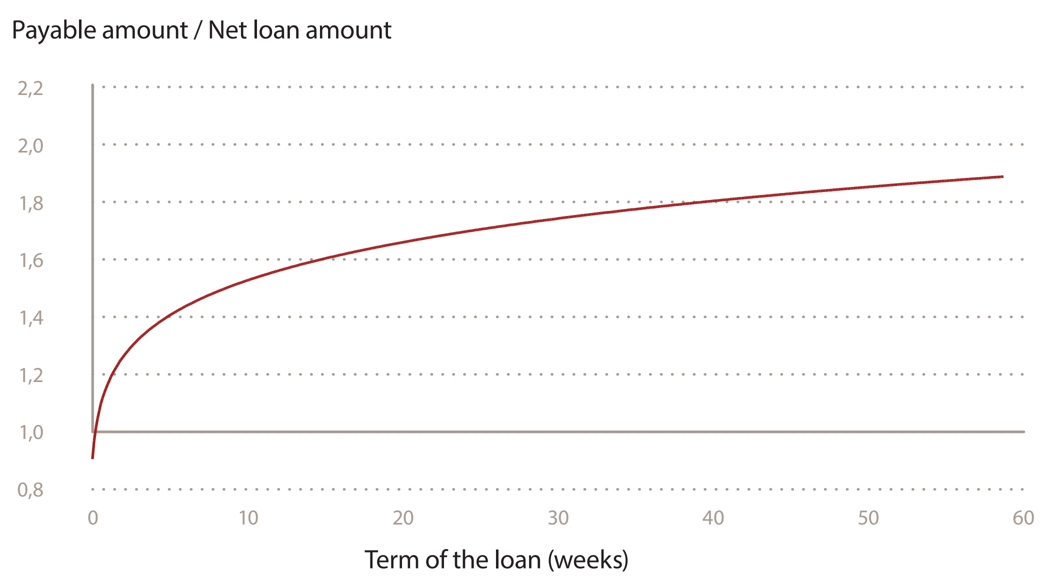
The total loan costs are directly proportional the loan term expressed in weeks (see Chart 10). The costs are significantly lower for loans granted for a term of up to 1 week, amounting to 10-15% of the net loan amount.

The costs then increase to reach ca. 50% for loans with a term of 20-30 weeks to 80%-100% for loans with a repayment term close to one year.

The relationship between the loan term and the real-term APR is exactly the opposite.

The base for calculating APR was the amount actually disbursed to the customer, and the repayment amounts were determined on the basis of repayment schedules presented to the customers under the individual agreements. This means that the costs of loans included all the above elements over the amount actually paid to the customer, irrespective of whether the costs were obligatory or not and whether they were or were not included in the gross amount of the loan according to the agreement.

Chart 10. Costs of a consumer loan depending on the loan term

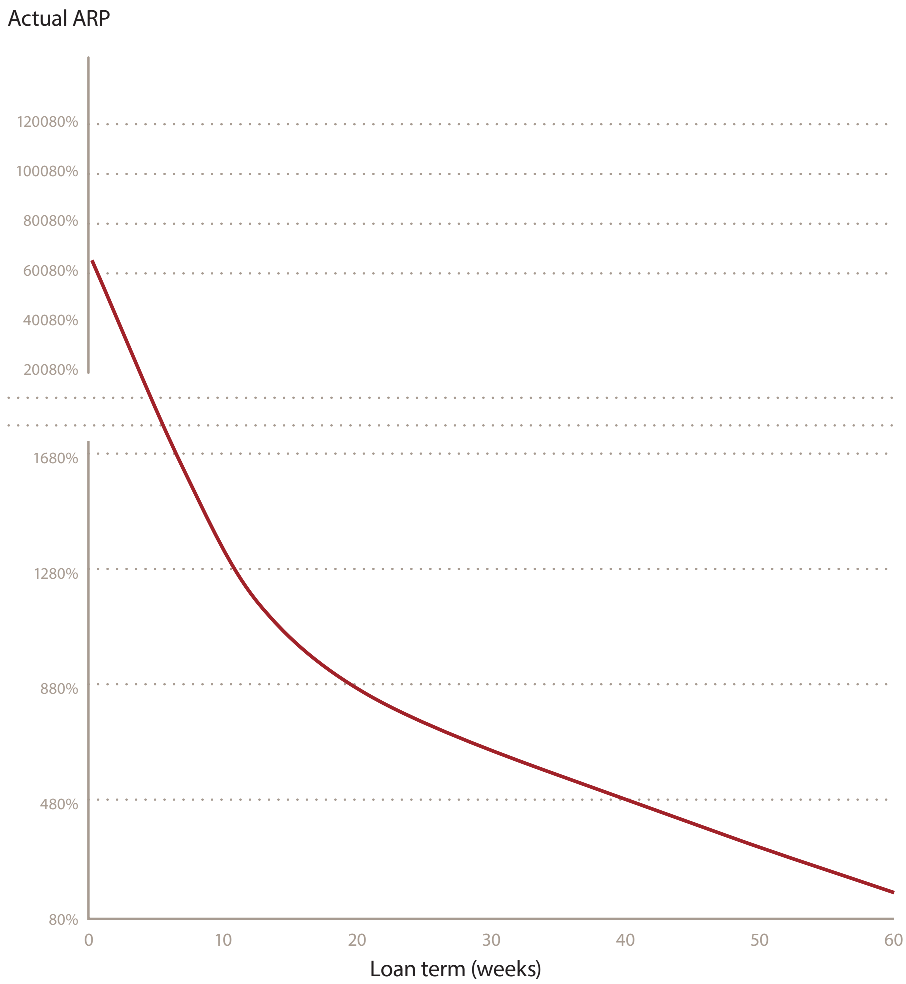


Source: Analysis of the results of PwC's Mystery Shopper study

One has to stress that the ambiguity regarding how to calculate APR leads to mixed results in terms of average APR. Thus, for loans with the term ranging from 10 odd weeks to one year, the APR (which included all elements over the amount paid to the customer) amounted to 778%, while the average rate specified in the agreement was 188%. For loans extended for shorter terms where the cost structure was much less complicated, the APR specified in the loan agreement was in line with the rate analysed in this report and amounted to tens of thousands percent.

Chart 12 shows the relationship between the term of a loan and its APR. It is clearly visible that APR is very high when the loan is granted for a very short term – up to one week. APR values for such products exceed tens of thousands percent. For loans with a 20-week term, APR is 1000-1200%, for loans with a 30- or 40-week term, the rate is ca. 650-700%, and for loans with the term exceeding 50 weeks the rate amounts to ca. 300%. Such great differences between APRs are obviously influenced by fixed charges relative to the total costs of the loans extended in the market in question.

Chart 11. APR level relative to loan term



Source: PwC's analysis based on the Mystery Shopper study

Different approaches to calculating the APR adopted by different lenders and enigmatic three- or four-digit numbers representing the APR value question the usefulness of that indicator for the customers to make comparisons between costs of loans. This concerns in particular the loans with the shortest maturity. This also means that any statutory limitations of APR may result in pushing this type of financial products out of the legitimate market.

Loan cost structure

The lender's business model has a significant impact on the loan cost structure. Regulatory limitations of cost elements will have a varied effect on the lender segments operating in the market.

The approximate cost structure depending on the term of the loan and the segment in which the lending company operates is presented in Chart 12. The chart shows clearly that for loans provided for a very short term, whether via Internet or through a physical office, it is difficult to pinpoint a single factor determining the level of the loan costs for the borrower. The customer who gets the loan for a short term pays first of all the upfront fee (46% of the total loan costs), then the insurance costs and the interest. Due to statutory requirements, the loan interest rate is replaced by a commission, which is defined as a fixed percentage of the borrowed amount. Some lenders decide to waive that cost; instead, they increase the insurance cost and/or the fixed charge.

For home collected loans with an average loan term (18 to 40 weeks in the studied cases), the main cost factor for the client is the home service fee. The average fee amounts to 42% of the loan amount and represents 56% of the total costs of the loan. The other important cost factors are the upfront fee and insurance, while interest and additional fees are less significant.

The longest term of the loan was one year. The loan in question was repaid on a monthly basis and was not collected at home. This was the only consumer loan with such distinct features in our sample; therefore we decided to include it in our analysis.

Because of lack of weekly home visits and less frequent repayments, such a loan seemed more risky from the lender's perspective. It is not surprising, therefore, that the most significant cost factor was insurance, which represented 48% of the loan amount and 55% of the total costs, which in fact replaced the costs of home service. The second important cost factor was the upfront fee, while interest was the least significant factor.

This analysis of the amount and structure of the loan costs reveals two important issues, apart from the doubts concerning APR. Firstly, the costs of loans provided for a similar term stay within a common range, which may help establish a reference level representative for the market. Secondly, the structure of the cost is strictly dependant on the business model.

In a survey conducted by PwC among lending companies, limitation of the maximum allowable level of lending costs is mentioned as an area of regulation potentially acceptable to the respondents.

