Title: **Options for reform to regulatory framework for consumer credit**	Impact Assessment (IA)
Lead department or agency: Department for Business, Innovation & Skills	**IA No:** BIS0132
Other departments or agencies: HM Treasury	**Date:** December 2010
	Stage: Consultation
	Source of intervention: Domestic
	Type of measure: Primary legislation
	Contact for enquiries: Philip O'Donnell (020 7215 6764)

Summary: Intervention and Options

What is the problem under consideration? Why is government intervention necessary?

Consumer credit is generally regulated separately from the rest of financial services, by a different organisation (the Office of Fair Trading, OFT) and under a separate legal framework (the Consumer Credit Act, CCA). However, there is some overlap with the supervisory responsibilities of the Financial Services Authority (FSA) under the Financial Services & Markets Act (FSMA), which can result in an inefficient allocation of supervisory resources. Many detailed rules governing conduct of consumer credit business are set out in primary legislation (CCA), therefore even relatively small changes require primary legislation. Proposals to alter the regulatory architecture for financial services, including the creation of the consumer protection & markets authority (CPMA), present an opportunity to change the regulatory framework to address these problems.

What are the policy objectives and the intended effects?

In assessing the potential for reform, the Government will be guided by the following objectives:

- Clarity, coherence and improved market oversight
- Effective and appropriate consumer protection, including through a responsive and flexible framework
- Simplification and deregulation
- Proportionality and cost-effectiveness

The intended effect is to create a world-class regulatory regime that keeps pace with a dynamic consumer credit market; responds to actual or potential gaps in consumer protection, and places a proportionate regulatory burden on business.

What policy options have been considered? Please justify preferred option (further details in Evidence Base)

The 'do nothing' option (i.e. maintaining the existing CCA-based regime) is subject to considerable uncertainty due to proposed institutional changes to the competition and consumer regimes. The potential transfer of existing OFT functions may mean that the OFT would no longer be operating in its current form in the future . Nevertheless, we assume that it will be possible to maintain the existing framework, despite a lack of certainty about the regulatory authority that would have responsibliity for the CCA regime. The alternative option (and subject of this consultation) is the regulation of consumer credit under a FSMA-style legislative framework by the CPMA - i.e. legislative change to replace the CCA with a rulebook, which the CPMA would be responsible for writing. The legal framework for the CPMA's powers and functions will be based on the model set out in FSMA, with modifications to enable the CPMA to carry out its conduct-focused responsibilities more effectively. At this stage, the Government believes that this option is most likely to achieve the range of objectives set out above.

When will the policy be reviewed to establish its impact and the extent to which the policy objectives have been achieved?	It will be reviewed 2019
Are there arrangements in place that will allow a systematic collection of monitoring information for future policy review?	Yes

Ministerial Sign-off For consultation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:......... Ed Davey .... Edward Davey ....

Summary: Analysis and Evidence

Policy Option 1

Description: Regulation of consumer credit under FSMA-style legislative framework by CPMA (i.e. statutory change to bring consumer credit within the remit of the CPMA under the successor legislation to FSMA, including replacing the CCA with FSMA provisions and CPMA rules and guidance)

Price Base Year 2010	PV Base Year 2010	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low:	High:	Best Estimate: TBC

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	12	3	Unquantified	**Unquantified**
High	20		Unquantified	**Unquantified**
Best Estimate	**16**		**Unquantified**	**Unquantified**

Description and scale of key monetised costs by 'main affected groups'

One-off costs of institutional change associated with extending CPMA responsibilities to include consumer credit (up to £5m); one-off costs to firms already regulated by both FSA and OFT from application for variation of permission (£12m-15m). Additional one-off and ongoing costs – as yet unquantified and outlined below – are likely to be significant (e.g. estimated compliance burdens under FSMA exceed £850m per year across all firms).

Other key non-monetised costs by 'main affected groups'

Ongoing costs to proportion of consumer credit firms from additional compliance costs and annual fees; one-off costs of developing rulebook-based material to replace CCA; one-off familiarisation costs (e.g. training) and application fees for proportion of consumer credit firms. Scale of these costs will vary according to degree of regulatory oversight and familiarity with FSMA-based regulation. However, lack of information about likely supervisory resources required renders these costs unquantifiable at this stage.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	None	N/A	131.6	**1,105**
High	None		131.6	**1,105**
Best Estimate	**None**		**131.6**	**1,105**

Description and scale of key monetised benefits by 'main affected groups'

Ongoing compliance cost savings to firms from repeal of CCA (£235m per year), net of burdens required under European legislation (£115m per year), giving total quantified burden reduction of £120m per year; reduction in costs of administering OFT consumer credit licence regime (up to £11.6m per year). However, as outlined above, potential additional requirements under FSMA-style regime remain unquantified; at this stage, it is not possible to know whether aggregate net burden of compliance for firms will be positive (i.e. a net increase) or negative (i.e. a net reduction).

Other key non-monetised benefits by 'main affected groups'

Avoidance of costs incurred by business and consumers from improved oversight (e.g. potential reduction in problem debt/write-offs, reduced detriment associated with problems flowing from slow legislative response); potential cost savings to CPMA from improved efficiency/economies of scale; cost savings for related bodies (e.g. FOS, CFEB); cost savings to dual-regulated businesses from a single regulatory regime (e.g. eliminating competing demands from regulators and/or duplication in compliance and supervision).

