



**Law  
Commission**  
Reforming the law

# Consumer Prepayments on Retailer Insolvency A Consultation Paper

Executive Summary  
June 2015

**50  
YEARS**

# 1. INTRODUCTION

- 1.1 Consumers often pay for goods and services in advance of receiving them. This is common practice for a range of products - from flights and theatre tickets to football season tickets and magazine subscriptions. Many furniture retailers rely on receiving deposits to place orders with suppliers. In addition, in 2014, the UK gift card and voucher market was valued at £5.4 billion,<sup>1</sup> with consumers and businesses paying immediately for a card or voucher allowing the holder to obtain an item at some stage in the future.
- 1.2 If the company holding the prepayment becomes insolvent, consumers risk losing their money. Insolvency law does not give consumers any special protection. Along with trade suppliers, landlords, HMRC and others, consumers are unsecured creditors. They will not receive anything until preferential creditors (such as employees) and secured creditors (such as banks and investment funds) have been paid.
- 1.3 This does not mean that consumers always lose out. As discussed in section 2 below, there are several ways in which consumers may be protected. However, such protection is sporadic and cannot always be relied on.

## HIGH-PROFILE INSOLVENCES

- 1.4 Over the years, there have been many notable cases where consumers lost out or risked losing out. At the time of its collapse in 2006, the Christmas savings club Farepak held around £37 million in consumer prepayments. Financially vulnerable savers had saved an average of £400 each. As unsecured creditors, they stood to receive less than 15% of their money back, though in the end this was supplemented by a Government response fund and a voluntary payment from Farepak's bank.
- 1.5 Deposits are particularly prevalent in the furniture, DIY and home improvements sector. Here, a long list of retailers have encountered financial difficulties and entered administration holding significant amounts in consumer prepayments. For example, when MFI went into administration, it held £27.3 million in deposits.
- 1.6 During the recent recession, high street chains such as HMV, Comet, Zavvi and Borders went into administration with many gift cards and vouchers in circulation. Often administrators decided to allow consumers to redeem vouchers, but not always.

## THIS PROJECT

- 1.7 In September 2014, the Department for Business, Innovation and Skills (BIS) asked the Law Commission to examine the protections given to consumer prepayments; to consider whether such protections should be strengthened; and to look at the options for doing so.

<sup>1</sup> UK Gift Card & Voucher Association, Gift Cards & Vouchers in the UK – Summary 2014, [http://www.ukgcva.co.uk/downloads/factsheets/summary\\_2014.pdf](http://www.ukgcva.co.uk/downloads/factsheets/summary_2014.pdf).

- 1.8 This project was not motivated by any particular insolvency. Instead we take a long-term look at the issue. Our aim is to generate informed public debate about these issues and to identify possible solutions which the Government could take forward. We have not been asked to draft legislation.

## RESPONSES

- 1.9 We seek responses to our proposals and questions by **17 September 2015**.

### How to respond

We provide an optional [response form](#) on our website. Please send your responses either:

- **By email to:** [prepayments@lawcommission.gsi.gov.uk](mailto:prepayments@lawcommission.gsi.gov.uk) or
- **By post to:** Laura Burgoyne, Law Commission, 1st Floor, Tower, Post Point 1.53, 52 Queen Anne's Gate, London SW1H 9AG  
Tel: 0203 334 5327

If you send your comments by post, it would be helpful if, where possible, you also send them to us electronically.

- 1.10 Our aim is to publish a final report by summer 2016.

## PREVIOUS REPORTS

- 1.11 Concern about consumer prepayments is far from new. The issue has been considered many times, including by the Cork Report in 1982; by the now disbanded Office of Fair Trading (OFT) in 1984, 1986 and 2006; and by Consumer Focus in 2009.

- 1.12 Reports have focused on three possible solutions:

- (1) a change to insolvency law;
- (2) voluntary sector-specific protections, possibly backed by regulation; and
- (3) liability on those who issue credit and debit cards.

- 1.13 However, the OFT noted that any detailed reconsideration of insolvency priorities would require more information about how money was actually distributed following retailer insolvency.

## INFORMATION GATHERING

- 1.14 We have drawn on four sources of information:

- (1) We identified a sample of 20 large retailer insolvencies between 2008 and 2014 which attracted press comment on the issue of consumer prepayments. We gathered data from public sources and talked to administrators about how decisions are reached.

- (2) With the help of the Institute of Chartered Accountants of England and Wales (ICAEW), we analysed a sample of 11 smaller insolvencies affecting consumers, so we could see how far the outcomes for larger businesses also applied to smaller ones.
- (3) Citizens Advice provided us with an analysis of 810 cases involving consumer prepayments from bureau evidence forms and from calls to their Consumer Service and its predecessor, Consumer Direct.
- (4) We talked to over 40 stakeholders, looking in particular at how chargeback works and at the challenges of providing voluntary protection.

1.15 A list of the organisations we have talked to is given in Appendix A of the Consultation Paper. We would like to thank the many people who have helped us and who have spoken to us so candidly.

## 2. THE EFFECT OF RETAILER INSOLVENCY ON CONSUMERS: WHAT HAPPENS NOW?

- 2.1 When a retailer becomes insolvent, the consumer no longer has a right against the company to use gift vouchers, receive goods for which they have paid a deposit, or get their money back. Instead, a consumer becomes one of many creditors, all seeking a share of the company's remaining assets.

### INSOLVENCY

- 2.2 A company is insolvent when the value of its assets is less than the amount of its debts, or when it cannot pay its debts as they fall due. In these circumstances, the directors lose control of the company. An insolvency practitioner (usually an accountant) will step in to take control, acting in accordance with statutory rules.

- 2.3 There are two main forms of insolvency proceedings:

(1) In *liquidation*, the company's assets will be sold and the proceeds distributed to the various creditors in accordance with the hierarchy set out in legislation. A business may go straight into liquidation.

(2) However, there may be a period of *administration* before this happens, during which an attempt is made to save the business or parts of it. During the administration, the insolvency practitioner (or "administrator") may choose to continue trading while working out the best way of dealing with the business.

- 2.4 Administrators have a general power to do anything "necessary or expedient for the management of the affairs, business and property of the company". However, administrators must perform their functions in the interests of the company's creditors as a whole. They are not permitted to favour or prefer some creditors (such as consumers) over others.

### THE STATUTORY HIERARCHY

- 2.5 In most retailer insolvencies, the business – or parts of it – will be sold. The proceeds of this sale will then be distributed to creditors in the following order:

(1) **Fixed charge holders.** These are secured lenders (typically banks or investment funds) who have registered a charge with Companies House over specific assets such as land or machinery. When these assets are sold, the money realised from the sale must first be used to repay the debt.

(2) **Expenses of the administration.** These include not only the administrator's fees, but any expense which arose during a period of trading in administration (including rent, VAT, staff pay and utility bills).

