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UK Lenders Face £9bn+ Car Loan Compensation Bill

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British finance firms could face a compensation bill exceeding £9 billion following a regulatory review into controversial motor finance deals, despite a recent Supreme Court ruling that favoured the industry.

The UK's Financial Conduct Authority (FCA) announced on Sunday that, although the Supreme Court had determined that most high-interest car loan agreements were lawful, the issue remains far from resolved. The court's decision, delivered on Friday, partially overturned earlier rulings that had found certain loan agreements unlawful. While this offered some reprieve to lenders, one of the three cases reviewed was upheld, leaving the door open for ongoing compensation claims.

These claims stem from the use of Discretionary Commission Arrangements (DCAs), a now-banned practice where car dealers were incentivised to charge higher interest rates in exchange for higher commissions from lenders. The FCA has described these arrangements as unfair, leading to a widespread investigation into historic loan agreements issued before the 2021 ban.

In its latest update, the FCA said the likely redress costs could top £9 billion, with some projections indicating a potential figure as high as £18 billion. However, the regulator cautioned that these higher-end estimates are unlikely. "While there are plausible scenarios which underpin estimates of a total cost as high as £18 billion, we do not consider those scenarios to be the most likely," the FCA stated. "Analyst estimates in the midpoint of this range are more plausible."

Millions of drivers may be eligible for compensation. The watchdog is also currently consulting on a formal redress scheme, with a final decision expected by early 2025.

Finance firms had previously warned of a wave of claims following the initial court rulings that labelled some agreements as unfair. The Supreme Court's clarification may limit the scope of legal challenges, but the FCA's proposed redress scheme means compensation is still likely on a significant scale.

The potential financial impact is considerable for major UK lenders, especially those with large motor finance portfolios. Some banks have already begun setting aside provisions in anticipation of payouts.

The FCA's investigation into car finance practices reflects a broader push for consumer protection and transparency in the financial sector. Discretionary commissions were outlawed in January 2021, but millions of agreements made before that date remain under scrutiny.

The regulator continues to gather evidence and input from both lenders and consumer groups. Motorists affected by the scheme are advised not to lodge individual claims while the consultation is ongoing, as any future redress process may be applied automatically.