Key assumptions/sensitivities/risks — **Discount rate (%)** 3.5

Due to data limitations, the majority of relevant costs and benefits have not been quantified; an assumption has been made about the decline in the population of regulated firms as a result of some choosing not to renew their licence (8%), which could affect the overall level of costs; a potential risk from an increase in compliance burden is market exit, which could lead to consumer detriment through reduced choice of suppliers and have an adverse impact on innovation and use of illegal lenders; firms may pass on increased costs to consumers in the form of higher prices; there is a risk that CPMA may not develop sufficient expertise to make appropriate interventions in consumer credit market; transition could take significant period of time (2-3 years), which may involve considerable additional resource.

Impact on admin burden (AB) (£m): TBC			Impact on policy cost savings (£m):	In scope
New AB: TBC	**AB savings:** TBC	**Net:** TBC	**Policy cost savings:** TBC	No

Enforcement, Implementation and Wider Impacts

What is the geographic coverage of the policy/option?			United Kingdom		
From what date will the policy be implemented?			2014 (est.)		
Which organisation(s) will enforce the policy?			CPMA		
What is the annual change in enforcement cost (£m)?			TBC		
Does enforcement comply with Hampton principles?			Yes		
Does implementation go beyond minimum EU requirements?			N/A		
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** N/A	**Non-traded:** N/A	
Does the proposal have an impact on competition?			Yes		
What proportion (%) of Total PV costs/benefits is directly attributable to primary legislation, if applicable?			**Costs:** 100	**Benefits:** 100	
Annual cost (£m) per organisation (excl. Transition) (Constant Price)	**Micro** TBC	**< 20** TBC	**Small** TBC	**Medium** TBC	**Large** TBC
Are any of these organisations exempt?	No	No	No	No	No

Specific Impact Tests: Checklist

Set out in the table below where information on any SITs undertaken as part of the analysis of the policy options can be found in the evidence base. For guidance on how to complete each test, double-click on the link for the guidance provided by the relevant department.

Please note this checklist is not intended to list each and every statutory consideration that departments should take into account when deciding which policy option to follow. It is the responsibility of departments to make sure that their duties are complied with.

Does your policy option/proposal have an impact on…?	Impact	Page ref within IA
Statutory equality duties[1] Statutory Equality Duties Impact Test guidance	Yes	30
Economic impacts		
Competition Competition Assessment Impact Test guidance	Yes	29
Small firms Small Firms Impact Test guidance	Yes	30
Environmental impacts		
Greenhouse gas assessment Greenhouse Gas Assessment Impact Test guidance	No	
Wider environmental issues Wider Environmental Issues Impact Test guidance	No	
Social impacts		
Health and well-being Health and Well-being Impact Test guidance	No	
Human rights Human Rights Impact Test guidance	No	
Justice system Justice Impact Test guidance	No	
Rural proofing Rural Proofing Impact Test guidance	No	
Sustainable development Sustainable Development Impact Test guidance	No	

[1] Race, disability and gender Impact assessments are statutory requirements for relevant policies. Equality statutory requirements will be expanded 2011, once the Equality Bill comes into force. Statutory equality duties parts of the Equality Bill apply to GB only. The Toolkit provides advice on statutory equality duties for public authorities with a remit in Northern Ireland.

Evidence Base (for summary sheets) – Notes

Use this space to set out the relevant references, evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Please fill in **References** section.

References

Include the links to relevant legislation and publications, such as public impact assessment of earlier stages (e.g. Consultation, Final, Enactment).

No.	Legislation or publication
1	Financial Services & Markets Act 2000: http://www.legislation.gov.uk/ukpga/2000/8/contents
2	'A new approach to financial regulation: judgement, focus and stability', HM Treasury (2010): http://www.hm-treasury.gov.uk/d/consult_financial_regulation_condoc.pdf
3	
4	

+ Add another row

Evidence Base

Ensure that the information in this section provides clear evidence of the information provided in the summary pages of this form (recommended maximum of 30 pages). Complete the **Annual profile of monetised costs and benefits** (transition and recurring) below over the life of the preferred policy (use the spreadsheet attached if the period is longer than 10 years).

The spreadsheet also contains an emission changes table that you will need to fill in if your measure has an impact on greenhouse gas emissions.

Annual profile of monetised costs and benefits* - (£m) constant prices

	Y_0	Y_1	Y_2	Y_3	Y_4	Y_5	Y_6	Y_7	Y_8	Y_9
Transition costs	6	5	5	-	-	-	-	-	-	-
Annual recurring cost	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.
Total annual costs	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.	Unqnt.
Transition benefits	-	-	-	-	-	-	-	-	-	-
Annual recurring benefits	131.6	126.3	121.2	116.4	111.8	107.5	103.3	99.4	95.7	92.1
Total annual benefits	131.6	126.3	121.2	116.4	111.8	107.5	103.3	99.4	95.7	92.1

* For non-monetised benefits please see summary pages and main evidence base section

Evidence Base (for summary sheets)

Regulatory Policy Committee

1. This impact assessment was submitted to the Regulatory Policy Committee (RPC) on 15th November 2010 for consideration. Due to changes and a desire to incorporate additional evidence, a revised version was sent to the RPC on 30th November. An opinion was received from the RPC on 14th December, which said that the analysis of potential costs and benefits of the proposal were incomplete.

2. In particular, three main areas of concern were highlighted:

   - An incomplete analysis of the administrative burdens associated with the introduction of a FSMA-style regime;
   - An incomplete analysis of impacts other than administrative impacts, for example on the current level of consumer detriment or competition, and
   - An incomplete analysis of the current regulatory framework for consumer credit.

3. In the event of a transfer of consumer credit responsibility, the CPMA would be responsible for writing a new rulebook following cost-benefit analysis and consultation with the public, as well as business and consumer representative bodies.