(3) **Preferential creditors.** Certain payments due to employees are given preferential status such as some arrears of wages, holiday pay and contributions to occupational pension schemes.

- (4) **Floating charge holders.** Banks or investment funds typically secure loans through a combination of fixed and floating charges. Like fixed charges, floating charges must be registered at Companies House. However, a floating charge may apply to all of the company's assets, both present and future. On insolvency, it will "crystallise" over the assets the company possesses at that time.

This puts floating charge holders in a powerful position. To mitigate this power, the Enterprise Act 2002 required some money to be set aside for unsecured creditors before the floating charge holder is paid. This is known as "the prescribed part", and is subject to statutory maximum of £600,000.

- (5) **Unsecured creditors.** The prescribed part, together with any remaining assets, is divided among the unsecured creditors, with each receiving the same proportion of their debt. Unsecured creditors are often numerous. As well as consumers, they may include suppliers, landlords, utility companies, and HMRC.
- (6) **Shareholders and members.** Any surplus – of which there is generally none – would be distributed to shareholders of the company.

## **THE EFFECT IN PRACTICE**

2.6 Our analysis of retailer insolvencies showed that:

- (1) Preferential claims represent a very low proportion of total liabilities; and these claims are typically paid in full.
- (2) Most large retailers (17 out of 20) had secured creditors, who received some but rarely all of the sums owed to them. The average return to secured creditors was between 30% and 40%. In the great majority of cases, the only money left for unsecured creditors was the "prescribed part".
- (3) Unsecured claims could be substantial, ranging from £11.1 million in Dwell to £699 million in Woolworths. The typical payment to unsecured creditors was negligible - less than 1% of the value of their prepayment. For example, in JJB Sports, the dividend was 0.34p in the pound, meaning that a consumer with a £100 claim would receive 34p.

2.7 Insolvency law does not give consumers any special protection. Their position near the bottom of the statutory hierarchy means that any dividend to consumers is likely to be extremely low

## **OTHER PROTECTIONS FOR CONSUMERS**

2.8 Despite these low dividends, consumers may receive some value for their prepayments in one (or more) of the following ways:

- (1) The administrator may decide to honour the prepayment (in full or in part) while the company is in administration.

- (2) A subsequent purchaser of the business may choose to honour the prepayment (again, in full or in part).
- (3) The company may have ring-fenced consumer prepayments by segregating them from its own funds and holding them in trust.
- (4) A consumer may already own the goods which have been ordered, despite not being in possession of them.
- (5) Consumers who have paid by credit or debit card may get a refund from the bank which issued the card.

2.9 We look briefly at each.

#### **Administrators' decisions**

- 2.10 Administrators may decide to continue trading in administration. If so, this opens up the possibility that administrators may honour gift vouchers or deliver prepaid goods during that period. Administrators have the power to do this, but only if it would help achieve a better result for the company's creditors as a whole. Administrators are not permitted to prefer consumers if it would damage the interests of other creditors.
- 2.11 The decision whether to honour gift vouchers is a commercial one. Honouring vouchers may preserve the value of the brand and bring consumers into the store. However, if the retailer has too many vouchers in circulation and insufficient stock, honouring vouchers could lead to losses to the detriment of creditors as a whole.

#### **Subsequent purchasers' decisions**

- 2.12 Alternatively, if a new purchaser takes over the business, the purchaser may decide to honour vouchers or orders. This can ensure continuing consumer goodwill in the business and bring people into stores. However, there is no legal obligation on them to do so.

#### **Trusts**

- 2.13 Companies can ring-fence consumer prepayments, and hold them on trust, on a voluntary basis for the benefit of consumers. Money held in trust does not form part of the company's assets, so it is not distributed to creditors generally. Instead, it can be repaid to consumers.
- 2.14 A retailer could use a trust as a permanent feature of its business model. Protection of this sort is sometimes required by consumer codes (discussed in section 5 below), but it is rare. None of the retailers in the sample used a trust in this way.

- 2.15 Alternatively, when faced with possible insolvency, a company could set up a trust to protect consumer prepayments made after the formation of the trust. We found a few examples of these last-minute trusts. For example, the directors of Zavvi set up a trust for voucher sales one month before entering administration. The directors of Land of Leather established a trust for consumer deposits three weeks before entering administration. These trusts only covered a minority of customers, but those who did enjoy the benefit of a trust had their claims paid in full.

#### **Ownership of the ordered goods**

- 2.16 There are complex legal rules about when a consumer who has ordered and paid for the goods becomes the owner of them. If the consumer is the rightful owner, the goods will not form part of the general asset pool: instead they must be made available to the consumer.
- 2.17 The case histories provided by Citizens Advice show that this is a live issue. In several cases, consumers had paid for goods and went to pick them up, only to be prevented from doing so because the retailer had gone into administration.
- 2.18 The law on this issue was developed for commercial sales and is difficult to apply in a consumer context. In section 7, we explore possible reforms.

#### **Refunds from the credit or debit card issuer**

- 2.19 Consumers who pay deposits by debit or credit card have the ability to contact the bank which issued the card and ask for a refund. The bank may then use the MasterCard or Visa “chargeback” rules to seek a refund from the merchant acquirer who processes card payments for the retailer.<sup>2</sup> Merchant acquirers often hold back collateral against such an eventuality.
- 2.20 In practice, chargeback is an extremely important protection for consumers. The amounts repaid in this way can be substantial. Available figures include MFI (£19.3 million); Homeform (£2.6 million); and Land of Leather (£1.1 million).
- 2.21 The main problem with chargeback is that consumers are not always aware of it, which means that this protection is not always fully used. As outlined in section 4, we propose that the scheme should be made more transparent.<sup>3</sup>

#### **PROBLEM SECTORS**

- 2.22 Our analysis revealed two problem sectors: gift cards and vouchers (which we refer to generically as vouchers) and deposits made for furniture and other home improvements (such as furnishings, kitchens and bathrooms).

<sup>2</sup> The merchant acquirer is the bank which accepts payments on behalf of the retailer. See chapter 5 of the Consultation Paper for more details.

<sup>3</sup> The proposals are set out in chapter 9 of the Consultation Paper.