Chart 12. Structure of loan costs relative to loan term and loan providing method

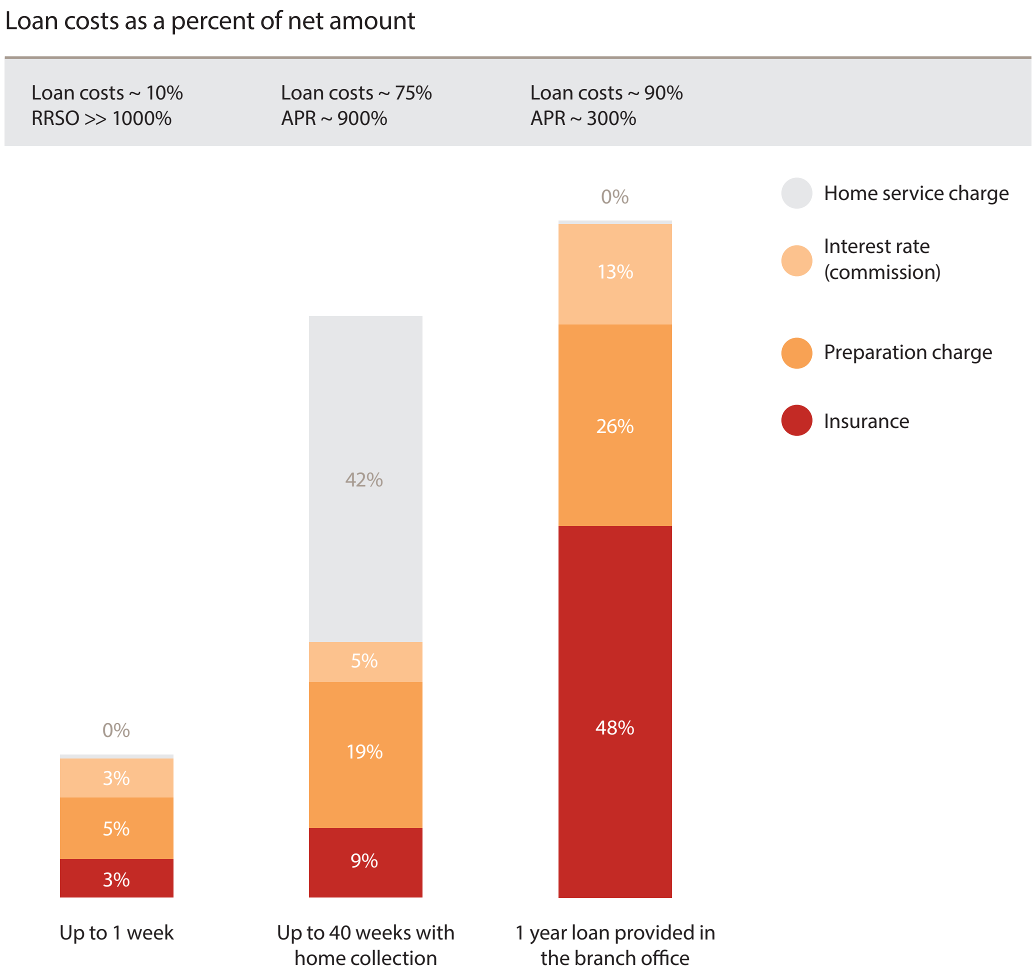
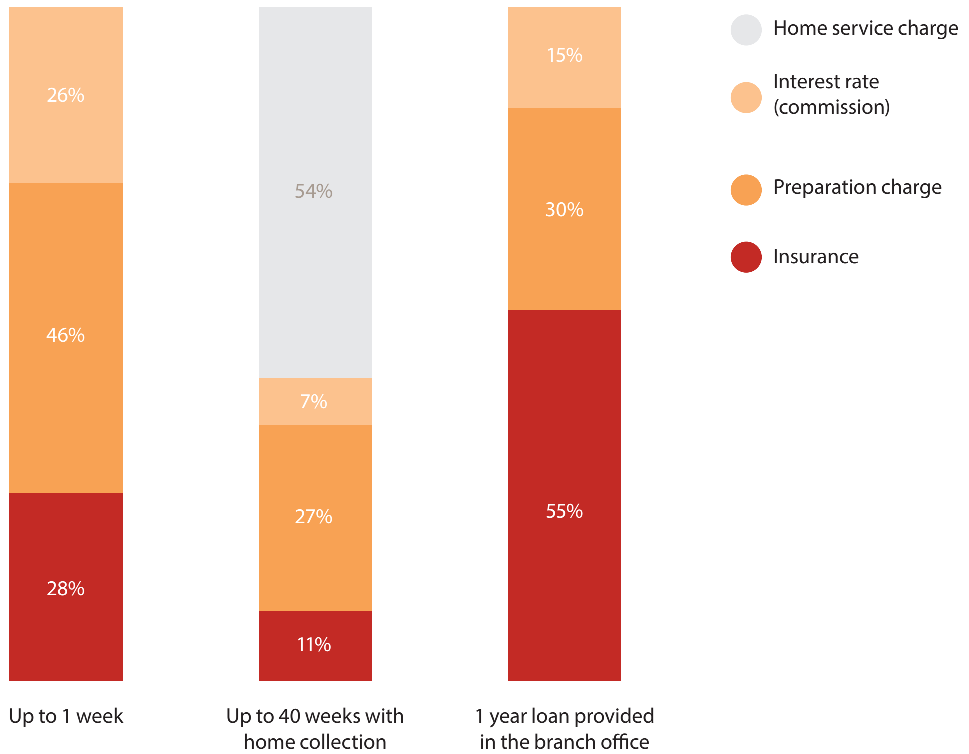


Chart 13. Structure of loan costs relative to loan term and loan providing method – total cost = 100%



3. Consumer practices

3.1. Practices of personal loan companies with regard to customers based on the Mystery Shopper study

Methodology of the study: general information

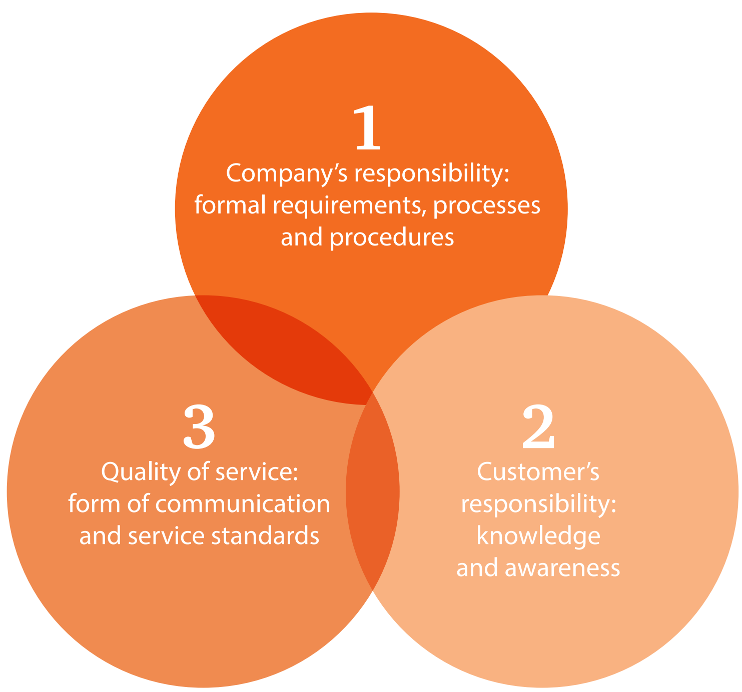
To evaluate and describe the consumer practices used by personal loan companies during the lending process, a qualitative study was conducted for the purpose of this report. The study was conducted through a Mystery Shopper method by a specialised third party company.
A comprehensive diagnosis of the lending process was conducted with regard to the following stages of the process:

- Visiting the website;
- Submitting a loan application;
- Accepting or rejecting decision;
- Signing the loan agreement and obtaining the money;
- Contact with the lender after obtaining the loan;
- Withdrawal from the loan agreement;
- Repayment of the loan.

Evaluation of the quality of the service during the lending process was based on:

- Respondents' records of events occurring during the credit process;
- An extensive process evaluation form filled in by the respondents;
- Analysis of the records and agreement formats, and any other documents provided to the respondents by personal loan companies;
- Process, form and quality of communication on the part of the lender;
- Analysis of the available marketing communications produced by personal loan companies.

The evaluation was conducted from the point of view of three main areas:



Sample

At first, the study envisaged a sample of 18 respondents in 12 companies. In the end, the study was conducted on a supplemented sample of 20 respondents (N=20) in 11 companies (contact with the twelfth one proved impossible). The sample was supplemented with two loan applications in order to obtain at least two agreements for each of the segments. The analysis of the results was broken down into 3 segments of the personal lenders market as presented in Chapter 2.4:

- Segment A – Home credit companies, N=7,
- Segment B – Lending companies with branches/outlets, N=6,
- Segment C – Online lending companies, N=7.

In each of the segments, the respondents were supposed to submit an application for a PLN 500 consumer loan for the shortest repayment term possible.

The findings and all information from the Consumer practices chapter are based on the study conducted for the purpose of this report.

Customer profiles

Respondents participating in the study met the criteria of either of the two customer profiles: standard customer and risky customer.

The number of customers within the specific profiles was 11 and 9, respectively.

Table 4. Customer profiles used in the Mystery Shopper study

Characteristics	Standard customer profile	Risky customer profile
Credit record	No negative credit record at credit bureaus (BIK, BIG) and other credit information agencies	Negative credit record at credit bureaus (BIK, BIG) or other credit information agencies: an over 30-day default in repayment of a bank loan
Employment	Employed for at least 3 months based on a contract of employment	Irregular income
Income	Regular, not higher than PLN 3,000 gross	Irregular income of PLN 2,500 gross on the average
Place of residence	Permanent place of residence or tenancy for at least a year	Permanent place of residence or tenancy for at least a year
Car	Declared ownership of a car	No
Age	Woman – 35-45 years of age Man – 40-50 years of age	Woman – 20-55 years of age Man – 20-55 years of age

3.2. Company's responsibility: formalities, processes and procedures

Objectives of the analysis

As part of its responsibility, the lender should, at each stage of the lending process, comply with legal requirements and ensure appropriate processes and procedures guaranteeing efficiency of operations as well as providing an ethical basis for actions towards the customer. This is especially important due to the specific nature of the customer in the sector. As shown in PwC's studies presented in the chapter entitled "Market and its participants", households indebted to personal loan companies perceive their own financial situations as much worse than household having debts with other institutions. The risk of overburdening the home budget with loan repayments appears especially high when household combine several types of loans and credits, and such customers seem to be a particularly vulnerable group. Thus, as proven by the analysis, personal loan companies should ensure that scoring includes appropriate procedures for obtaining information on the potential customers' credit standing.

At every stage of the process, legal tools can be applied to ensure consumer protection. The diagram below shows the regulations that are important for each individual stage of the lending service process.