4. In relation to the first of the concerns noted above, we acknowledge that the current analysis lacks any quantitative estimates of the likely costs associated with the introduction of a FSMA-style regime. We have sought to gather as much evidence as possible through industry analysis and working with analytical colleagues from both OFT and FSA. However, the detail of a FSMA-style regime for consumer credit regulation would be for the CPMA to determine based on its own further analysis and consultation and as such it is not possible to provide detailed quantification of the administrative burdens associated with the introduction of the regime at this stage. We will continue to collect evidence via the consultation process and work closely with both OFT and FSA to do our best to provide estimates for the Final Stage impact assessment. In the absence of this information, we have provided comparative data on other regulatory changes, as well as independent assessments of the current burdens under FSMA to give a best estimate of the likely impacts.

5. With reference to the second concern noted above, we have been similarly hampered by a lack of evidence about the potential impact of moving to a FSMA-style regime. Estimating the impact on levels of consumer detriment is particularly difficult, given that a large proportion of this impact is likely to be largely preventative, i.e. stopping problems that have not yet developed. As identified in Annex 1 of the impact assessment (post-implementation review), it is very hard to measure the current levels of consumer detriment in relation to consumer credit, but we have identified sources of aggregate and survey data on the extent of financial difficulty and associated losses to both businesses and consumers, which is the best information we have at this stage, prior to consultation.

6. In relation to the latter part of the second concern regarding competition, we agree with the RPC that the impact assessment does not currently provide a robust analysis on the effects on competition in the consumer credit market. However, we have provided a qualitative analysis in Annex 2 of the impact assessment and are seeking views through the consultation on any further information that might help to quantify this. In addition, we would expect that market monitoring activity by OFT, or future industry intelligence collected by BIS, would help to keep abreast of any developments regarding competition, which we will analyse and include in the Final Stage impact assessment.

7. In response to the last concern, we have now included further information about the current regulatory regime under the Consumer Credit Act at the end of the impact assessment (Annex 4).

Background

Current regulatory responsibilities

8. The FSA is the UK's main financial services regulator. The Financial Services and Markets Act 2000 (FSMA) gives the FSA five statutory objectives, including 'securing the appropriate degree of protection for consumers'.[2] The FSA currently has the authority to regulate most consumer financial

[2] http://www.fsa.gov.uk/pages/about/aims/statutory/index.shtml

services and products, including insurance, investments, deposits and first-charge residential mortgages.

9. The OFT is the UK's consumer and competition authority, with a broad remit covering the whole of the UK economy. In addition to its general powers to enforce consumer and competition law, under the Consumer Credit Act 1974 (CCA, amended both in 2006 and more recently by implementation of the Consumer Credit Directive) the OFT is the licensing authority and main enforcement body for regulated consumer credit, including personal loans and the provision of goods and services on credit and related activities, such as debt collection and debt management.[3]

10. These two organisations approach their regulatory responsibilities in very different ways, which is largely determined by their respective legislative bases. Under FSMA, the FSA takes an outcomes-focused approach to regulation, setting out 11 principles which govern business behaviour.[4] Alongside this, the FSA has extensive powers to make more detailed rules, such as those regulating conduct of business for investment businesses.[5] These rule-making powers are generally subject to requirements to consult and to conduct cost-benefit analysis, with final rules set out in rulebooks which have the force of secondary legislation.

11. By contrast, CCA is more narrowly framed. It grants the OFT functions of administering the licensing system, supervising the working and enforcement of the CCA and any regulations made by it, as well as undertaking enforcement action itself. Specific conduct of business rules are contained in primary and secondary legislation under CCA, the amendment of which requires Parliamentary approval and can therefore entail substantial delays. The CCA does not grant the OFT any formal rule-making powers, although it gives the OFT a role in setting standards through powers to issue guidance on how it will exercise its functions under the CCA and on behaviours which it considers will call into question a firm's fitness to hold a licence (for example, recently issued guidance in relation to Irresponsible Lending[6]).

Extent of regulatory overlap

12. There are overlaps in authorisation – it is estimated that 16,000 firms are directly authorised or licensed under both FSMA and CCA.[7] For example, a firm may be authorised and regulated under FSMA for the provision of mortgage advice and arranging insurance and also licensed under CCA to carry on the business of consumer credit, debt adjusting and debt counselling. This can lead to several problems, including duplication of compliance costs and potential inconsistency in regulatory approach, which may lead to uncertainty for business as well as consumers.

13. However, the degree of overlap is likely to be larger than this. For example, many FSA 'Appointed Representatives'[8] (ARs) – which are not directly authorised but appointed by an authorised firm (a principal) to conduct certain activities on its behalf – also hold OFT consumer credit licences. There are currently almost 30,000 ARs active as retail intermediaries, but it is unknown precisely how many of these will also hold a consumer credit licence. Discussions with stakeholders suggest that a significant proportion may hold credit licences, but due to uncertainties it has been estimated that the total overlap in OFT/FSA-regulated population may be 23,000-52,000 firms. The table below gives some further detail on the extent of overlap for OFT licence holders by area of business activity.