### **Gift vouchers**

- 2.23 Gift vouchers were an issue in 15 out of the 20 large insolvencies we looked at. The total value of vouchers in circulation can be substantial: for example, HMV had £6.5 million in circulation, and Comet had £4.7 million. The number of vouchers in circulation can also be high: nearly half a million in both the Zavvi and Borders administrations.
- 2.24 In fact, consumer losses were not as prevalent as might appear. In seven cases, gift vouchers were honoured to 100% of their value during a period of trading in administration or by subsequent purchasers. In a further two cases, gift vouchers were partially redeemable. For example, the administrators for Borders agreed to accept vouchers but required consumers to spend double their value. This encouraged footfall in stores and meant that the funds for the general body of creditors were enhanced by the additional expenditure.
- 2.25 In the remaining six cases, gift vouchers were not honoured - either because there was no period of trading in administration (Jessops), it was not commercially viable to do so (Zavvi), or because new purchasers were found at an early stage and themselves decided not to honour the vouchers (Republic, JBB Sports, La Senza and Peacocks).
- 2.26 As far as we have been able to estimate, the total losses to consumers in these six cases were over £7 million. In other words, over £7 million of vouchers in circulation were rendered worthless (though some may not have been redeemed in any event).

### **Deposits held by retailers in the furniture and home improvement sectors**

- 2.27 Many of the largest losses concern deposits for furniture, bathrooms and fitted kitchens. Information about the level of consumer repayments was available in six cases. The total of prepayments held in these six cases was around £60 million.

<b>Date</b>	<b>Retailer</b>	<b>Estimate of consumer deposits held at time of insolvency</b>
2008	MFI	£27.3 million
2009	Land of Leather	£3.5 million
2011	Homeform	£5.6 million
2011	Focus DIY	£3 million
2013	Dreams	£11.8 million
2013	Dwell	£6 million
2014	Paul Simon	£2.4 million

- 2.28 Not all these prepayments were lost. Some orders were fulfilled during a period of trading in administration (though these tended to be those where only a small deposit was taken). Others were fulfilled by new buyers of the business. Consumers who had paid for items worth over £100 and less than £30,000 on a credit card had legal rights against their bank. Others who had paid by debit card requested a refund from the bank which issued the card, and recovered their payment through chargeback arrangements.
- 2.29 The heaviest losses fell on consumers who had paid by cash or cheque, who tend to be drawn from less well off socio-economic groups.<sup>4</sup> Although only some figures are available, these “cash buyers” lost around £8.5 million in the MFI insolvency; £2.6 million in Homeform; and £1.1 million in Land of Leather. An analysis of case histories provided by Citizens Advice suggested that the average amount lost in the cases reported to them was £698.

<sup>4</sup> S Brooker for Consumer Focus, *Pay now, pay later: consumer prepayments and how to protect them* (August 2009) p 14.

## **3. ASSESSMENT**

### **THE SIZE OF THE PROBLEM**

- 3.1 It is difficult to provide an authoritative figure on the total or average losses caused to prepaying consumers each year by retailer insolvency. Insolvency losses are relatively uncommon, which means that figures have to be extrapolated from small sample sizes. Administrators' reports vary widely in the level of information they provide, and may not present the final position.
- 3.2 Consumer Focus estimated in 2009 that consumers had lost around £133.3 million of prepayments in the previous two years, but only some of these losses were caused by retailer insolvency.
- 3.3 It is safe to say that the level of consumer detriment caused by retailer insolvency is low compared to loss caused by more common problems such as faulty goods or misleading statements. In these cases, consumer detriment has been estimated at over £3 billion. Despite the press headlines, retailer insolvency is still relatively rare and even where it occurs there are several ways in which consumers may be recompensed.
- 3.4 The problem is not that consumer losses are common, but that when they occur they are particularly stark. Complaints made to Citizens Advice reveal that consumers struggle to understand insolvency law. They are often astonished to find that money paid in good faith has simply been lost.

### **A NEED FOR FURTHER PROTECTION?**

- 3.5 When companies become insolvent, it is inevitable that creditors will suffer loss. We do not think that consumers can or should be sheltered from all loss. Consumers often lose small amounts whereas small trade creditors, and individual contractors without employee status, may suffer much greater hardship.
- 3.6 On the other hand, there are arguments for reinforcing consumer protections:
  - (1) The discrepancy between consumer expectations and the law suggests that the subject should at least be considered.
  - (2) The retail economy depends on consumer confidence. That confidence could be dented by even a handful of retailer insolvencies in which consumers suffer notable losses.
  - (3) Consumer prepayments bring new money into the business. Consumers are effectively lending money to the business, but (unlike other lenders) they do so without the opportunity to investigate the insolvency risk or to take security, and without charging interest.

- (4) Businesses with financial problems, finding it difficult to borrow money from sophisticated lenders, may seek to increase prepayments from consumers in the knowledge that the goods or services may never be delivered. Under the current rules, floating charge holders benefit directly from these prepayments. This may provide an incentive for businesses and their floating charge holders to inappropriately require increased prepayments in the weeks and months leading up to insolvency.
- 3.7 We ask consultees whether they agree that the protection available to consumers on retailer insolvency should be reformed.

### **PROBLEM SECTORS**

- 3.8 We think that the risk to consumers arises from a combination of two main factors:
- (1) The value of the prepayment;
  - (2) The time between the prepayment and the delivery of the goods or services.
- 3.9 Although consumers prepay for many goods and services from flights to wedding receptions, our analysis of retailer insolvencies has identified two areas of particular concern: gift vouchers, where the value of the prepayment may be low but the period of between purchase and redemption significant; and deposits in the furniture and home improvement sectors, where both a substantial prepayment may be made and where delivery of the goods is often subject to a lead-time of several weeks or months.
- 3.10 We ask consultees whether there are other sectors in which consumer prepayments are problematic in the event of retailer insolvency.

### **OPTIONS FOR REFORM**

- 3.11 The consultation paper considers options for reform in five areas:
- (1) The chargeback scheme;
  - (2) Facilitating possible means of protection;
  - (3) Possible regulation in high-risk sectors;
  - (4) A limited preferential status for consumers who make large payments in the months leading up to insolvency and are not protected by other means; and
  - (5) Changes to the legal rules about when ownership passes to consumers.

### **THE NEED FOR PUBLIC DEBATE**

- 3.12 Inevitably, insolvency law is required to allocate or apportion loss between innocent parties. There are no right answers about where the loss should lie. The rules must reflect societal and political judgements. We are therefore particularly keen to receive a wide range of views and responses to this consultation.

## **4. CHARGEBACK**

- 4.1 A consumer who has paid by credit or debit card is usually able to claim against the bank which issued the card, instead of lodging a claim with the administrators of the insolvent company.
- 4.2 In the case of a payment made by credit card, where the price of the goods or services is greater than £100 and less than £30,000, the consumer has a statutory right to claim against the credit card provider under section 75 of the Consumer Credit Act 1974. This section applies generally, not just on the retailer's insolvency, and gives the consumer substantial rights. The consumer may seek damages from the credit card provider for any breach of contract or misrepresentation claim which the consumer could have made against the retailer.
- 4.3 For other claims – that is for any purchases made by debit card, and for goods worth less than £100 – the protection is non-statutory. Consumers may request a “chargeback” from their card issuer. Card issuers may then reverse the transaction and recover the money from the merchant acquirer, invoking the chargeback procedures set out in the Visa and MasterCard scheme rules. In turn, merchant acquirers act as proxies for consumers, assessing retailers' insolvency risk and holding back funds as collateral where they consider the risk to be real.