Stage	1 Customer's decision to contract a loan	2 Inquiring and applying for a consumer loan	3 Getting more information about the offering and agreeing on the final terms and conditions of the loan	4 Signing and executing the agreement	5 Closing the process
Regulations	Act on Consumer Credit (implementing Directive 2008/48/EC) Act on Competition and Consumer Protection Act on Combating Unfair Market Practices	Civil Code Act on Personal Data Protection Banking Law	Act on Consumer Credit Act on Competition and Consumer Protection Act on Combating Unfair Competition	Civil Code (Art. 385(1) providing for a register of forbidden contract clauses) Act on Combating Unfair Market Practices	Act on Consumer Credit Civil Code Code of Civil Procedure Act on Combating Unfair Market Practices

With those assumptions in mind, and taking into account the results of analysis of other documents identifying key aspects of operations of personal lenders in Poland, the following issues were found to be key determinants of a responsible and quality loan process ensured by the lender:

- Appropriate method of customer credit scoring,
- Effective risk management system based on standardised and transparent procedures;
- Completeness, transparency and legibility of the loan agreement, which must be compliant with the applicable law.

The above conditions were adopted as a basis for the Mystery Shopper study, during which the following questioned were raised in respect of the lender's responsibility area:

- Do the lenders make business decisions related to customer risk assessment in an effective and ethical manner?
- Do the lenders pursue their obligations in a responsible manner and in accordance with the applicable law?

Detailed findings

Finding 1: The lending process followed by the personal loan companies included in the study is similar in each company and based on standardised stages. A large number of the companies operate in an efficient, predictable and effective manner, and in accordance with the customers' expectations.

Practices noted during the Mystery Shopper study:

- The documents received by the respondents from the lending companies included the loan agreement, agreement withdrawal form, and information form. Respondents from Segments A and B had to sign the loan agreements, while Segment C customers received framework loan agreements, which enabled them to apply for subsequent loans after repayment of the original loan.
- In most of the cases, lenders from all segments responded to the loan applications within the time limit specified in their websites, which included from several hours to maximum 2 days.
- A vast majority of the respondents had no difficulties in contacting the representative of the lending company during the duration of the loan agreement. During the discussion, the respondents did not have any problems with obtaining information about the level of their debts or the possibility of an earlier repayment.
- The process of withdrawing from the agreement was in most cases consistent with the information provided to the respondents on signing the loan agreement. After filling in an appropriate application and contacting the lender, the respondents transferred the due amounts to appropriate bank accounts or paid cash to the lender's representative.
- In most of the cases the costs of withdrawal from the loan agreement were not applied, as provided for by the loan agreements.

Finding 2: The scoring methods and procedures vary depending on the business model and risk appetite of a lender, and therefore may result in different lending decisions.

Practices noted during the Mystery Shopper study:

- Most of the respondents in Segment A managed to get their loan applications accepted. Companies operating in that segment granted loans both to standard and risky customers. In the case of Segments B and C companies, applications from all respondents classified as risky customers were rejected. Moreover, only some of the standard profile customers were accepted and were able to sign the loan agreement.

	Decision	Segment A	Segment B	Segment C
Standard customer	Granted	3	2	2
	Refused	1	0	2
	No information	0	1	0
Risky customer	Granted	2	0	0
	OdRefusedmowa	1	3	3
	No information	0	0	0

- The documents required by lenders operating in Segments A and B for verification purposes were in most cases consistent with those presented in the websites. Respondents from all three segments had to produce the ID and documents confirming regular income as well as the amount of income. In Segment B there was also an optional additional requirement for providing utility bills. In the case of Segment C, the respondents were only asked to fill in an appropriate form, where they were asked to answer questions about their personal details and make a transfer from their personal bank account. In some cases, the respondents also had to present a proof of employment.
- To perform the credit scoring and establish the customer profile, representatives of Segments A and B lenders asked questions to obtain the following information:
  - Income regularity;
  - Income level;
  - Contract of employment (including contract type);
  - Place, type and form of employment (e.g. full-time or not);
  - Number of dependents;
  - Other debts to be repaid;
  - Amount of other repayments due;
  - Existing debt;
  - Existing enforcement titles;
  - Marital status.

It must be mentioned that in none of the cases the sales representative verified all of the above elements at the same time.

Finding 3: In some cases, certain lenders perform their obligations in a different way than required by the law or good practice.

Practices noted during the Mystery Shopper study:

- Provisions of loan agreements are sometimes inconsistent with the applicable laws.
- In each segment there were cases where customers rejected during the credit scoring

Risks for the consumer related to typical loan agreement templates	When signing a loan contract, lenders must adhere to strict requirements provided for by the Consumer Credit Act. However, despite that:
	A minority of the examined companies failed to comply with some information requirements, in particular by failing to inform the customer on the rules and terms of repayment in a clear and understandable way and before signing the agreement.
	Some of the loan agreements examined during the study lacked full information about APR, commission and total cost of the loan.
	Some of the loan agreements lacked sufficient information on a possibility to take advantage of the extrajudicial process of settlement of disputes and on the rules of applying for such process.
	In some cases, the lenders were entitled to make unilateral amendments to the loan agreement even though the Competition and Consumer Protection Office found this to be a forbidden contractual clause.
	Standard agreement forms used by almost all personal loan companies included in the study lacked clarity and legibility, e.g. they were printed in small font, and made an impression of General Terms of Sale, and the complex character of some of the terms and conditions could affect their understanding.

conducted by the lending company were not informed about the reasons for the rejection, which is against the law; in some cases the rejection was caused by lack of precise information about the required documents. The reasons for the refusals included lack of a required document (certificate) or lack of a product that would suit the customer profile (Segments A and B). In Segment C, one of the reasons for the rejection was lack of regular income or negative feedback from the credit bureaus (BIG).

The lending process is a typical business process, with consistent stages in all three segments. A large number of the companies operate in an efficient, predictable and effective manner, and in accordance with the customers' expectations about the time required to obtain the loan.

There were cases where lenders performed their obligations in a different way than required by the law or good practice. Customers should be educated on how to take advantage of the current regulations and enforce the already existing customer protection and lender control tools.

3.3. Customer's responsibility: awareness and knowledge

Objectives of the analysis

During the process of obtaining a loan, the customer is responsible for making an informed choice of the offering and giving informed consent to the terms and conditions of the loan agreement, as well as for identifying aspects which violate his or her interests at every stage of the loan process. Customer awareness is related to the person's knowledge of finance. As revealed by PwC's analysis presented in the chapter entitled „Market and its participants", there are no significant differences in education or place of residence between household members taking loans from personal loan companies and those indebted to other institutions.

With those assumptions in mind, and taking into account the results of other analyses, the following aspects were found to be key determinants of a customer's informed participation in the loan process:

- Customer's education and social awareness related to the financial market;
- Customer's awareness of his or her rights as a consumer;
- Proper access to the information about the product and the terms and conditions of the loan agreement at the stage of making a borrowing decision.

The above conditions were adopted as a basis for the Mystery Shopper study, during which the following questioned were raised in respect of the customer's responsibility area:

- Is the requirement of completeness of information published on the website and included in the loan agreement a sufficient condition to ensure that the terms and conditions of the loan are clear and understandable for a customer?
- Is the publicly available information sufficiently complete and reliable for the customer to make the best possible decision?

Detailed results of the study

Finding 1: Completeness of the information included in the loan agreements covered by the study is not sufficient to guarantee legibility of the overall terms and conditions of the loan. On that basis, the customers may still lack understanding of all risk related to the selected offers. The study revealed that very often the customers do not understand the concept of APR and in some cases are not able to determine the real costs of the loan.

Practices noted during the Mystery Shopper study:

- The respondents who used services of lenders from all three segments were aware of the loan amount and the term of the loan.
- The loan agreements signed by the respondents included a reference to APR. In one

case only ARP was not quoted despite the fact that the agreement contained a special field for that purpose, which was a violation of the applicable law.

- Despite the possibility to get familiar with the loan documents, most of the respondents were not able to determine the value of APR specified in the loan agreement. Estimating the correct value was problematic for customers of all three segments.
- The customers also found it difficult to calculate the total amount payable to the lender. In that case, consumers from Segments B and C proved most knowledgeable as opposed to Segment A consumers; the latter did not know what the payable amount was or were not able to estimate it correctly in any of the cases.

Evaluation of the responses provided by the respondents to the questions about understanding the features of the loans contracted during the Mystery Shopper study ("+" - most of the responses true; "-" – most of the responses not true).

Segment	APR	Final amount payable	Loan amount	Loan term
A	-	-	+	+
B	-	+	+	+
C	-	+	+	+

Source: Own work based on the results of the Mystery Shopper study

Specific financial indicators used for describing the products and included in the loan agreements (such as APR) may be too complicated and difficult to understand for an average customer. As the terms may not be fully understood by the borrowers, this may create certain risks while making a decision to take a loan or when assessing suitability of a product offered to the customer for the actual financial needs and capacities.

The study confirmed that customers often lack understanding of the real costs of the loan. The marketing communications presented online or through the representative do not always provide the consumer with the required knowledge necessary to make an informed credit decision.

Finding 2: To protect his or her best interests, the customer should be aware of which information is important and what he or she needs to know in the loan process. The information found on the website or provided by the lending company's representative may be insufficient.

Practices noted during the Mystery Shopper study:

- Marketing communications found on the websites of some of the Segment A and B companies did not include concrete product offers with description and calculations of parameters prepared for a representative example. This makes it more difficult to compare offerings of various lenders or verify provisions of loan agreements.
- A great number of lenders covered by the study failed to present their offering in a sufficiently transparent manner. Potential borrowers who relied only on the available marketing information get very little knowledge about the offered products and services. The lender often fail to present all types of fees or additional obligations involved in the loan process, e.g. the obligation to sign the loan insurance agreement or pay the home service costs.
- All other companies from the three market segments that included in their marketing communications a representative example, the APR value, the loanamount, the final amount payable and payment term on their website used the same terms and conditions in the loan agreement signed later with the customer.
- Marketing communications of some of the companies from Segments A and B included in the study lacked information on all costs related to the loan process, e.g. upfront fees. In most of the cases the respondents learned about those costs from the website or during the meeting with the sales representative.
- Marketing communications of some lenders included misleading information about the scope of the lender's product and services.

GOOD PRACTICE

Positive examples observed during the study included personal loan companies which offered special loan calculators for potential customers to calculate most of the loan costs, and presented additional obligations of borrowers in their marketing communications.