[3] Certain other pieces of related legislation also form part of the consumer credit regime, for example, the Bills of Sale legislation (England and Wales only) and Part 8 of the Enterprise Act 2002

[4] http://fsahandbook.info/FSA/html/handbook/PRIN/2/1

[5] http://www.fsa.gov.uk/pages/library/policy/cp/2001/cond_bus.shtml

[6] http://www.oft.gov.uk/shared_oft/business_leaflets/general/oft1107.pdf

[7] This was estimated on the basis of how many businesses pay the Financial Ombudsman Service levy to the FSA and not the OFT; the degree of overlap is further obscured by the fact that different legal entities in the same group can be licensed/authorised by OFT or FSA and that some groups will contain multiple licensed/authorised entities

[8] Appointed representatives are expected to meet the same standards for conducting regulated activities as the principal directly authorised firm ('Principal'), but the onus for monitoring their compliance rests with the Principal rather than the FSA (for more information, see: http://www.fsa.gov.uk/pubs/other/factsheet_appointed.pdf)

Table: FSA coverage of OFT licence-holders, estimated by sub-sector

Sector	Total Sector size	Number of OFT licence holders also regulated by FSA[9]	
		Lower Bound	Upper Bound
Housing	9,500	0	1,500
Household goods & services	2,500	0	500
Personal goods & services	6,500	0	1,500
Professional & financial services	56,500	21,000	42,000
Transport	14,500	2,000	5,500
Recreational goods & services	6,500	0	1,000
Total	**96,000**	**23,000**	**52,000**

Source: BIS estimates based on OFT data[10].

14. Taking into account both directly-authorised firms and Appointed Representatives, the total FSA-regulated population is around 60,000[11], which implies that 40-90% of the FSA-regulated population are also licensed by the OFT. In contrast, there are around 96,000 extant consumer credit licence holders, which suggests that 45-75% of OFT-licensed firms are not currently regulated by the FSA.[12]

15. The OFT licence holder population includes a significant proportion of smaller businesses, with just over one-third of the total (approximately 35,000) estimated to be sole traders. Around 12% of all firms directly authorised by the FSA are sole traders and the FSA has previously stated that around 95% of the firms they regulate are small firms.[13]

16. The wide scope of the CCA means that many licensees are not financial services businesses themselves, as reflected in the estimate that only a relatively small proportion (less than 5%) are actively lending money to consumers. The remainder of the OFT-licensed community may provide access to credit, allow payment in instalments for goods and services, or provide ancillary services such as debt advice or credit reference information. Preliminary estimates suggest that around half of all current OFT consumer credit licence holders are involved in financial services, but not as their core activity. The licensed population therefore includes high street retailers, car dealers and suppliers of general goods and services.

17. The range of organisations currently authorised and supervised by the FSA is also very wide – ranging from, for example, a sole trader who advises on mortgages or a local credit union to a global financial conglomerate – and there are over 2,500 firms directly authorised by the FSA for whom financial services are not their core business; for example, in sectors such as retail, leisure and transport.

18. In addition to overlaps in the regulated population, there are also overlaps across the financial services product spectrum. For example, as the FSA is responsible for payment services, the use of credit cards as payment instruments is regulated by the FSA, but the underlying credit agreement is regulated by the OFT; mortgage products with unsecured loan elements span both regimes; current accounts with overdraft facilities are also subject to regulation by both OFT and FSA, and both organisations have an interest in the treatment of consumers in financial difficulty (e.g. where consumers have both mortgage and unsecured debts).

Advantages of a single regulator for retail financial services

19. Previous research has set out several benefits of having a single retail financial services regulator – for example, there may be economies of scale and scope available to an integrated regulator, facilitating the allocation of scarce regulatory resources more efficiently and effectively.[14] Such

[9] This includes AR s and firms that are directly authorised
[10] These are provisional estimates
[11] Comprising roughly 25,000 directly-authorised firms and 35,000 Appointed Representatives (of which approximately 22,500 are Appointed Representatives and 12,500 are 'introducer' Appointed Representatives)
[12] Recently, the OFT licensed population has been falling; furthermore, as the requirement to renew/pay a maintenance fee only applies once every 5 years, it is likely that a proportion of current licence holders will have ceased trading or will not wish to renew their licence
[13] http://www.parliament.uk/documents/upload/fsa-20070208-online.pdf
[14] 'Revisiting the rationale for a single national financial services regulator', Briault (2002)

economies of scope may be achieved through moving to a single set of central support services (e.g. information services, premises, human resources, financial control) or a unified approach to standard-setting, authorisation, supervision and enforcement for retail financial services.

20. Some of these benefits may apply to the incorporation of consumer credit with broader retail financial services supervision. For example, firms are increasingly offering products that cross the current regulatory boundaries (e.g. flexible mortgages that incorporate unsecured loan elements, linking of unsecured lending facilities to deposit accounts or current accounts with overdraft facilities), which weakens the argument for regulating consumer credit separately.

21. Therefore, a regulator which can take an integrated view of firms across the whole retail financial services sector (i.e. including consumer credit) should be in a stronger position to identify and respond to emerging risks, through supervision and analysis of industry and market-wide issues. This ability would also be enhanced by having the regulator operate within a flexible framework that allows it to consult, make and amend rules without needing to seek Parliamentary approval for the implementation of primary or secondary legislation. The overall result is that there could be a reduction in costs for the regulator compared to the current system.

22. There should also be benefits to consumers from having a consistent approach to retail financial services regulation and applying the same high-level standards and sanctions to all segments of the market. Granting the regulator a wider range of enforcement powers for consumer credit regulation (as available under FSMA) should increase its ability to encourage compliance and reduce detriment to consumers.

23. There should also be a reduction in the compliance costs for businesses that are currently subject to dual regulation. Dual-regulated businesses should benefit from the elimination of competing demands from two regulators, duplication of supervision and from a reduction in unnecessary complexity by simplifying the current regime.