### **THE IMPORTANCE OF CHARGEBACK**

- 4.4 Chargeback arrangements are central to the protections available to consumers on retailer insolvency. This system may result in considerable sums being refunded to consumers.
- 4.5 As chargeback arrangements have become institutionalised, they are now less voluntary than might appear. Consumers who have been refused a chargeback have the right to complain to the Financial Ombudsman Service (FOS). The FOS requires banks and building societies to deal with disputed transactions fairly, within the terms of the chargeback provisions in the scheme rules. The FOS has confirmed that, in the case of retailer insolvency, it is prepared to require a card issuer to compensate a consumer if it unreasonably refuses to refund money when it could have made a chargeback claim.
- 4.6 However, consumers often lack information about chargeback. They may not know how to request a chargeback, or how to pursue the request if they meet an initial rebuff. We have been told that card issuers take different approaches to how they train their staff to respond to chargeback claims, with some card issuers doing much more than others.

### **THE NEED FOR TRANSPARENCY**

- 4.7 Our view is that chargeback arrangements should be transparent. We make three proposals to improve information about how chargeback works.

### **Information from insolvency practitioners**

- 4.8 We think that, in the event of retailer insolvency, insolvency practitioners (that is, administrators and liquidators) should give information to consumer creditors about the possibility of asking their card issuer to raise a chargeback.
- 4.9 We also think it would be helpful for them to place a document on the retailer's website, which consumers could download and present to their bank, confirming that the company is in administration or liquidation and that goods or services are unlikely to be delivered.
- 4.10 Our preliminary view is that the issue could be dealt with through guidance, rather than requiring legislative change.

### **Information from card issuers**

- 4.11 We think that all card issuers should give consumers a brief explanation of how to raise a chargeback.<sup>5</sup> This should include:
- (1) Contact details (including a phone number and website address);
  - (2) Details of situations in which consumers may ask their card issuer to raise a chargeback, including when a retailer enters administration, and what documentation needs to be provided to the card issuer; and
  - (3) A statement that consumers who think they have met with an unreasonable refusal may complain to the Financial Ombudsman Service.
- 4.12 We would welcome views on whether this can be dealt on a voluntary basis (perhaps with support from the Banking Standards Review Council) or whether it would require action from the Financial Conduct Authority.

### **Information from card schemes**

- 4.13 We think that card schemes such as Visa and MasterCard should provide a publicly available authoritative guide on the situations in which a chargeback may be available. We think that this should be available online free of charge on the card scheme websites, and should be kept updated as rules change.
- 4.14 Again, we do not think that this proposal would require legislative change and could be taken forward by the Payment Systems Regulator.

### **SHOULD CHARGEBACK REMAIN VOLUNTARY?**

- 4.15 This leads to a more fundamental question. Should chargeback remain a purely voluntary arrangement in cases which fall outside the ambit of section 75 of the Consumer Credit Act 1974? The alternative would be to impose some new form of legal duty on banks to refund consumer prepayments made by credit and debit card whenever goods and services are not delivered.

<sup>5</sup> Some card issuers already do this. See, for example:  
[http://ask.barclays.co.uk/help/day2day\\_banking/unrecognised\\_transaction](http://ask.barclays.co.uk/help/day2day_banking/unrecognised_transaction).

- 4.16 The main argument against any legislative change is that the current system works well, and will not necessarily be improved by Government intervention (“if it ain’t broke, don’t fix it”). Any legislation is likely to be limited in scope: in Denmark, for example, there is a statutory scheme but it only applies to distance sales, while the Visa and MasterCard rules apply across the board.
- 4.17 On the other hand, the voluntary nature of chargeback means that the card schemes could in theory reduce it or even remove it. Given how important chargeback is, any moves to significantly reduce or remove the scheme could have a major detrimental effect on the entire retail sector. If this were to occur, we think that the Government would need to intervene.
- 4.18 Our current provisional view is that, provided chargeback is made more transparent, the case for legislative intervention has not been made out. However, the issue would need to be reconsidered if the card schemes were to make major changes to their current arrangements. The issue has implications which are much wider than just retailer insolvency, and we welcome respondents’ views.

## 5. POSSIBLE MEANS OF PROTECTION

- 5.1 For the last 40 years, Government policy has been to encourage trade bodies to agree voluntary schemes to protect consumer prepayments in high-risk industries. These have met with mixed success.
- 5.2 Whether voluntary or mandatory, we accept that options for protection need to be practical and affordable for businesses.

### CONSUMER CODES

- 5.3 Prepayment protection is required under the Consumer Codes Approval Scheme (CCAS) administered by the Chartered Trading Standards Institute (CTSI), which cover sectors as diverse as renewable energy, removal companies and carpets.
- 5.4 In Chapter 6 of the Consultation Paper, we look at the CCAS and a variety of other codes. We conclude that they ameliorate problems associated with consumer prepayments in many sectors. They have been particularly successful for industries that typically take only small deposits, and where other suppliers are able to step in to fulfil orders. Despite incomplete coverage of, and across, sectors, the point was also put to us that “something is better than nothing”. A scheme which solves 50% of problems is better than no scheme at all.
- 5.5 That said, consumer codes suffer from the following problems:

- (1) Voluntary codes attract the good firms. Businesses with a poor track record of consumer protection do not sign up to them, or may leave when problems start. This makes the raising of standards across the sector difficult.
- (2) There is the proliferation problem. As consumers are faced with more and more schemes and logos, they may have little idea of the protection each offers. Retailers may find that signing up to a good scheme offers no greater marketing advantage than signing up to one which imposes minimal requirements.
- (3) Prepayment protection is often particularly onerous for retailers. In 2011, the OFT, which previously administered the CCAS, commented that although prepayment protection was a key issue of consumer confidence, some sponsors found it the most difficult requirement to meet.

### THE AVAILABLE OPTIONS

- 5.6 The following options are open to retailers who wish to provide consumers with protection on insolvency, but none are without difficulties:
  - (1) **Trust arrangements.** Businesses may put consumer prepayments in a segregated account, subject to a trust in favour of consumers. However, trusts can be administratively complex, and involve legal and accountancy costs. They also deprive the business of working capital.

- (2) **Bonding.** While this may provide some protection, we understand that bonds rarely cover 100% of prepayments taken. In the travel industry where bonding is common, such arrangements are generally supplemented by an insurance-backed reserve fund.
- (3) **Insurance.** This is an attractive solution but we have been told that the market is underdeveloped. Without a mass market for this form of insurance, costs will tend to be high.