3.4. Service quality: providing information about the product and customer service standards

Objectives of the analysis

An important area in the lending process is the space on the interface between the customer and the lender represented by the sales representative while interacting during a sales meeting (if applicable), or at the stage of negotiating the final terms and conditions of the agreement, signing and executing the agreement and closing the loan process (in this case, withdrawal from the agreement). Within this area, the key to responsible lending process is providing product information and ensuring an appropriate standard of service adapted to the profile and needs of the customer.

Currently, there are little or no studies in the Polish market that would present in detail the profiles of the customers of personal loan companies. Based on the review of the lenders' business models, available products and services, as well as the results of analysis and publicly available information, one can see that profiles of customers of lending companies from different segments are different as well, and the common trait of all customer groups is the demand for readily available funds.

On that basis, differences are revealed in terms of:

- Having a bank account (not all customers of personal loan companies have one);
- Access to internet;
- Age;
- Being a private individual or a legal entity.

The study leads to a conclusion that the most informed group of customers are Segment C customers as they have certain experience in using the services of financial institutions; they use electronic banking and, as revealed in the course of the Mystery Shopper study, are aware of the implications of signing a loan agreement, at least to a certain degree.

Considering the above, the following aspects were found to be key determinants of responsible provision of information about the product and the quality of the customer service:

- Responsible approach to selling and ethical behaviour of sales representatives;
- Ensuring that efforts are taken to maintain high standards and best quality of customer service regardless of customer types;
- Flexibility of the service and adapting to the needs of various customers;
- Ensuring reliable and complete communications concerning the product and the terms and conditions of the loan agreement.

These conditions were adopted as a basis for the Mystery Shopper study, during which the following questioned were raised in respect of the service quality area:

- In what way does the customer service process ensure that the customer signs the agreement in an informed manner?
- In what way does the customer service process ensure that the customer learns about his or her rights and obligations as well as the terms and conditions of the loan provided for in the loan agreement?

Detailed findings

Finding 1: In the studied cases, the customer service process when granting the loan was not always consistent within one company despite the adopted standards and operation procedures. It often depended on the individual behaviour and attitude of the sales representative and on his or her knowledge.

Practices noted during the Mystery Shopper study:

- Differences were observed in the quality of contacts with sales representatives during the lending process in all three segments.
- While reviewing respondents' views about the first contact with sales representatives of Segment A and B lenders, two major opinions were noted:
  - The first group included numerous positive views on a sales representative's professional approach and extensive product knowledge, as well as good relationship built with the customer during the meeting.
    "The representative was very nice to me. He informed me of the related charges, and contacted me shortly after I made an enquiry on the website."
  - The other group of respondents showed a different, more negative approach to the situation. Those respondents mentioned difficulties in contacting the representative, hurried visits and lack of accurate and complete information about the loan from the representative.
    "He was in a hurry; he filled in the form twice and hardly spoke to me."
    "The representative did not introduce himself and gave only perfunctory information."
    "To me, the representative wasn't professional, he didn't even take the documents and made an impression of being a know-it-all kind of guy."

Finding 2: The study showed that respondents did not always carefully read the loan agreements and sometimes had trouble understanding the terms and conditions of the agreements. Moreover, the study suggests that contact with the lender's representative is not always helpful when it comes to understanding the terms and conditions of the agreement. Such a situation increases the risk of the consumer failing to make a fully informed decision.

Practices noted during the Mystery Shopper study:
During discussions (if any) of the terms of the loan, customers were not given the whole information about the process. It seems that they may not be aware of the whole risk involved in signing the loan agreement.

- All respondents received the loan agreement in written form.
- The respondents admitted that they only had a cursory glance at the agreement. "I read it cursorily. The representative did not discuss the text of the agreement at all."
- At the meeting with the lender's representative (in cases where the customer service model provides for such a meeting) and during discussions about the loan agreement initiated by the representative, the customer's attention was usually drawn to the following issues:
  - Repayment amounts;
  - Repayment schedule and method;
  - Total amount to be repaid.

  Sometimes, the following issues were also discussed:
  - That the loan agreement was based on standard terms and conditions;
  - Term of the loan;
  - Loan amount;
  - Option to return the loan within X days;
  - Additional costs to the borrower;
  - Interest rate;
  - Upfront fees;
  - Home service costs.
- In most of the cases, when learning about the loan process the respondents also learned what to do to withdraw from the loan agreement – usually it required filling in an appropriate form, contacting the representative and repaying the whole loan.
- The customers did not always have an opportunity to have any unclear provisions of the loan agreement explained.
- There was a case in Segment A when the customer asked about a possibility to make repayments through bank transfers and learned that home collection service required fewer formalities. The respondent did not say whether the costs of the two options were explained to him on that occasion.
- In most cases, Segment A and B representatives did not mention the risks involved in the repayment process. Few representatives from Segment A companies informed the respondents about the consequences of untimely repayment.
- The early repayment option was communicated to some of the respondents only. In such cases, they were also informed that early repayment reduced the total cost of the loan.
- Only in few cases were the respondents informed about the complaint procedure.

Finding 3: In some cases, the original loan amount was increased during the meeting with the customer.

Practices noted during the Mystery Shopper study:
All respondents were required to submit an application for a PLN 500 loan. A vast majority of the customers who got their applications accepted, were also encouraged to take advantage of other lending possibilities offered by the company – this usually meant increasing the loan amount. The highest loan amount offered to a respondent was PLN 4000, which was 8 times more than what was originally requested (in the end, the respondent borrowed just PLN 500). Other examples included a proposal to extend the loan term against a fee and a reward for motivating other people to use the lender's services.

Case study

A respondent was forced to ask for a higher than originally planned loan. He filled in a loan application form for PLN 500 for an 18-week repayment term. The application was accepted and the customer met the lender's representative. During the visit it turned out that to receive PLN 500 in cash, the customer has to take a PLN 700 loan. This is because the company collects the first repayment upon signing the loan agreement. In this case, the first instalment was set at PLN 200, therefore the original loan amount had to be increased. In the end, the respondent received PLN 500 in cash, while the amount of PLN 700 was put into the loan agreement as the amount to be repaid over a 25-week term.

Finding 4: During the study, other aspects and activities of personal loan companies were identified, which are a result of the asymmetric relationship between the lender and the borrower.

Practices noted during the Mystery Shopper study at the stage of inquiring about and declaring interest in the consumer loan

Case study

One respondent, who had already submitted the application, could not reach the lending company by phone; moreover, he did not find the company's offices at the indicated address.

Response of the lending company's employee: "You have to keep calling until someone answers the phone."

Case study

When completing an online application, one respondent was asked for his user name and password to the internet bank account.

Practices noted during the Mystery Shopper study at the stage of negotiating the offering as well as the final terms and conditions of the loan:

Case study

To our question "What information about the loan repayment process did the representative provide?", the respondent answered: „The information was scarce – just that the repayments were collected weekly and the fee for the 4 repayments was charged in advance for the convenience of both parties." Moreover, when asked about the possibilities to make repayment through a bank account, the representative said that such form of repayment required more formalities and suggested that home collection was a better option. This was not only misleading, but also inconsistent with the terms and conditions of the loan agreement.

Case study

Another example of activities inconsistent with the terms and conditions of the agreement was collecting the fee during receipt of the application (a couple zloty) without issuing any receipt to the customer.

Practices noted during the Mystery Shopper study at the stage of signing and executing the loan agreement:

Case study

In one case, the representative of the lending company collected the first repayment 2 days after signing the loan agreement (the respondent did not receive the repayment schedule or documents enabling her to withdraw from the agreement):

"The representative told me that she would collect the first repayment next Monday. When I asked her what was the reason for coming so early – it was Saturday evening – she just said that unfortunately that date was fixed in the repayment schedule."

Practices noted during the Mystery Shopper study at the stage of withdrawing from the loan agreement:

- Only some of the respondents were informed by the representative or learned from the website that the agreement withdrawal form is an integral part of the main agreement. Such information was lacking in the case of Segment B companies. On the other hand, many of the respondents in Segments A and C were informed about such a document.
- Similar opinions were gathered with regard to informing the customers about the whole process of withdrawing from the loan agreement. Again, representatives of Segments A and C lender made the customers aware of the procedure, while Segment B representatives did not.

Case study

One respondent had to ask the representative for the agreement withdrawal form.

"But I didn't get the repayment schedule, or the agreement withdrawal form, so I asked specifically for the form. I was told that the form would be delivered the following week."

Case study

Discussion with the representative about withdrawing from the loan agreement:

"First, the lady from the office informed me that I had to repay the whole amount plus the commission, the whole interest, additional charges, upfront fee, and home service fee. When I protested and quoted para. 28 of the loan agreement, she told me to repay only the money that I actually took."

In the examined cases, despite the adopted customer service standards and operating procedures, the loan processes within one company were not always conducted in a consistent manner. The quality of the customer service often relied on the individual behaviour, attitude and knowledge of the sales representative.

Moreover, the study revealed that respondents often failed to read agreements with appropriate care, and were not always sufficiently aware of the terms and conditions of the loan. In addition, it seems that the contact with the representative of the lender is not always helpful in terms of understanding the provisions of the agreement. All these may increase the risk of making an uninformed decision by consumers.

There were cases where during the meeting with the customer, the initial loan amount was increased.

4. Analysis of the systems regulating operation of personal loan companies in Poland and abroad: best practices

The objective of this chapter is to discuss regulations in the personal loans market in Poland and abroad. Comparison of the regulatory systems in various jurisdictions should enable identification of the existing institutional measures and good market practices; as a consequence, changes in the existing regulations may be proposed.

In Poland, personal loan companies, like any other enterprises, are required to comply with the generally applicable laws and regulations. They are subject both to the provisions of the Polish Civil Code[10] ("CC") (including in particular Chapter XIX introducing the institution of a loan, and provisions concerning the maximum value of statutory interest), and the Commercial Companies Code[11] to the extent that they operate as a partnership or a joint stock/limited liability company. They are also subject to the Act on Freedom of Business Activities within the framework of their professional activities[12], and the key provisions of the Consumer Credit Act. Like any other entities, personal loan companies are also subject to the supervision exercised by the General Inspector for Personal Data Protection with regard to protection of personal data, and General Inspector for Financial Information with regard to obligations related to preventing money laundering and terrorism financing[13].