Scope for change to regulatory framework

24. The overlap between the OFT's consumer credit licensing function and the FSA's regulatory duties was raised as part of the Hampton Review in 2005, which recommended consideration of steps to reduce the risk of regulatory duplication and lack of co-ordination.[15] However, following consultation with a range of stakeholders, the previous Government announced that it would prefer to address these concerns by closer working between OFT and FSA, rather than structural reforms.[16] At the same time, the OFT and FSA published a Joint Statement of Intent announcing their intention to collaborate more closely on matters of joint regulatory interest and subsequently published a Joint Action Plan outlining improvements made and further improvements planned to the way they dealt with firms that are regulated by both the OFT and FSA.[17]

25. However, the recent consultation by HM Treasury[18] included proposals to reform the institutional framework for financial regulation in the UK. As part of these reforms, a new consumer protection and markets authority (CPMA) will be created, which will be a focused conduct of business regulator with the primary objective of ensuring confidence in financial services and markets, with a particular focus on protecting consumers and ensuring market integrity. In taking over part of the FSA's role, the CPMA will take a tougher, more proactive and more focused approach to regulating conduct in financial services and markets than has the FSA. This change presents an opportunity to consider whether any potential structural shortcomings in the UK regulatory framework for retail financial services might be addressed by combining consumer credit with other retail financial services regulation.

Issue

26. As set out above, the regulatory framework for retail financial services is split between the FSMA and the CCA. This division is felt by many to be sub-optimal, which leads to several problems:

- Split accountability for some objectives;
- Lack of coherence in consumer protection and market oversight;
- Confusion and duplication for firms and consumers;

[15] http://www.berr.gov.uk/files/file22988.pdf
[16] http://webarchive.nationalarchives.gov.uk/+/http://www.hm-treasury.gov.uk/d/hampton_compliance281106.pdf
[17] http://www.fsa.gov.uk/pubs/other/OFT_FSA_Actionplan.pdf
[18] http://www.hm-treasury.gov.uk/consult_financial_regulation.htm

- A regulatory regime that is too reactive and insufficiently flexible, and
- Deterrence to effective deregulation.

Split accountability for some objectives

27. Accountability for some objectives relating to retail financial services is split between the OFT, FSA, Trading Standards Services[19], specialist Illegal Money Lending teams, the Department for Enterprise, Trade and Investment in Northern Ireland (DETINI), the Department for Business, Innovation and Skills (BIS) and HM Treasury.
28. This can be made to work most of the time, helped by concordats between the relevant organisations, and can indeed deliver benefits. But for the market as a whole, no single organisation is clearly accountable for performance against a set of clear statutory objectives.

Lack of coherence in consumer protection and market oversight

29. The split in responsibility makes it difficult for regulators to take a strategic view of priorities across the entire retail financial services sector. Decisions are driven by different legal duties and powers of individual regulators. Having two regulatory regimes for what is often from the consumer's perspective a single product or service (such as personal current accounts with overdrafts or flexible mortgages) can result in different rights and divergence in protection for personal and small business consumers.
30. In their submission to the Trade & Industry Select Committee, the British Bankers' Association (BBA) proposed that further consideration be given to the transfer of responsibilities for consumer credit to the FSA, "…as it seems incongruous that all financial services are regulated by the FSA, with the exception of consumer credit".[20] They also expressed a preference for a more co-ordinated approach to investigation (so that banks were not subject to multiple overlapping investigations and data requests), as well as a common communication approach to reduce/eliminate conflicting messages about approaches to issues.
31. However, such views are not shared by all lenders, or by all businesses; some trade associations have expressed a preference for consumer credit responsibilities to remain with the OFT. It has been submitted that a shift to another regulator, even though well-intentioned, could stifle and depress a market that calls for relatively light-touch control. It could be argued that the discrete characteristics of the unsecured lending market – lower consumer risk, specific Directives within European law, separate and well-established UK legislation (Consumer Credit Acts 1974 and 2006) and its own risk flow (with funds moving away from the supplier, in contrast to investment and insurance) – justify a distinct approach.
32. Even though some firms that are currently dual-regulated (e.g. banks and large finance houses) may favour a single regulator for administrative convenience, for many firms there would be no direct benefit in terms of greater coherence as they already only deal with one regulator (i.e. the OFT). Some stakeholders believe that the credit sector overseen by the OFT has been relatively stable, in spite of extensive legislative change. A change in regulator, particularly one with limited experience of a wide and highly complex sector, could potentially be counterproductive in terms of uncertainty and upheaval.
33. A single regulator for retail financial services would be better placed to deal rapidly and effectively with emerging consumer protection concerns, such as the recent debate around the right of 'set-off'.[21] The current regulatory arrangements – where treatment of customers regarding credit agreements is covered by the Lending Code, but treatment of customers regarding bank accounts is regulated by the FSA – means that there are challenges in developing a coherent policy response to this emerging issue.
34. Such problems may have been exacerbated by the recent deterioration in macroeconomic circumstances, leading to potentially significant costs being imposed on consumers and the economy more widely.

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[19] For example, Trading Standards Services currently have powers to prosecute under the CCA (and take enforcement action under the Enterprise Act 2002) and consequently collect evidence on the activities of licence holders (which contributes to market oversight), provide local advice to businesses on credit matters, supply intelligence to OFT for licensing purposes and monitor compliance with OFT sanctions.

[20] http://www.publications.parliament.uk/pa/cm200607/cmselect/cmtrdind/591/591we07.htm

[21] 'Set-off' is a practice by which financial institutions can use money available in one account (e.g. a current account) to repay an outstanding debt (e.g. a loan)

Confusion and duplication for firms and consumers

35. As set out above, the separate regulation of consumer credit and other retail financial services can be incongruous and confusing for consumers and firms. The regulatory overlap means that some firms have to seek authorisation from two bodies (even across single products) and meet two separate sets of rules. Dual regulation of firms that are both FSA-authorised and OFT-licensed can lead to duplication of costs in terms of compliance and supervision.