### **CAN PROTECTIONS BE MADE MORE FEASIBLE?**

- 5.7 We explore whether anything can be done to make it easier for businesses to introduce protections for consumers through the above mechanisms. We also consider the possibility of a “consumer charge” as a completely new means of protection.

#### **Trust arrangements**

- 5.8 Traders told us that holding deposits in trust in the normal course of business is fraught with difficulties. The initial legal costs may be high; independent trustees may need to be employed; and businesses may face accounting challenges. However, the main objection presented to us was that holding all prepayments in trust would deprive businesses of their working capital as they would have no way to access the funds until the goods or services were provided.
- 5.9 We are interested in ideas about how these difficulties can be addressed. One possibility would be to develop standard trust arrangements which only require firms to hold some money in trust, allowing them to access sufficient funds to run the business and supply the goods. The Park Christmas Savings Club, a member of the Christmas Prepayment Association, has arrangements in its trust deeds to allow the business to “draw-down” working capital subject to certain protections and limits.

#### **Insurance**

- 5.10 The insurance market for consumer prepayments appears to be underdeveloped. While it could be used for gift vouchers and deposits, only a few insurers are willing to provide this. Where insurance is offered, it is often expensive and hedged with restrictions.
- 5.11 The main barrier to insurance appears to be the absence of claims data which insurers need to assess the risk properly. The problem is circular: without data, it is difficult to get insurance, and without insurance, there is no data. Furthermore, any single retailer seeking deposit insurance is likely to be treated with suspicion and/or charged an excessive premium. The way of overcoming this obstacle may be for retailers to act together to demand insurance.
- 5.12 Insurers will legitimately want to know that, if a retailer were to become insolvent, the insurer could administer claims without undue cost. There may well be a business need for consumers to register for protection, particularly in the case of gift vouchers, which are given from one person to another. We think that there is merit in a registration system, provided that consumers can register easily (including online) and for free.

- 5.13 We welcome respondents' views on their experience of prepayment insurance and what can be done to overcome any barriers to it.

**A consumer charge?**

- 5.14 We have considered whether there are other mechanisms by which businesses can act voluntarily to give some creditors greater protection on insolvency. The standard way in which businesses provide creditors with security is by granting a fixed or floating charge, which is registered at Companies House. This mechanism could be developed to provide a new voluntary means of granting security to certain classes of consumer claims on retailer insolvency.
- 5.15 The proposal would be to set up a new statutory scheme, to allow a business to register a "consumer charge" with Companies House. The charge would be in favour of a specified group of consumers (such as those participating in a Christmas savings scheme) for specified debts (such a repayment of the savings). A consumer charge would be a first-ranking floating charge, which would rank below fixed charge holders and preferential creditors but above other floating charges. It would therefore need consent from any existing floating charge holder. The practical effect would be to give consumers priority status on insolvency, but (unlike trusts) businesses would not need to put money aside
- 5.16 Any new charge would need to be set out in statute, and would require considerable work to refine the details. We ask whether there would be sufficient interest to justify giving detailed examination to such an idea.

## 6. A NEED FOR REGULATION?

- 6.1 There has been a long-standing debate over whether protection of consumer prepayments should be left to voluntary arrangements or whether those arrangements should be underpinned by regulation. Regulation has been introduced in some sectors, most notably the package travel industry.

### THE ARGUMENTS FOR AND AGAINST REGULATION

#### Arguments for regulation

- 6.2 The main argument in favour of regulation is that it would cover all businesses, not simply the good ones. It is possible that without strong Government intervention, little progress will be made. In particular, concerted action is needed to break through the barriers to obtaining insurance.
- 6.3 Encouraging such action may require at least the threat of regulation, if not regulation itself. In 1984, the OFT suggested that, if voluntary arrangements failed, regulators may need statutory powers to require firms to protect prepayments. Consumer Focus has also argued for reserve powers.

#### Arguments against regulation

- 6.4 Requiring protection of prepayments imposes costs, which would be passed on to consumers. In some cases protecting prepayments is not viable, either because the business depends on prepayments for their working capital or because profit margins are so small that the potential costs mean protecting prepayments is not an affordable option. It may also undermine competition: new businesses might not be able to start up if compliance costs are too great.
- 6.5 Furthermore, it is difficult to target regulations appropriately at high-risk businesses. As the OFT put it, any definitions could invite “either evasion or unintended consequences”.<sup>6</sup> Finally, regulations only help if they are enforced, and this also imposes costs.

#### Balancing these arguments

- 6.6 We agree that regulation should not impose undue costs or bureaucratic requirements on well-run businesses. We think sector-specific regulation should only be considered if it can be targeted appropriately at high-risk areas and introduced without undue cost. We are interested in two issues:
- (1) Is it possible to identify risk factors, so that any regulation can be targeted at those areas posing significant risks?
  - (2) In those sectors, can measures be used to protect prepayments which do not impose undue costs and bureaucracy on the firms involved?

<sup>6</sup> The Office of Fair Trading, *The Protection of Consumer Prepayments: A Discussion Paper* (1984) para 9.

## **THE VOUCHER SECTOR GENERALLY**

- 6.7 Most high street retailers sell gift vouchers. Some can be thought of as simple contractual promises from a single retailer to provide goods or services up to certain value. Others begin to resemble money in that they can be passed from individual to individual but can also be redeemed for goods and services from a wide range of retailers. Although issuing money is a regulated activity, most gift cards are not regulated. The Electronic Money Regulations 2011 contain exemptions for cards which can only be used for a single retailer, a specific shopping centre or a particular type of product.
- 6.8 We do not think that most gift cards and vouchers should be regulated, for three reasons.
- (1) Our research suggests that the level of detriment is relatively small in comparison with the size of the market, which is now worth £5.4 billion.
  - (2) When consumers do lose money, it appears that they typically lose small and affordable amounts. For example, in Zavvi the average value of vouchers held by consumers was only £8.12.
  - (3) Vouchers are issued by a wide range of businesses, including many small and medium retailers. The regulation of all gift vouchers would impose a significant burden on them.
- 6.9 However, we urge retailers to do more to protect vouchers on a voluntary basis. The voucher industry will only thrive if consumers have confidence in it, and that confidence could be undermined by one or two major insolvencies.
- 6.10 Consumers appear to have little idea about whether vouchers are protected. We would wish to increase consumer awareness in this area. We think that providers of vouchers should state in the terms and conditions whether or not any protection is in place in the event of insolvency. We ask whether this can be introduced voluntarily or whether it would require regulation.