10. The Civil Code Act of 23 April 1964 (Journal of Laws 1964 no. 16 itme 93, as amended.)

11. Commercial Companies Code Act of 15 September 2000 (Journal of Laws 2000 no. 94, item 1037 as amended)

12. Act on Protection of Personal Data of 29 August 1997 (Journal of Laws 1997 no. 133 item 883 as amended)

13. Act on Preventing Money Laundering and Terrorism Financing of 16 November 2000 r. (Journal of Laws 2010 no. 46, item 276, consolidated text, as amended)

4.1. Licencing and supervision

Currently personal loan companies are not required to obtain a licence if their activities do not involve collecting funds from customers and exposing them to risk[14]. Lenders than are neither bank nor credit institutions, whose core business consists in providing loans to their own account, are classified by the Banking Act to the broad category of financial institutions. Other institutions in that category include leasing companies, asset management companies, and payment institutions. Also in the EU regulations, both the directives[15] and the regulations of the European Parliament and of the Council directly applied by member states, personal loan companies that meet the aforementioned criteria are not covered by prudential regulations, unlike banks.

From the institutional perspective, the regulatory and control powers of FSA defined in the Act on Financial Market Supervision and to some extent in the Banking Act (with regard to banks) do not apply to personal lending companies[16]. As there is no requirement to maintain a register of personal loan companies, their activities are not regulated or supervised in a way comparable to banking activities.

In the public debate in Poland, some are of the opinion that applying regulatory supervision to personal loan companies or registration of such entities will increase safety of the trade[17]. Many circles believe[18] that expanding control competences of state authorities and authorising them to demand explanation from lenders who are suspected of non-compliance with the current laws will improve the discipline in the personal loan market, which, combined with the market transparency ensured by a register of companies, will increase the safety of customers using the services of personal loan companies. At the same time, it should be considered whether the focus should be on developing additional

14. The definition of a credit institution(and its local Polish equivalent such as bank in the light of the classification adopted in the Banking Act) includes the following key elements: taking deposits or other repayable funds from the public and granting credits for its own account (Art. 4(1)(17) of the Banking Act and the relevant provision of Art. 4(1)(1) of the Regulation of the European Parliament and the Council no. 575/2013 of 26 June 2013 r. on prudential requirements for credit institutions and investment firms, amending Regulation EU no. 648/2012), which become effective on 1 April 2014.

15. Especially in the key Directive of the European Parliament and the Council no. 2013/36/EU of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC detailed regulations or on strengthening the instruments for enforcing the existing law.

Such regulations are used in many European countries; therefore the concept is already reflected in the existing legislative systems.

Approaches to the mandatory registration of personal loan companies and subjecting them to state authorities' supervision are different in different EU countries. In this respect, there are two basic groups of countries.

The first group consists of countries which decided not to have separate regulations for the market – such as Poland, Czech Republic or Spain. In those jurisdictions, the operations of personal loan companies are regulated to the same extent as any other professional business activity. Lending companies in those countries are also subject to consumer loan regulations[19], usually transposed from Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers to the extent that such companies provide consumer loans, and, on general terms, by consumer protection regulations.

Both in the EU and on a global scale, there are differences in approaches to supervision over personal loan companies, both with regard to the aspects of conduct of business as well as the aspect of prudential supervision. Lenders in some countries are subject to full supervisory regime under the financial supervision system (e.g. Germany or Italy); whereas in other countries they are subject to partial supervision (UK) or general conduct of business supervision (Poland).

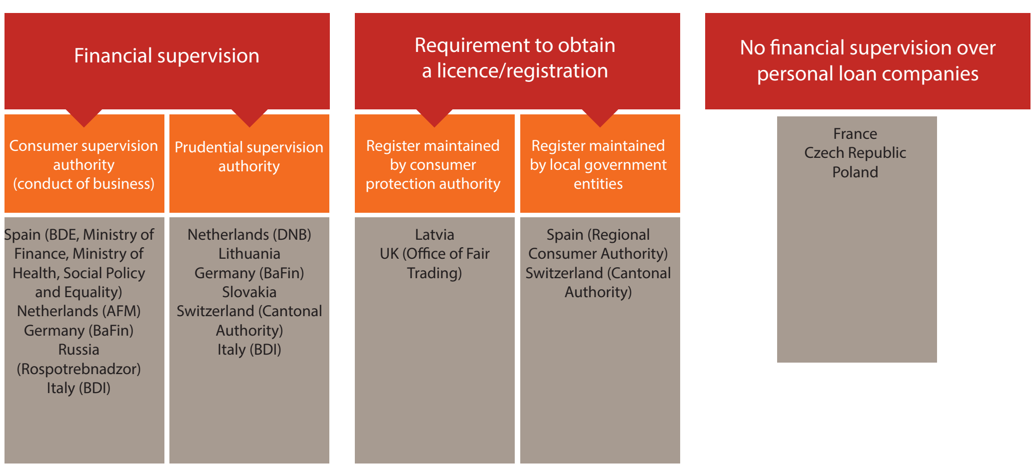
The group of countries that decided to introduce detailed regulations of the personal loans market, two distinct approaches to regulation are noted.

The first approach relies on subjecting personal loan companies to financial supervision in the same way as it is done with regard to banks. In some countries, e.g. Germany, this is because granting a loan is treated as a banking activity, therefore there is no reason for leaving personal lenders outside the financial supervision system[20]. It should be noted that both the German and Italian models (which also provides for direct banking supervision of personal loan companies) does not leave any room for the activity of companies that do not meet the requirements for entities that provide banking services. The purpose of such restrictive approach is to increase safety of the consumers; however, as a side effect, this may spur development of grey economy lenders.

In countries which adopted such a model of regulation, personal loan companies are either controlled by a separate financial regulator (Germany and Italy), who often supervises the whole financial market (in terms of conduct of business, prudential supervision or both), or by a consumer protection office in the country (on general terms, as in the case of any other company), which is the case in Poland and Czech Republic.

Switzerland adopted a slightly different solution where operations of personal loan companies are not subject to financial supervision; however, each such entity must be registered. The competent authorities to maintain registers of lenders are respective

Chart 14. Licencing and supervision over personal loan companies in selected European countries as of 27 November 2013[21]



16. Act on 21 July 2006 on Financial Market Supervision (Journal of Laws 2006 no. 157 item 1119 as amended)

17. See e.g. the report of Fundacja Republikańska entitled Problematyka regulacji rynku firm pożyczkowych w Polsce (Problem of regulating the

18. Ibidem

19. Act of 12 May 2011 on Consumer Loan in Poland.

20. Pursuant to Directive 2006/48/EC effective until 31 December 2013, and Directive 2013/36/EU of the European Parliament and of the Council, and Regulation of the European Parliament and of the Council (EU) no. 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms, effective from 1 January 2014, a personal loan company financed through own funds does not meet the key criterion of a credit institution, i.e. taking deposits or other repayable funds from the public.

21. PwC's analyses and the report entitled Consumer Finance Protection with particular focus on credit, Financial Stability Board 2011

cantonal authorities in cantons where the entities conduct their operations.

A different solution was also adopted in the UK where the competent body to issue licenses for conducting consumer loans and credits is Director General of Fair Trading[22]. This is also a supervisory body authorised to impose financial penalties on entities that fail to comply with the provisions of the Consumer Credit Act[23].

Differences in the adopted legislative measures related to the licence requirement and supervision over lending companies result from different approaches to financial market supervision and differences in the legislative systems. Many markets show a tendency to apply special regulations to personal lending business in order to improve safety of trade and protect the interest of the consumers (conduct of business) with different approach to prudential regulation.

Planned amendments to Polish legislation:

The government's proposal on the draft amendments to the Act on Financial Market Supervision[24] provides for two regulatory changes in the area of supervision as well as in the licencing requirement. Firstly, it proposes to extend FSA's supervision over all institutions operating in the financial market. FSA's authority in general would allow it to request explanation from the financial market operators if there is a suspicion that their operations violate the applicable law. The planned amendment also provides for stricter criminal sanctions for conducting banking activities without an appropriate permission. If FSA's powers were expanded to cover personal loan companies, criminal sanctions would apply also to such entities. However, the government's draft lacks detailed information on what sanctions are to be tightened and how, therefore the question of personal loan companies being covered by such sanctions is purely hypothetical.

The second aspect is a proposal to create a separate register, the entry to which would be mandatory for entities conducting activities such as providing loans to consumers. This would result in the activities of personal lenders loan companies becoming regulated activities pursuant to Art. 64(1) on the Act on Freedom of Business Activity. According to the proposal included in the government draft, the register would be maintained by the Chairman of the Competition and Consumer Protection Office. The adopted catalogue of requirements to be met by companies in order to be entered to the register is to ensure transparency and stability of the trade in the lending sector, as well as better consumer protections. One of the requirements is that the persons conducting activities consisting in providing loans must have no criminal record; there are also requirements regarding the age of such persons and the minimum level of initial capital (share capital in the case of joint stock or limited liability companies) required to start the lending business (currently, the government draft includes PLN 60,000 as the minimum level of share capital).

22. Office of Fair Trading, http://www.oft.gov.uk/

23. The Consumer Credit Act 1974

24. Assumptions to the draft act amending the Act on Financial Market Supervision, Banking Act and certain other acts (draft no. ZD74 of 27 June 2013)

The legislative systems of European countries offer different approaches to the question of licencing the activities of personal lenders, or covering them with banking supervision. The adopted solutions include either strict regulation by central banks or regulatory authorities, introduction of registers and licenses maintained by consumer protection offices, or lack of regulation of that type. The important thing is that the countries where the market of term loans is not regulated have a public debate about the need to regulate the market of personal loan companies.

The amendments proposed to the Polish law provide for a balanced approach: by combining some of the supervisory powers of FSA with the mandatory entry to a register maintained by the Competition and Consumer Protection Office, it offers a compromise between the supervisory model and the licence-based model.

4.2. Annual Percentage Rate limits

The Annual Percentage Rate (hereinafter "APR") is a statutory rate used in Poland to define the characteristics of the credit[25]. APR defines the total cost of the credit paid by the consumer, expressed as an annualised percentage value of the total loan amount. APR is calculated in the same way as the internal rate of return, which is used to calculate the economic efficiency of an investment project. The purpose of using APR as an indicator is to enable customers to compare offerings of various lenders. However, as showed in the Mystery Shopper study in this report, consumers have difficulties in interpreting the real value of APR, especially in the case of loans with the shortest terms. Calculation and verification of APR is even more difficult.