36. In their submission to the Trade & Industry Select Committee in 2007, the Finance and Leasing Association (FLA) felt that the separate regulation of consumer lending from other retail financial services did not make any sense other than for administrative convenience.[22] This dual regulation, from "two different regulators with very different statutory powers and two very different ways of regulating", led to significant compliance costs (mainly due to the duplication of administrative burdens in many areas) including placing conflicting or competing demands on members' businesses.[23] A further risk identified by the FLA was the potential for regulatory creep, as members may find it more convenient to apply the highest level of regulation to their activities, even though some of those activities may not be directly subject to the regulation applied.[24] Overall, the FLA's preference was for one body with clear objectives and guidelines, rather than two bodies 'policing' different industry guidance and codes in different ways.

37. In more recent representations to BIS, the FLA has expressed concerns that further change could lead to regulatory uncertainty and disruption, which could reduce market capacity even further. Nevertheless, the FLA feels that any change to the regulatory architecture should be seen as an opportunity to simplify and improve the current regime, to prevent unnecessary complexity and deliver a single body of rules.

38. In their recent response to the Conservatives' White Paper on financial services, the Confederation of British Industry (CBI) commented that "the split of responsibilities for consumer regulation of financial services between the OFT and the FSA has been confusing at best, and administratively problematic and damaging at worst."[25] The CBI thought it sensible to combine the supervision of consumer activity in a single entity, which they felt would remove the duplication and confusion arising from both the FSA and OFT having a role in supervising consumer credit.

39. The CBI considered the advantages of such a single regulator to include: simplified training and systems for lenders, resulting in cost savings over the longer term; more coherent lending practice, lessening the potential for confusion amongst consumers, advisers and lenders, and more consistent regulations and guidance across the financial services sector.[26] Last, the CBI commented that initiatives aimed at addressing specific problems in the credit market could have unintended consequences, such as reducing the supply of affordable credit to consumers. An integrated cross-industry approach could therefore deal with some of these potential pitfalls.

A regulatory regime that is too reactive and insufficiently flexible

40. The fast pace at which the UK credit market has developed in recent years, combined with the dynamic nature of product development, has not always been matched by changes to the legislative and regulatory framework. This may have contributed to problems where legislation has been slow to respond.[27] The 2006 CCA, which significantly reformed the 1974 CCA, was the first major overhaul of consumer credit legislation for 32 years. Furthermore, many requirements of the CCA regime are enshrined in the Act itself, meaning that primary legislation can be needed even to make relatively small changes. For example, the CCA imposes requirements on lenders as to what information should be provided to consumers in a particular circumstance. While the precise detail is generally in secondary legislation, changing which consumers receive information and when will often require amendments to primary legislation.

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[22] http://www.publications.parliament.uk/pa/cm200607/cmselect/cmtrdind/591/591we12.htm
[23] The overlap between OFT and FSA on FLA members' businesses varies widely and depends largely on member business models and product range; good examples of overlap include advertisements and financial promotions, and brokerage advertisements for secured lending
[24] For example, FSA high-level principles may be applied to FSA-regulated general insurance activities, as well as OFT-regulated loan activities under the Consumer Credit Act
[25] http://www.cbi.org.uk/pdf/20091006-cbi-conservatives-white-paper-response-final.pdf
[26] See footnote 25
[27] For example, recent issues raised in respect of consumer credit legislation include Claims Management Companies' involvement with potential unenforceability of certain credit agreements, and the requirement to issue periodic statements to 'goneaway' consumers or those in an Individual Voluntary Agreement (IVA)

41. The FSMA model, in contrast, could allow for more flexible approaches to informing consumers. Concerns have also been raised that the consumer credit licensing system has not worked sufficiently well to protect consumers from abuse by some financial service providers.[28] In many cases, the OFT lacks direct powers to outlaw emerging unfair practices across the board, relying on the deterrent effect of individual enforcement cases which can be subject to lengthy appeal. The FSMA regime, in contrast, is characterised by more proactive supervision.

42. The OFT's powers were significantly updated in the Consumer Credit Act 2006, ensuring that it had an effective range of sanctions to enable it to take meaningful and timely action in respect of emerging practices that it considers may call into question firms' fitness to hold a licence. These reforms came into force almost 35 years after the regime was established and were the culmination of a six year-process of policy debate, legislative passage and implementation. Likewise, the fact that many detailed rules are enshrined in legislation means it is not easy to correct unintended consequences which place unnecessary burdens on firms, or to amend rules in order to support beneficial innovations – for example, in making them appropriate for a world in which financial services are increasingly remotely delivered through the phone or internet. This has potentially also acted as a deterrent to effective deregulation.

43. A number of consumer organisations are critical of the current regulatory arrangements. For example, in a recent submission to BIS, Citizens Advice stated that the current system for regulating consumer credit cannot adequately protect all consumers and is, in their view, under-resourced, too slow to respond to problems in the market and too reactive.[29] They would prefer a consumer credit regulator to have rule-making powers to set standards, to deal with (including prohibiting) detrimental practices, terms and products directly. In addition, Citizens Advice feels that the current consumer credit licensing regime is too focused on firms, rather than the market as a whole, with enforcement based on sanctioning bad practice rather than setting standards, which results in chasing detriment through legal processes rather than preventing it through regulatory standard-setting.