## **VOUCHERS USED FOR SAVINGS SCHEMES**

- 6.11 We have concerns where vouchers are marketed as a form of savings. The biggest consumer losses in recent years arose when the Christmas savings club Farepak collapsed in 2006.
- 6.12 Most Christmas savings schemes are now members of the Christmas Prepayment Association with voluntary trust arrangements in place. However, some supermarkets run savings clubs without such arrangements. Other retailers who suggest that vouchers are a suitable way to save include holiday companies and toy stores who market cards as children's "piggy banks".
- 6.13 Where people put their money in savings, they expect their money to be protected. This protection is already in place where consumers save with financial institutions. However, the schemes we are concerned with are not regulated because they take prepayments for products, services or vouchers rather than holding and returning cash in the way that banks and building societies do.

- 6.14 We provisionally propose that firms should be prevented from marketing or structuring a scheme in a way which suggests that it is suitable as a savings vehicle without protecting the funds in some way. We do not propose that such savings clubs should be regulated as financial institutions. Instead, adequate protection might be achieved in a variety of ways, such as setting up a trust, through insurance or bonding arrangements, or with our proposed consumer charge.
- 6.15 We seek views on this proposal. We are particularly interested in whether our definition is correctly targeted, and in how far the proposal would impose additional costs.

### **VOUCHER INTERMEDIARIES**

- 6.16 Voucher intermediaries sell vouchers which can be redeemed from a range of retailers or third party suppliers. The intermediary holds the funds until the voucher is used. As intermediaries do not hold stock, they are less likely to trade while in administration.
- 6.17 Many intermediaries take active steps to maintain high liquidity to more than the value of their prepayment liability and therefore avoid insolvency in the first place. For example, they hold cash balances or low-to-medium risk investments to the value of vouchers. They have rigorous accounting standards, and do not use funds for other purposes. Furthermore, some voucher intermediaries are run on a not-for-profit basis and so are not under the same commercial pressures.
- 6.18 However, intermediaries are under no obligation to hold funds in this way. It is perfectly legal for intermediaries to use their funds for high-risk investments or to expand their business. If they were to become insolvent, retailers may stop accepting the vouchers, which would become worthless.
- 6.19 We think that the intermediary business model can pose particular risks where:
- (1) Vouchers represent significant funds (for example, where vouchers cover the cost of hotel stays, “experience days” or spa treatments);
  - (2) The liabilities are owed for a long time (for example, where vouchers sold for Christmas are likely to be redeemed during the summer); and
  - (3) Funds are put at risk and no other protection is in place.
- 6.20 Despite the risks, we are only aware of one intermediary becoming insolvent: Red Letter Days in 2005. In that case, loss to consumers was avoided because new purchasers of the business agreed to honour vouchers.
- 6.21 Nevertheless, there are potential problems here which may need to be monitored. We suggest that legislation should provide the Government with a reserve power to introduce prepayment protection regulations for high-risk voucher intermediaries if the need arises.

## **DEPOSITS FOR FURNITURE AND HOME IMPROVEMENTS**

- 6.22 It has proved to be particularly difficult to introduce voluntary protections in this sector, as retailers rely on deposits for working capital. Furthermore, given the track record of the industry, insurance is difficult to obtain.
- 6.23 Similar problems would arise if deposit protection were to be made a regulatory requirement. We are pessimistic that regulations could protect prepayments without imposing undue costs and bureaucracy on the firms involved.
- 6.24 We think that a different approach is needed in order to address the problems of retailers who take large deposits. In the next section, we consider a change to the insolvency priorities, to grant a limited preferential status to consumers.

## 7. LIMITED PREFERENTIAL STATUS FOR CONSUMERS?

- 7.1 The current statutory hierarchy of creditors' claims on insolvency gives consumers a low status as unsecured creditors. We do not think that all consumer claims should be moved up the hierarchy and given preferential status. Many claims are small, which means that, in relative terms, they are expensive to distribute and failure to satisfy them will not cause much hardship. To provide a special status for all consumer debts could substantially reduce payments to secured lenders, thereby making lending more risky and, in consequence, more expensive.
- 7.2 However, we think that there is a case for giving preferential status to a small and limited category of the claims of consumers who have made significant prepayments shortly before the retailer enters insolvency and where no other protections are in place.
- 7.3 Three arguments can be made in favour of giving preferential status to these consumer claims.
- (1) **Hardship.** Consumers are often vulnerable and may suffer hardship, particularly those who pay by cash or cheque.
  - (2) **Inability to assess risk.** Prepaying consumers are effectively lending money to the business but, unlike other creditors, they are not in a position to assess the credit risk. By comparison, secured creditors will be told about any financial difficulties while trade creditors may protect themselves through retention of title clauses, credit insurance or changed payment terms. Cash buyers, in particular, are prejudiced. When consumers pay by card, the merchant acquirer can assess risk on their behalf and withhold collateral to fund chargeback claims.
  - (3) **Perverse incentives.** Where a business tries to trade its way out of difficulty by taking more prepayments, secured lenders have little incentive to prevent this, as payments from consumers will increase the return to floating charge holders. Directors will not be criticised for continuing to accept consumer prepayments, provided that there is a reasonable prospect of avoiding insolvency.

We do not think it is helpful to blame directors in most cases; they have every reason to try to save their companies. However, we are concerned about a body of legal rules which allows floating charge holders to benefit from additional deposits taken from consumers at a time when those "in the know" realise that contracts may not be fulfilled.

- 7.4 We do not think that preferential status would be justified on the basis of hardship alone. Many trade creditors may also be vulnerable (such as unpaid contract cleaners, or self-employed van drivers). We only make this proposal because the other arguments set out above also apply.

## THE PROPOSAL

7.5 We propose that consumers should have preferential status if their claims meet **all** of the following criteria:

- (1) The **claimant is a consumer** as defined in section 2(3) of the Consumer Rights Act 2015. That is, the claimant is “an individual acting for purposes that are wholly or mainly outside that individual’s trade, business, craft or profession”.
- (2) The claim relates to a **prepayment**. In other words, the consumer has paid money to the insolvent business (or has parted with goods with a money value), and did not receive goods or services in exchange at the time. Preferential status would be limited to the value of the prepayment.
- (3) The payment is made **during the 3 months** leading up to insolvency, when the financial problems facing the company are likely to become apparent. We have considered whether this should be a flexible test, but are inclined to think it would be simpler to have a set time limit.
- (4) The **claim is sufficiently large** to justify the costs of distribution. Our provisional view is that preferential status should be limited to claims where the consumer has paid £100 or more, either in a single transaction or in a series of linked transactions.
- (5) The consumer **used a payment method which did not offer another remedy (such as chargeback)**. In other words, it would not cover payments by credit and debit cards, but would be limited to other payment mechanisms such as cash, cheque or online bank transfer.

7.6 Our proposal is that this limited category of claims should have preferential status, behind preferential claims of employees but before floating charge holders. This proposal would not give such consumers full protection: there may be no funds available. However, it would protect consumers in the majority of cases we looked at where funds were available and paid to secured creditors.