25. Art. 5, 25 and Appendix no. 4 to the Act on Consumer Credit

Different approaches to APR limits:

Switzerland: statutory limit of 15%
Lithuania: statutory limit of 200%
France: statutory limit: no more than 1/3 over the average interest rate adopted by the Central Bank
Germany: limit of 200% established by way of case law
UK, Denmark, Spain, Poland, Sweden: no statutory limitation of APR

Attempts to regulate the APR limit are usually justified by the intention to establish the maximum amount of the costs and charges added to the loan or credit in order to protect the interest of the consumer against usury: an excessive and disproportionate interest rate. This argument is brought up when the cost of the loan seems to deviate from the market rates, and the additional costs substantially exceed the reasonable charges justified by the range of provided services; at the same time, the customer is unaware of the actual costs to be paid over the originally borrowed amount.

In the current legal circumstances in Poland, the legislator did not limit the maximum amount of APR. The only limit applied is the limit of the interest arising from a legal act, defined in the civil code. Pursuant to the definition contained therein, the amount of due interest must not exceed four times the amount of the NBP's lombard credit interest rate[26].

The absence of a statutory definition of the APR limits is in line with the prevailing trends in the European financial markets. The APR limits have not been specified by the legislators in the UK, Denmark, Spain or Sweden. The same applies to Germany, Czech Republic and Slovakia; however, in those countries the APR limits were established through court decisions, and appropriate recommendations were developed for APR limitations, which are respected by most companies.

The countries that adopted the statutory limitation of APR include Switzerland and Lithuania. Interestingly, these countries have different limits: Switzerland adopted the ARP limit of 15 %, while in Lithuania the limit is 200%.

26. Art. 359(2)[1] of the Civil Code

Planned amendments to the Polish law

In Poland, two draft amendments to the personal loan market regulation were developed[27]. The idea of the amendments is to limit the **total costs of the loan reflected through APR**. Initially, the government draft provided for an upper APR limit established with the use of the multiplier such as NBP's lombard credit rate; the proposal was severely criticised during the social consultation process.

27. The government's proposal on the assumptions to the draft act amending the Act on Financial Market Supervision, Banking Act and certain other acts (draft no. ZD74 of 27 August 2013) and draft amendment to the Act on Consumer Credit developed by the Law and Justice Party, available on www.pis.org.pl

Consequently, the current draft does not introduce the APR limit; instead, it proposes **a limit on the total cost of the credit, excluding the interest, referring to the cost of the actually provided consumer credit.** According to the draft regulation, **the total cost of credit defined in the Act on Consumer Credit[28], excluding the interest, may not exceed 30% of the amount of the consumer credit.**

28. Art. 5.6 of the Act of 12 May 2011 on Consumer Credit (Journal of Laws of 2011 no. 126, item 715)

The second draft amendment to the regulations on interest rates of loans and credits granted to consumers has been developed by one of the parliamentary clubs. Unlike the government draft, it does not set one limit for the total cost of the loan other than the cost of interest. Instead, it limits the value of the individual ARP components: the cost of fees and commissions are limited to 5% and 0.75% of the loan value for every week from the moment of disbursing the funds until the final repayment. The above limits are added up. Adopting such a model will lead to a situation where the total value of additional credit cost cannot exceed 44% during a year (5%+0.75% * 52 weeks). What is important, the total amount of the costs limited in this way would not include additional costs arising from non-performance or improper performance of the agreement by the borrower, unless the credit representative expected the borrower to fail to repay the liability.

Both drafts have a similar objective, although attained with different techniques. The Ministry of Finance's draft postulates establishing a limit on non-interest costs to complement the limit on the interest costs already existing in the Civil Code, based on a simple formula and clearly defined threshold value. On the other hand, the draft submitted by one of the parliamentary clubs wants to achieve the same goal of limiting the excessive non-interest costs for the customer, but the proposed formula links the maximum value of the commission not only to the loan amount (as in the government's proposal), but also to the term of the loan (unlike the government's proposal). Such a formula promotes loans of a shorter term, where charges would be relatively small compared to loans with longer maturity.

European regulations are not uniform either with regard to statutory limitations of the APR level or the approach to the APR calculation model. Both Polish draft amendments of the laws take notice of the need to regulate that issue; however, they are not consistent with regard to the assumptions as well as the methods of calculation of the upper APR limit. Developing an algorithm which would ensure consumer safety without giving precedence to any specific business models at the expense of others, is a real challenge for the legislator.

4.3. Regulations concerning liability to consumers

In the preceding subchapters, we presented the regulatory aspects of the personal loan companies in the prudential supervision area as well as in the area of limiting the cost of the loan, which are currently the subject of the public debate as well as of the proposed amendments of Polish legislation. To get a grasp of a full picture of the regulatory environment in which the lenders currently operate, we should have a closer look at the regulations in the area of consumer protection.

Like all other companies, personal lenders are subject to the supervision of the Chairman of the Competition and Consumer Protection Office to the extent that their activities may harm interests of consumers or pose a risk to market competition. As the share in the financial market held by such companies is rather small, they do not create any real risk of violating rules of competition or creating a monopoly in the loan segment. On the other hand, protecting consumer interest is a valid question in the context of operation of lending companies.

A. Forbidden contractual clauses

The Chairman of the Competition and Consumer Protection Office maintains a register of the so-called forbidden contractual clauses with sample agreements found by the Office to be inconsistent with the law (violating collective consumer interests). A number of clauses in the loan and credit agreements lack transparency. The Chairman assessed many times the provisions that build asymmetrical relations between the creditor and the borrower, the possibility of making arbitrary changes in the methods of calculating the costs or limiting the option of earlier repayment of a loan. Pursuant to the Act on Protection of Competition and Consumers[29], the Chairman of the Competition and Consumer Protection Office may impose a financial penalty on the business entity in the amount not exceeding 10% of the income for preceding financial year, if the company committed (even unintentionally) an act that violated the collective consumer interests, which also includes using forbidden contractual clauses.

29. Act of 16 February on the Protection of Competition and Consumers (Journal of Laws 2007, no. 50, item 331)

B. Acts of unfair competition in the lending practice of lenders

Moreover, personal loan companies (like banks) must follow the provisions of the Act on Combating Unfair Competition[30], in particular the provisions forbidding the use of misleading advertising in order to influence a customer to buy a certain service or providing misleading product or service information (in particular by concealing information about the service or the risk involved in purchasing the service). Pursuant to the Act on Combating Unfair Competition, claims for violation of the Act are made under the civil law, but actions can be brought to the court not only by another company or consumer, but also the Chairman of the Competition and Consumer Protection Office.

Apart from respecting the provisions of the Act on Combating Unfair Competition, personal loan companies must follow detailed regulations regarding lenders' responsibilities with regard to advertising, specified in the Act on Consumer Credit[31]. According to these regulations, creditor is required to inform the customer of the loan interest rate and the charges included in the total cost of the loan, the total loan amount, the ARP value, and, when applicable, the total amount payable by the consumer, the repayment amounts and the duration of the loan agreement. Moreover, in the light of the Act on Consumer Credit, advertising used by the personal loan company may not suggest that the no credit assessment is required, as performing such an assessment is one of the lender's obligations under the Act.

30. Journal of Laws 1993 no. 47 item 211, Act of 16 April 1993 on combating unfair competition

31. Act of 12 May 2011 on Consumer Credit (Journal of Laws 2011 no. 126, item 715)

C. Key responsibilities of the lender towards the consumer

Before signing the agreement, the personal company lender should conduct a customer credit risk assessment. This is done on the basis of the information received from the consumer or included in the lender's database. If the lending company will have to refuse the loan after such assessment, it must inform the consumer free of charge about the database in which the customer credit risk was reviewed.

Before granting a loan, the company is also expected to explain to the consumer the terms and conditions of the loan agreement; the consumer must be able to make a decision about signing the agreement. If the result of the credit risk assessment is positive, the consumer may also ask for a draft version of the loan agreement, which should include the consumer's details and all terms and conditions of the prospective loan. To ensure that the consumer gets all the necessary information about the loan agreement, a standard information form has been introduced. The form is attached as Appendix to the Act on Consumer Credit. The obligation to fill in the form in a correct way lies with the lenders and credit intermediaries. The form must include the following information:

- Details of the creditor and credit intermediary (if any);
- Type of credit;
- Term of the credit;
- Credit interest rate (and conditions of interest rate change);
- Total amount of the credit;
- Annual Percentage Rate;
- Total amount payable by the consumer;
- Rules and terms of credit repayment;
- Requirement to sign an additional agreement (if applicable), in particular the insurance agreement;
- Interest rate applicable to overdue debt;
- Consequences of non-payment;
- Required collateral for the consumer credit (if applicable).

An important question is the validity of the information form. Although the act does not specify when such form should be provided, the information should be provided to the consumer early enough before signing the agreement to enable the consumer to read the terms and conditions of the loan and its costs, and compare them with those offered by other lenders. To enable the consumer to make an informed decision, the form should be valid for at least 3 business days.

Pursuant to the Act on Consumer Credit, the personal loan company must ensure that the loan agreement includes detailed information about the parties to the agreement, duration of the agreement, rules and dates of repayment, and any fees and costs charged by the company (the detailed information to be included in the agreement are specified in Article 30 of the Act). Along with the agreement, the customer should also receive the agreement withdrawal form.

The key responsibilities of personal loan companies are presented above. The Act on Consumer Credit defines each responsibility in detail to guarantee the highest possible consumer protection level.

Proposed amendment to the law: As mentioned before, the government proposal on amendments to the Act on Financial Supervision and certain other laws is based on the assumption that the register of personal loan companies will be maintained by the Chairman of the Competition and Consumer Protection Office. Therefore, apart from the existing supervision of compliance with the consumer protection regulations, including monitoring of abusive clauses, the Office will be charged with an additional duty of "quasi-licencing", i.e. registration of personal loan companies which intend to provide services to consumers. Such a solution is used in other legislative models – for example, the activities of lending companies in the UK are regulated in this way[32].