44. However, it should be noted that CCA allows OFT to issue guidance on behaviours and practices which it considers call into question a firm's fitness to hold a consumer credit licence. For example, it has issued guidance in relation to irresponsible lending (see above), debt collection[30] and debt management[31]. This power to issue guidance can make clear what behaviours the OFT views as unacceptable, but there are significant limits under this power on the OFT's ability to require specific behaviours or actions. In contrast, under FSMA the FSA has quite broad rule-making powers that can deal with emerging issues much more quickly and efficiently. It should be noted that such powers, however, are not likely to be used very regularly – constant changes can be particularly damaging to market participants and could significantly add to compliance costs, and all proposed rule changes are generally subject to detailed consultation and cost-benefit analysis. Nevertheless, this process would likely still be more reactive and flexible than the requirement to make changes via primary legislation.

Deterrence to effective deregulation

45. As set out above, the usual requirement for primary legislation to amend the CCA (except where change is required by European law or where the Legislative Reform Order procedure is available) makes it very cumbersome to deregulate. This has meant that even simple changes, such as the uncontroversial change to remove the requirement to send information to people who are no longer at an address, are still outstanding. Reframing the regulatory regime for consumer credit offers the potential for wider deregulation (subject to EU constraints) which could deliver benefits for both businesses and consumers and would provide for more rapid and effective resolution of unintended effects in future.

Rationale

46. On balance, evidence from stakeholders indicates that the current regulatory arrangements for consumer credit may not be optimal. Several problems have been identified as stemming from the current regulatory framework for consumer credit: split accountability for some objectives; lack of coherence in consumer protection and market oversight; confusion and duplication for firms and

[28] http://www.publications.parliament.uk/pa/cm200607/cmselect/cmtrdind/591/591we10.htm
[29] http://www.citizensadvice.org.uk/print/bis_credit_and_debt_review_-_initial_indication_of_strategic_issues-2.pdf
[30] http://www.oft.gov.uk/OFTwork/publications/publication-categories/guidance/consumer_credit_act/oft664
[31] http://www.oft.gov.uk/shared_oft/business_leaflets/credit_licences/oft366.pdf

consumers; a regulatory regime that is too reactive and insufficiently flexible, and deterrence to effective deregulation.

47. Currently, regulatory overlap between the FSA and the OFT can make compliance administratively problematic (where there may be competing demands) and potentially increase costs for businesses. Where the same financial products are regulated separately under FSMA and CCA (e.g. mortgages with unsecured loan elements, current accounts with overdrafts), this can hinder the development of effective and timely policy solutions to solve potential issues for consumers as they emerge.

48. Where such problems are not dealt with quickly, the costs that are borne by businesses and consumers will continue to be incurred. Compared to a situation where alterations to consumer credit rules require Parliamentary approval (as under the CCA), the ability to adjust rules more quickly should help to avoid these costs when they materialise.

49. This opportunity provides scope for increased resources to be allocated to the protection of consumers, some of whom may be vulnerable and/or in severe financial difficulties, from exploitation and harassment – for example, by debt collectors, debt managers or doorstep lenders. By expanding the remit of the regulatory regime for retail financial services to include consumer credit, there is also scope to promote better outcomes for consumers.

50. Finally, broadening the responsibilities of the CPMA to incorporate consumer credit could facilitate the realisation of economies of scope with other products and services subject to regulation by the CPMA. As a result, this could reduce the overall average cost of regulatory oversight for CPMA-regulated firms.

Policy objectives

51. The Government believes that there remains a fundamental weakness caused by the split in responsibility for retail financial services regulation between the CCA and FSMA regimes. In addition, it has concerns about regulatory overlap and sees opportunities to improve consumer protection in relation to consumer credit.

52. The objective of intervention is to provide a consumer credit regime that can respond quickly and efficiently to problems as and when they emerge, so that any costs borne by consumers and/or businesses as a result are minimised. Improved oversight should help to improve the overall quality of lending, reducing the incidence of unsustainable borrowing, such as write-offs associated with consumer lending (which exceeded £5bn in the first half of 2010). By providing consistent treatment of different financial products and services, consumers should be able to make decisions with more certainty, leading to a more efficient credit market.

53. The Government's ambition is to create a world-class regulatory regime that keeps pace with a dynamic consumer credit market; responds to actual or potential gaps in consumer protection; and places a proportionate regulatory burden on business. Any new consumer credit regime should be flexible enough to respond to innovation in the consumer credit market, yet give as much certainty as possible to both industry and consumers. In considering whether or not to proceed with the transfer of consumer credit regulation to a FSMA-style regime, the Government will therefore be guided by the following objectives:

- **Clarity, coherence and improved market oversight**: A new regime should provide greater regulatory coherence, a single point of accountability and ensure consistent treatment of similar firms and products. The Government wants more compatible rules, approaches and terminology to be applied to similar or competing products, including those that currently span the two regimes. The regime should be properly resourced and have the necessary powers to secure better market information and ensure earlier identification of risks to consumers and market confidence. The Government also wants to reduce the compliance and administration burdens for firms currently regulated under different regimes by both the FSA and the OFT.

- **Effective and appropriate consumer protection, including through a responsive and flexible framework**: Consumer protection is at the core of consumer credit regulation. The Government wants a regime that at least maintains, and where possible strengthens, overall protection for consumers, including small businesses. This does not mean eliminating all risk, or removing responsibility from consumers. The Government wants consumers to benefit from a broader range of enforcement powers that can be applied flexibly and the more pre-emptive approach to consumer protection to be taken by the CPMA. The regime should have the scope to make and amend rules without the need for primary legislation but with appropriate public consultation and cost-benefit analysis processes in place.