## IMPACT OF THE PROPOSAL

### On the furniture and home improvement sector

7.7 The proposal is not confined to the furniture and home improvement sector, but we think that this is the sector where it will have the greatest impact.

7.8 We expect that, in most cases, preferential status would result in the consumer receiving the goods rather than getting a refund. We have been told that, where trading continues in administration and commercial considerations allow, administrators will try to fulfil orders. However, at present, they can only do so where the deposit is relatively small (so that the final payment covers the cost of supply and delivery), or where the merchant acquirer agrees to fund the fulfilment of orders because this will reduce their chargeback liability. Our proposal is designed to encourage a greater number of orders to be fulfilled, even where the consumer has paid a large deposit in cash.

### **On the gift voucher sector**

- 7.9 By contrast, this proposal will have a limited impact on vouchers. Most vouchers have a face value of less than £100, and may well be held for more than three months. We accept that the protection given to voucher holders under this change would be limited, but hope that it would sit alongside voluntary protection.

### **On floating charge holders**

- 7.10 The impact of this proposal would be likely to fall predominantly on floating charge holders. We do not think the impact would be great, as the category of claims given preferential status is very limited. It would only bite in those few businesses which take large deposits by cash or cheque.
- 7.11 In these cases, it would make floating charge holders more cautious in their lending practices. Lenders would need to focus on the underlying strength of the business, and its general asset base, rather than securing their lending on consumer deposits. We think that this caution would be beneficial. It would remove any incentive on secured lenders to allow an increase in deposits in the run up to insolvency, as floating charge holders would no longer benefit from them.

### **On unsecured creditors**

- 7.12 In the majority of the cases we examined, there was no return to unsecured creditors, except for the prescribed part. Granting consumers a preference would therefore have had no impact on the outcome to other unsecured creditors. The only, marginal, effect would have been a small reduction in the number of claims on the prescribed part, thereby allowing a small increase in payments to other unsecured creditors.
- 7.13 However, for some small and medium businesses without secured creditors, the impact of the proposal would be felt by other unsecured creditors.

### **CONSULTEES' VIEWS**

- 7.14 This would be an important change. We seek views on both the principle and detail of this proposal and on its likely impact

## 8. TRANSFER OF OWNERSHIP

- 8.1 If ownership of pre-ordered or prepaid goods has passed to the consumer, the goods do not form part of the general asset pool: instead they must be made available for the consumer to collect.
- 8.2 The case histories given to us by Citizens Advice show that this may be a live issue on retailer insolvency. This is an example:

We ordered some curtains, paid for them and had them shortened by the shop... We called in today to collect them and were told that the shop had gone into receivership as of 12 noon yesterday and that we couldn't have the curtains as they were assets of the company and the assets were frozen. Surely if we have paid for them, they are no longer the company's assets but they are our assets and we should have been able to pick them up?

- 8.3 As we explain below, the current law on this issue is from clear.

### THE CURRENT LAW

- 8.4 The general rule that ownership is transferred to the buyer when the parties to the contract intend it to be transferred.<sup>7</sup> However, unless a different intention appears, the Sale of Goods Act 1979 set out rules for ascertaining the intention of the parties. Different rules apply to "specific goods" and to "unascertained goods".

#### Specific goods

- 8.5 "Specific goods" are defined as "goods identified and agreed upon at the time a contract of sale is made".<sup>8</sup> In the example above, the curtains would be specific goods if they are ready-made and available to take away from the shop at the point of purchase.
- 8.6 For specific goods, ownership generally passes at the time the contract is made, so long as the contract is unconditional and the goods are in a "deliverable state". Where the seller is bound to do something to put the goods into a deliverable state, ownership does not pass until that thing has been done and the buyer has been notified.
- 8.7 In the example, there is at least a question about whether the curtains are in a "deliverable state" until the retailer has completed the alterations. The practical result is not entirely clear.

<sup>7</sup> Sale of Goods Act 1979, s 17. While we employ the more modern terminology of "transfer of ownership" in the Consultation Paper, the 1979 Act refers to the "passing of property",

<sup>8</sup> Sale of Goods Act 1979, s 61.

### **Unascertained goods**

- 8.8 In many cases the specific items to which the contract relates may not be identified at the time of the contract. To use the example again, the curtains would be unascertained if the retailer could select a packet of curtains from the warehouse, or if the consumer ordered curtains to be made to order.
- 8.9 For unascertained goods, there is a presumption that ownership passes to the buyer when the goods are “unconditionally appropriated” to the contract.<sup>9</sup> This rule was developed for commercial contracts, and is difficult to apply to a consumer context. It appears that setting aside or labelling goods for dispatch is not enough. Instead, they become “unconditionally appropriated” when the seller delivers the goods to the buyer or to a carrier.
- 8.10 Again the law is unclear. It is far from certain whether the act of altering the curtains does or does not show an intention for ownership to pass.

### **THE NEED FOR REFORM**

- 8.11 The current statutory rules in this area are overly complex and uncertain. We propose new, simpler rules on transfer of ownership of goods, which would apply in the consumer context. Our aim is to establish rules which can be applied in practice by administrators and shop staff and which allow consumers to receive goods which have been identified for them and paid for.

### **PROPOSALS**

- 8.12 We propose new rules to apply to consumer sales.
- (1) For specific goods, ownership should pass to the buyer on conclusion of the contract, even where the seller is required to do something further to the goods (such as adapt goods to the buyer’s specifications).
  - (2) For unascertained and future goods, ownership should pass to the buyer where goods have been “identified” for the fulfilment of that contract. Such identification may include labelling the goods or segregating them from the retailer’s general stock.
- 8.13 We ask whether these rules should be mandatory (so that they apply to all consumer contracts), or whether it should be possible to make alternative provision by agreement.

### **PAYMENT**

- 8.14 The current rules do not require the buyer to have paid for the goods. In practice, problems are unlikely to arise where the consumer has paid only a small deposit. Here the administrators will be keen to complete the sale and receive the balance of the payment.

<sup>9</sup> Sale of Goods Act 1979, s 18, rule 5.

- 8.15 The greatest problems arise where the goods have been paid for in full, but ownership has not passed. Here administrators have no commercial reason to complete the order. Our proposal will help consumers in these circumstances, at least if goods have been identified, labelled or set aside for them.
- 8.16 We have considered whether transfer of ownership should be dependent on the consumer having paid for the goods in full. However, this would disadvantage those who have made large depositions (such as 90%) and who would have no right to the goods.
- 8.17 Where a consumer has not fully paid for the relevant goods, the retailer or administrator would not be obliged to release the goods until the consumer had paid for them in full, as an unpaid seller has a lien on the goods for the price.<sup>10</sup> This means that the seller has a right to retain the goods until the whole of the price has been paid, even if ownership has already passed to the buyer.