32. Source: Office of Free Trading – Payday loans compliance review: http://www.oft.gov.uk/OFTwork/credit/payday-lenders-caompliance-review#.Uos3NMTkuPw

The European countries quoted above have developed mechanisms for consumer protection also in the financial market. There are differences with regard to the issue of the powers granted to consumer protection offices in the context of maintaining a register and issuing licences to companies intending to provide lending services. The proposed regulatory changes in Poland assume that such powers will be granted to the Competition and Consumer Protection Office in the spirit of the British model.

4.4. Debt recovery

The question of recovery of debts is an important aspect of lending companies' operations. However, it should be remembered that the debt recovery regulations are defined by the Code of Civil Procedure and there are no specific regulations applicable to the industry.

Generally speaking, debt recovery is a process where liabilities related to a product sold or a service provided are being recovered. The objective of the debt recovery process is to obtain payment from the debtor as soon as possible and with the use of minimum financial and organisational means.

Effective recovery of the debt from the debtor is possible only when the debt matures, i.e. after the repayment date. First, the debtor should be called to pay – he or she should be informed of an additional repayment term. This stage of enforcement is often called "amicable enforcement" or "soft collection"[33]. In reality, loan companies often send reminders, calls to pay and payment demands to the debtors, as well as make reminding phone calls, for which the debtor is additionally charged. The amount of the charges is the subject of the current public debate. Amicable enforcement methods also include mediation or negotiations with the debtor, the purpose of which is to persuade the debtor to repay the liability without bringing the case to the court.

When the loan company has exhausted the soft recovery methods (according to the current law, it is sufficient to send a payment reminder specifying the payment date), the case may be brought to the court. It must be remembered that enforcement will not be effective if the liabilities are statute-limited. If the period of limitation has expired, the debtor may decline repayment of the debt. This means that during the enforcement proceedings, the debtor may raise a charge of the statute of limitations and refuse to pay the debt, while the creditor cannot force him or her to make the payment. In such a case, the claim does not expire but becomes a so called natural liability, the payment of which depends solely on the good will of the debtor. If no statute of limitations is raised, the court will issue a judgement after expiry of the statute of limitations. When a case is brought to the court, the company may also demand payment of statutory or contractual interest. After obtaining the favourable and final court verdict, it becomes an enforcement order, to which the court appends a title of execution and which may be then enforced. In this respect, personal loan companies are in a worse position than bank which can issue a bank enforcement order.

The next step is to applying to the enforcement officer with a request to initiate the enforcement procedure and carry out the execution from the debtor's assets. The enforcement proceedings are conducted by the enforcement officer, who summons the company to make advance payments towards the costs of the enforcement proceedings, which are later charged to the debtor.

The lender who wants to recover the debt may take advantage of a number of instruments, either as part of amicable collection or court recovery, or recovery against a warrant

33. K. Turaliński, „Windykacja Gospodarcza – podręcznik do nauki zawodu" (Business debt recovery: job manual), Wydawnictwo Ardius, Warsaw, 2010 of execution. The selected method of debt recovery depends on the loan company. However, one should bear in mind that even when the procedure is conducted on the basis of an enforcement title or a warrant of execution, the due amounts may not be recovered. Very often enforcement procedure has to be discontinued due to insolvency of the debtor. Therefore the appropriate customer risk assessment is so important, as it will protect the lender against high costs of the court and enforcement proceedings in situations where there are very low chances that the debtor repays the loan as well as the other costs.

Currently, there are no regulations that would specifically regulate the methods of enforcement applied by companies. The Competition and Consumer Protection Office uses the available legal instruments (such as actions for cessation of practices violating collective consumer interests) in cases when the paid reminders are sent to debtors automatically and without assessment of their individual circumstances[34].

Debt recovery activities are not included in a catalogue of aggressive and unfair market practices pursuant to Art. 9 (2) and (3)[35] of the Act on Combating Unfair Market Practices[36]. This reduces the possibility of recognising some of the recovery practices as aggressive or misleading. A market practice is considered aggressive if it involves an unacceptable pressure which may influence the consumer's decision, also after signing the agreement. In particular, when assessing the operations of the company, things such as threats to use illegal measures or use of offensive expressions or behaviour will be taken into account, as defined in Article 8 of the Act. In the current legal circumstances, using aggressive practices in respect of a consumer is subject to a fine[37].

34. This was the case in one of the banks, where reminders were sent automatically by the system. The consumer had to pay additional debt recovery charges even if he was late with the payment by one minute.

35. In any circumstances unfair market practices are the following aggressive market practices:

- *Paying visits at the consumer's place of residence, even if the consumer does not intend to stay there permanently; ignoring the consumer's requests to leave home or stop the visits, with the exception of enforcement of contractual obligations to the extent allowed by the current regulations;*
- *Burdensome solicitation, not caused by any act or omission of the consumer, to purchase products by phone, fax, electronic mail or other means of telecommunication, with the exception of enforcement of contractual obligations to the extent allowed by the current regulations.*

36. Act of 27 August 2007 on Combating Unfair Market Practices (Journal of Laws no. 171 item 1206 , as amended)

37. Article 15 of the Act on Combating Unfair Market Practices

The debt recovery process is regulated in the code of civil procedure and applies equally to all entities participating in civil law transactions. The Act on Combating Unfair Market Practices introduces mechanisms which the consumer may use to protect himself or herself against aggressive debt recover practices. Exerting pressure on the consumer may be decided by the court to be a violation of the existing law and lead to a fine.

Table 5. Overview of regulatory practice in selected European countries

	Banking supervision / registration requirement	APR limits	Consumer protection
Germany	Operations of personal lenders are subject to financial supervision (BaFiN), both in terms of conduct of business and prudential supervision.	There is no statutory limit; the allowed limit is set at 200% based on court decisions	Companies are supervised by a consumer protection authority with the entitlements based on those defined in the EC directive to ensure that they follow fair market practices (with regard to advertising, providing information and detailed contractual provisions).
UK	Operations of personal lenders are regulated by the Office of Fair Trading, which also runs an appropriate register.	No	The Office of Fair Trading maintains a register of lending companies and is authorised to control their activities and impose penalties for non-compliance.
Switzerland	Operations of personal lenders are not subject to banking supervision, but the companies must register in the lenders' register. Registers are maintained by Cantonal authorities.	Maximum APR limited to 15%	Federal Consumer Bureau is responsible for protecting consumers and controlling businesses.
France	Lending operations are not subject to financial supervision.	Maximum APR limited to 1/3 over the average interest rate defined on a quarterly basis by the Central Bank	Companies are supervised by a consumer protection authority with the entitlements based on those defined in the EC directive to ensure that they follow fair market practices (with regard to advertising, providing information and detailed contractual provisions).
Italy	Operations of personal lenders are supervised by the Central Bank which is also a financial supervision authority. The Central Bank maintains a register of personal loan companies.	Maximum APR is updated every 3 months by the Central Bank	There is no separate consumer protection authority; however, a number of acts on consumer rights were passed. Consumers may assert their rights in civil courts.
Latvia	Operations of personal lenders are not subject to banking supervision; however, lending companies must obtain an appropriate licence to conduct their business. Currently, the registry of licensed lenders is maintained by the Consumer Protection Agency.	There is no statutory APR limit. Currently, there are discussions to set the APR limit at 100%.	The competent authority for receiving complaints regarding non-compliance of lending companies is the Consumer Protection Agency. There are also a number of regulations that require personal loan companies to provide specific information (including transparent information about all costs of the loan, APR etc.).

4.5. Withdrawal from the agreement

The Act on Consumer Credit gives the consumer a right to withdraw from a credit or loan agreement without stating the reasons for the withdrawal. The consumer may exercise the right provided that he/she sends a written statement of withdrawal from the contract to the creditor within the time limit of 14 days. To make it even easier for the customers, the legislator required the lenders to attach a blank withdrawal form to the loan agreement.

The right to withdraw from the agreement without stating the reason must not in any case be made dependent on repayment of the principal or additional costs. In the case of withdrawal, the parties must return their mutual considerations, therefore there is no reason for charging the consumer with the additional costs after the withdrawal. Interest may be charged only for the days on which the agreement was effective.

Problems with executing the withdrawal appear when:

a) The agreement is signed online;
b) The loan is provided in form of a credit facility.

According to the act, the time limit for withdrawal is 14 days after the consumer has received the loan agreement on durable media. If subsequent loans are granted under one loan facility, the consumer signs the agreement only once. Therefore, when additional loans are contracted under a single loan facility (within the same framework agreement from a formal point of view), the right to withdraw from the agreement does not apply.

The right to withdraw from the agreement is the consumer's indisputable right specified in the law. According to the law, the consumer has 14 days to withdraw from the agreement after signing. For revolving loans (e.g. a loan facility) the right does not apply when subsequent loans are taken as part of the same agreement.

During a discussion on the need to introduce new regulations in any segments, there are always contradicting view. The supporters of the first view will support introduction of new regulations, pointing out to the need for security and transparency of the trade, and for protecting the more vulnerable market participants. The supporters of the opposite view will say that the current legal environment ensures a sufficient number of mechanisms for protecting market transparency and the competition between the entities, as well as the consumers. Nevertheless, proper application of the law, including successful enforcement, may be a challenge.

It seems that both views are appropriate with regard to the personal loan companies market. The biggest chance for implementing positive changes in the market is created by combining new, balanced regulations to increase the transparency of the market without interfering with the existing business models, with proper application of the existing law. One should remember that the current legal system offers a number of mechanisms that ensure proper operation of the market; however, their success depend on reliability of public administration bodies, such as the Public Prosecutor, registration courts and tax authorities, which are entitled to report suspicions about illegal activities to the prosecutor.

A lot depends on the awareness and activity of consumers, who are now protected against unfair market practices, but are often unaware that the model of protection of their rights based on the civil law requires them to undertake certain actions.

5. Summary: key findings for the personal loans market in Poland

The primary purpose of each market regulation is to adjust the causes due to which the regulated market is not fully efficient. On the other hand, the scope of market regulation must be defined so as to prevent the collapse of the market, competitive imbalance, or other irregularities that were not present in the market before. Any conclusions for the lending market and potential regulation of the market have been based on the above principles.

The analysis of the market of personal loans extended by companies other than banks revealed the following key challenges for the market:

The scope and method of use of the information collected by personal loan companies before granting the loan, required for proper assessment of the potential customer's credit status, remains a challenge for the lenders.

Personal loan companies should have access to and use full information about the creditworthiness of their potential customers to reduce the risk of their being caught in a debt spiral. In this context, it is important to have access to full information about other debts of the customer, including the information from the credit bureau and other credit information agencies. Reducing that risk is especially important since our analysis revealed that approximately half of the customers of personal loan companies are already indebted to other institutions.

The terms and conditions of the loan, the scope of information and method of presenting it to customers, and most of all the text of the loan agreement should be clear and understandable to customers.

Any limitations of the terms and conditions of the loans should be market neutral, which means that they should not have different impact on the business models already existing in the market. The scope and method of presentation of the information about the terms and conditions of the loan should be adjusted to the customer of lowest awareness of the risks related to signing a loan agreement. Lack of transparency in the agreements may result in a debt spiral for customers who are not aware of all the costs of a contracted loan.

Customer service practices continue to be a problem.

An important aspect of operations of personal lenders is the sales culture. This aspect can be regulated to a limited extent only. Nevertheless, a code of good practice, internal codes of conduct and codes of ethics may eliminate such negative market characteristics as information asymmetry.

The aforementioned areas may be regulated through the following elements:

1. APR

Quoting the value of the loan's APR in the loan agreement is now a mandatory requirement; however, it still remains unclear to the customers. Different approaches to calculating the APR adopted by different lenders and enigmatic three- or four-digit numbers representing the APR value put a big question mark over usefulness of the indicator for customers to make comparisons between costs of loans. This concerns in particular loans of the shortest maturity. Introduction of a statutory APR limit may eliminate the products from the legal market. Therefore, for the sake of customer protection, it may be required to put a limit on loan costs other than ARP and/or adopt a precise method of APR calculation.

2. Other loan parameters

Other key parameters of loans include total loan costs and repayment schedule. That information should be presented to customers in a clear and uniform format to enable them to compare offers from different lenders. In order to limit the lending costs, one should consider differences in the cost structures. As revealed by the analysis, regulations related to individual components of the loan cost structure would have different effects on the existing business models, possibly eliminating some of them from the market, and therefore they would not be market-neutral. It seems that a measure that would not affect the market regardless of the business model would be limiting the total loan costs depending on the maturity date. Linking the limitation of the total costs of a loan with the loan maturity date seems necessary to natural market relationship between those two parameters and the resulting various business models.

3. Text and form of presentation of information in loan agreements

As proved in the course of analysis, customers of personal loan companies are often unable to fully understand, and therefore evaluate the effects of their borrowing decision on their financial status. For the same reason, they are not able to assess whether lender's offering is attractive. Therefore, a requirement to ensure transparency of loan agreements should be considered. Any potential regulations regarding the contents and method of presenting the loan agreements should comply with the prevailing market realities. At the same time, to protect interests of the consumers, it seems worthwhile to put a special emphasis on creating conditions for making informed borrowing decisions through the following means:

- Striving for simplification of communications and ensuring that the key information is more legible to the customer;
- Striving for simplification of financial parameters describing the products, which are used in customer communications;
- Focusing the customer's attention to key information in the marketing communications as well as the actual loan agreement;
- Increasing the financial awareness and education of potential borrowers;
- More effective and consistent application of the existing requirement to present a representative example in marketing communications.

4. Requirement for verification of the customers' creditworthiness

As revealed in the course of the study, personal loan companies do not use the whole information about the financial standing of their clients. It seems viable then that they should have access to information about people intending to take a loan and requiring them to use such information as well as recommending (through best practices or rules) that such information is provided by credit bureaus and credit information agencies. This would limit the excessive indebtedness of those who are unable to repay their loans.

This issue is also related to the currently discussed draft amendment of the Act on Economic Information and improvement of the flow of information on customer debts between the banking sector and the non-regulated sector. One of the method to improve that flow of information could be a slight liberalisation of the banking secrecy regulations (only with regard to exchange of information about customer debts) in order to provide personal lenders with direct access to credit information of banking customers, while requiring them to submit information to credit bureaus. Legislative activities are also necessary, including activities with regard to the Banking Act, to provide access to information to a broader range of entities (e.g. banks, personal loan companies and special operators who have credit database know-how) to strengthen the competition in the credit bureau market (currently monopolised), and therefore ensure that prices for loan companies and banks using the information are lower. A more immediate measure would be improving exchange of customer debt information between credit bureaus and credit information agencies. It should be stressed that companies participating in the survey mentioned introduction of the information exchange between banks, SKOKs and personal lenders as one of the basic regulation proposals for the industry. One may therefore expect than any potential amendments moving into that direction will be also welcomed by the interested parties.

5. No criminal record of individuals conducting the lending business

This proposal is also supported by the companies that participated in the survey. The requirement that a person conducting a business based on mutual trust, such as extending loans, seems only natural. It might also improve the credibility of the market operators. The possibility to check the police records is strictly connected to the proposal of introducing a register of personal loan companies, because the true and accurate character of the statements made by persons applying for registration can only be checked at the stage of examining the registration documents by an appropriate authority before making the decision to enter the company to the register.

6. Register of companies

Introduction of a register of companies and subjecting them to control by state authorities would improve transparency and discipline in the personal loans market, while increasing the level of customer protection. Moreover, it might improve the negative image of that segment of the financial market. The idea was also supported by the personal loan companies that participated in the survey.

7. Level of share capital

A substantial level of the initial capital (share capital in the case of joint stock or limited liability companies) required to start personal lending operations, which has been proposed in the government's draft amendment, is no guarantee or warranty of the lender's reliability. A personal loan company may be funded with its owners' funds, bank credits, issue of bonds (in the case of large companies), or funds obtained from the parent company. Stable funding of companies operating in the quickly growing personal loan market, if we assume that high standards of lending are followed, will require investment not only in the sales network but also in the customer credit scoring system, including maintenance of a professional customer base, expenses related to obtaining information from credit bureaus and credit information agencies, staff training, proper communication process to prevent money laundering. One must remember that setting the minimum initial capital threshold too high may restrict economic freedom. On the other hand, setting the threshold too low may create a risk of fraud, such as money laundering.

8. Other conclusions

The planned regulations should, therefore, ensure safety to companies and customers, and also introduce transparent rules of fair competition to the market. On the other hand, not all aspects should be externally regulated. For example, to strengthen the responsible selling culture, it seems justified to consider introduction of a code of good practice, which would be established as part of a broad agreement between companies or within commercial chambers representing such companies.

In addition, to ensure full protection of consumer interests, special emphasis should be put on financial education of potential borrowers so that they are able to make more informed and balanced consumer decisions.

6. Glossary of terms

Non-banking financial services	services consisting of activities which are similar to banking services (granting loans, financial intermediation etc.), but are provided outside the Banking Act or the Act on Financial Market Supervision regime.
Pyramid scheme	an entity whose business model involves providing financial services funded through deposits accepted from clients enrolling in the scheme without proper authorisation.
Shadow banking	a market of entities offering services that are similar to banking services but the state financial supervision system. The International Monetary Fund includes in this definition the companies whose activities are based on accepting deposits from clients and converting them into investment instruments of longer maturity. The European Commission uses the term referring entities that provide services similar to financial services, operating outside the financial supervision system.
Loan	a financial service consisting in transferring the ownership of funds onto the borrower for a specified period of time.
Financial supervision	supervision over the financial market. In Poland, financial supervision is performed by Komisja Nadzoru Finansowego (Financial Supervision Authority). Currently, financial supervision covers companies from the banking sector, capital market, insurance market and pension market companies, as well as companies providing payment services and social credit unions.
Annual Percentage Rate (APR)	the total cost of the loan or credit paid by the consumer, expressed as an annualised percentage value of the total loan amount.
Scoring	a tool for assessment of the creditworthiness of a customer in the lending process, which is performed on the basis of the adopted rules and criteria as well as the risk appetite of the company determined by its business model.
Reference rate	interest rate used as a basis for calculating the credit interest rate, referring to minimum interest rate of basic open market transactions conducted by the National Bank of Poland, defined by Rada Polityki Pieniężnej (Monetary Policy Council) and announced in the Official Journal of the National Bank of Poland.
Credit interest rate	interest rate expressed as fixed or variable rate applied to the credit total amount on an annual basis.

Fixed credit interest rate	interest rate specified in the credit agreement, determined with the use of a specified fixed percentage value applied to the whole term of the agreement or defined terms of the agreement.
Credit risk assessment	assessment of the consumer's ability to repay the loan, including the loan interest, on the dates specified in the consumer loan agreement, performed by the creditor.
Maturity date	the date on which borrower's loan liabilities have to be repaid; the loan maturity date.

Author of the report:
PwC Polska Sp. z o.o.

Graphic design:
the MOONLIGHT | creation & development
and PwC in Poland

The report has been financed
by Provident Polska S.A.

Date of issue:
11 December 2013

This report has been developed by PwC Polska Sp. z o.o. ("PwC"). The work related to the report was conducted from October to November 2013 and included conducting independent research of the market and examining its key elements. To ensure independent and impartial character of the report, PwC conducted its work independently without any interference of any third parties in the contents of the report.

The document presented by PwC contains information obtained from a variety of sources, including the Mystery Shopper qualitative and quantitative study, as well as from the analysis of the available data. PwC did not verify the sources or accuracy of the information provided by them. Therefore, PwC shall not bear responsibility for such information, nor does it provide any warranty as to the accuracy or completeness of this report.

PwC did not provide any additional services after 2 December 2013, which was the date on which the final project deliverables were provided. Therefore, the report does not take into account the effects of events and circumstances or information that occurred or appeared after that date, i.e. the date of providing the final project deliverables. PwC shall not be responsible for the impact on the aforementioned effects, events, circumstances or information on the final report.

We would like to draw your attention to the important comments on the scope of PwC's work, the purpose of the report and the assumptions as well as limitations regarding access to information used in this report. PwC shall not bear any liability, contractual or tort, for any acts of or their consequences to third parties, or any decisions made on the basis of this report.