### **IMPACT OF THESE PROPOSALS**

- 8.18 Where the retailer is trading in administration, the rules would be relatively easy to apply. For specific goods, staff could be directed to hand over specific goods which are being held by the retailer awaiting alteration (or where the alteration has been completed and the goods are merely awaiting delivery). For unascertained or future goods, staff could be directed to hand over those goods which have already been labelled.
- 8.19 Where there is no trading in administration, consumers would be required to visit the retailer or another holding location at their own expense to reclaim goods, in the same way as suppliers with retention of title clauses.
- 8.20 We accept that these new rules would have a relatively limited effect. However, we think they would reduce the number of disputes and be perceived as less obviously unfair to consumers.

<sup>10</sup> Sale of Goods Act 1979, s 39(1).

## 9. LIST OF PROPOSALS AND QUESTIONS

This chapter brings together all of the provisional proposals and consultation questions contained in the consultation paper. We invite consultees to comment on all or some of these, as appropriate. This will greatly assist us in formulating our recommendations for reform.

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### ASSESSMENT

- Q1 Do consultees agree that the protection given to some types of consumer prepayments on retailer insolvency should be reformed?
- Q2 In this report we identify two particular sectors where consumers risk losses on retailer insolvency: gift vouchers and deposits in the furniture and home improvement sectors. Are there other sectors in which consumer prepayments are particularly problematic in the event of retailer insolvency?

### CHARGEBACK

**Proposal 1** Insolvency practitioners should give information to consumer creditors about chargeback claims and make available on the retailer's website a confirmation that the company is in administration or liquidation.

**Proposal 2** All card issuers should give consumers a brief explanation of how to raise a chargeback. This should include:

- (1) Contact details (including a phone number and website address);
- (2) Details of situations in which consumers may raise a chargeback, including when a retailer enters administration, and what documentation needs to be provided to the bank;
- (3) A statement that consumers who think they have met with an unreasonable refusal may complain to the Financial Ombudsman Service.

**Proposal 3** Card schemes should provide a publicly available authoritative guide on how chargeback works.

- Q3 Do you agree with these proposals?
- Q4 If so, do you have any comments on how they should be implemented?
- Q5 Our provisional view is that chargeback should not be required by legislation. We seek views for and against legislating for new legal duties to be imposed on card issuers to refund payments in circumstances currently covered by chargeback.

## **POSSIBLE MEANS OF PROTECTION**

- Q6 Would trusts designed to protect some rather than all prepayments (either where funds could be drawn-down, or where only some prepayments were put into trust), be an acceptable compromise in situations where ring-fencing all prepayments is not practical or affordable for the business?
- Q7 Would it be useful to develop a series of standard trust deeds which businesses could use to protect consumer prepayments?
- Q8 Do consultees have any experience of prepayment insurance? If so, we would be interested to learn more about:
- (1) Cost of insurance and who bears this;
  - (2) Extent of insurance coverage and any limitations or exclusions which may apply;
  - (3) Claims procedure for consumers including documentation to be supplied;
  - (4) Interaction between insurance and section 75 claims (for example, whether consumers must first pursue a section 75 claim where available before making a claim under the insurance policy).

If applicable, we would also be grateful for sample policy documents.

- Q9 What can be done to overcome barriers to consumer prepayment insurance?
- Q10 Is there merit in developing a new statutory “consumer charge” to be registered at Companies House, which businesses could use on a voluntary basis to give priority to some specified classes of consumer claims?

## **A NEED FOR REGULATION?**

**Proposal 4** Rather than introducing mandatory prepayment protection for all gift vouchers, retailers should be encouraged to take more voluntary steps to protect consumers.

- Q11 Do consultees agree?

**Proposal 5** Providers of vouchers should state in the terms and conditions of the voucher whether or not the value of the voucher is subject to any protection in the event of insolvency.

- Q12 Do consultees agree? Could this be introduced voluntarily, or would it require regulation?

**Proposal 6** It should be unlawful to market a scheme in a way which suggests that it can be used as a savings vehicle without putting some form of protection in place to protect the funds.

Q13 Do consultees agree?

We welcome additional comments on this proposal. In particular:

(1) Is our definition correctly targeted?

(2) What additional costs would our proposal impose?

**Proposal 7** Legislation should provide the Government with reserve powers to regulate high-risk voucher intermediaries which hold significant funds over a long period and which may use those funds for other purposes without providing consumers with alternative protection.

Q14 Do consultees agree?

Q15 What would the risks and potential costs be for any voucher intermediary (whether “high-risk” or not) if they were required to introduce protection mechanisms such as trusts, insurance or bonding?

Q16 Do consultees agree that sector-specific regulation is not a suitable means of protecting consumer prepayments in the furniture and home improvement sectors?

#### **LIMITED PREFERENTIAL STATUS FOR CONSUMERS**

**Proposal 8** A limited category of consumer claims should be given preferential status, to rank behind employees but in front of floating charge holders. It would apply where the consumer provided a significant sum of new money to the business in the run-up to the insolvency, using a payment method which did not offer a chargeback remedy.

Q17 Do consultees agree with the policy behind this proposal?

Q18 Do consultees agree that the preferential status should apply to money paid within a set period before the date of entering administration/liquidation? We seek views on whether that set period should be three months.

Q19 Do consultees agree that preferential status should be limited to claims where the consumer has paid more than a certain amount, either in a single transaction or in a series of linked transactions? We seek views on whether that amount should be £100.

Q20 We seek views on the impact of this proposal generally. We are also interested in the following issues:

- (1) Are retailers able to keep records of prepayments of (say) £100 or more made by cash or cheque, so as to present a running total of such sums to their floating charge holders?
- (2) Would floating charge holders be able to monitor these sums?
- (3) Do many businesses rely on these prepayments to a significant degree?

Q21 We are interested in hearing about examples of businesses:

- (1) which rely on these prepayments but do not have secured creditors; and/or
- (2) which successfully traded their way out of financial difficulties by relying on consumer deposits by cash or cheque.

### **TRANSFER OF OWNERSHIP**

**Proposal 9** For specific goods, which are identified at the time of the contract, ownership should be transferred at the time the contract is made. This should apply even if the retailer has agreed to alter the goods in some way before the consumer takes possession.

**Proposal 10** For unascertained or future goods, which are not identified at the time of the contract, ownership should be transferred when goods are identified for fulfilment of the contract.

Q22 Do consultees agree with these proposals? In particular:

- (1) Would they assist administrators in determining whether to fulfil consumer orders?
- (2) What impact would they have on other creditors?

Q23 Should these rules be mandatory, so that they apply by law to all contracts? Alternatively, should the parties be able to agree alternative provisions?

Q24 Are there any arguments for ownership of goods to be transferred immediately to consumers upon conclusion of the contract?