- **Simplification and deregulation:** The new consumer credit regime should promote opportunities for simplifying rules and regulation, removing any unnecessary burdens on firms that are not justified by the benefits to consumers.
- **Proportionality and cost effectiveness:** Finally, a new regime should be proportionate and fair, with resources within the regulatory regime allocated effectively.

Options analysis

54. Ideally, any option would be evaluated relative to a base case of 'do nothing'. However, this consultation should be considered in the context of the Government's Public Bodies Bill announcement and the statement by the Secretary of State for Business, Innovation and Skills on 14 October 2010[32], and their implications for the future of the OFT. As part of a wider review, the Government will be publishing consultations in early 2011 to determine the future location of certain competition and general consumer functions that currently fall to the OFT.

55. As these consultations have yet to take place, we cannot be certain that the OFT will continue to be operating in its current form under our 'do nothing'. Therefore, our base case here is that the CCA remains in place and the regulation of consumer credit would remain separate to other retail consumer financial services. Unfortunately, the permanent regulatory authority with responsibility for the CCA regime under this option would not be confirmed until the outcome of the above consultations. If a decision is made to retain the CCA regime, the Government would consider the most appropriate regulatory authority for the CCA regime following the conclusion of wider work on the future of the competition and general consumer functions of the OFT, and would issue a further consultation on this if necessary.

56. Therefore, in relation to the issue of reform of consumer credit regulation, we have only considered the potential for regulating consumer credit under a Financial Services & Markets Act (FSMA)-style regime enforced by the CPMA. This would also involve replacing the CCA with new rules, which the CPMA would be responsible for writing and consulting on. This is Option 1, the Government's preferred option.

Alternatives to regulation

57. In identifying potential options for reform, non-regulatory options are unlikely to satisfactorily achieve the objectives set out above.

- self-regulation

58. A layer of voluntary self-regulation already exists in respect of 'mainstream' consumer credit (loans, credit cards and current account overdrafts) provided by banks, building societies and credit card companies in the form of the Lending Code[33], monitored and enforced by the Lending Standards Board[34], and applies to dealings with consumers, micro-enterprises and charities with an annual income of less than £1m. The Finance and Leasing Association (FLA) represents store card providers, second-charge mortgage lenders and a range of other non-bank lenders. The FLA requires its members to adhere to its Codes, although these are not separately monitored and enforced. Outside of the lending sphere, an OFT-approved code of conduct has been established by DEMSA (Debt Managers Standards Association) to promote good practice in the debt management industry, and to protect the interests of the public and the creditors to whom they owe money.[35]

59. However, broadening the remit of existing self-regulatory bodies to incorporate all aspects of unsecured lending – such as home credit or payday lending – is unlikely to be feasible and may not be consistent with European obligations. Moreover, it is likely that self-regulation would result in weaker consumer protection, as an independent public regulator (backed by statutory rules) offers a more effective method of deterrence and enforcement. For example, evidence from other areas of financial services indicates that self-regulation is not always most effective, with FSA intervention

[32] http://www.bis.gov.uk/consumer
[33] http://www.lendingstandardsboard.org.uk/docs/lendingcode.pdf; a revised code is expected to be launched at the end of March 2011
[34] http://www.lendingstandardsboard.org.uk/
[35] http://www.demsa.co.uk/code-of-conduct/

replacing industry-based codes of conduct (such as the Mortgage Code, which was replaced by statutory regulation in 2004).

60. In addition, a self-regulatory approach would not realise the potential economies of scale and scope or exploit the synergies associated with a single regulatory regime for retail financial services, as regulation of consumer credit would remain separate from the regulation of other retail financial services. A self-regulatory solution would also not offer any scope for enhancing oversight of firms and enforcement powers.

61. Nevertheless, self-regulation can play a valuable role in responding to problems in the market quickly, delivering better outcomes for consumers while keeping the formal regulatory burden to a minimum. If consumer credit were transferred to a FSMA-style regime, the CPMA would need to consider and consult on whether a reformed consumer credit regime could formally incorporate provisions set out in existing voluntary codes or whether such provisions should remain the subject of self-regulation, perhaps with provision for CPMA confirmation of industry guidance.

One in, one out

62. The option below includes a substantial deregulatory element (the repeal of the Consumer Credit Act and associated regulations), which would count as an 'out' under better regulation principles. As we do not yet have a firm idea about the precise balance between what may be proposed for introduction (and/or removal) under a new regime following consultation, we do not yet have firm estimates about the costs associated with this option (and hence its deregulatory elements). Nevertheless, we will keep the situation under close review and, for those proposals brought forward following consultation that would constitute an 'in', if additional deregulatory measures ('outs') are required, these will be identified as appropriate.

Option 1: FSMA-style regulation under CPMA

63. Integrating the consumer credit functions of the OFT into the CPMA will require legislative change. Under this option, the CPMA would become responsible for the consumer credit regime and would be given rule-making powers in the area of consumer credit regulation. The Government proposes that the legal framework for the CPMA's powers and functions would be based on the model set out in FSMA, with modifications made to enable the CPMA to carry out its conduct-focused responsibilities more effectively. The CCA would therefore be repealed and replaced with requirements following the FSMA model.

64. However, the detail of a FSMA-style regime for consumer credit regulation would be for the CPMA to determine based on its own further analysis and consultation, and subject to the constraints imposed by EU law (such as the Consumer Credit Directive) and the structure of the new CPMA regime. In doing so, the CPMA would draw on the experience and expertise of the OFT and Trading Standards Services.

65. Without seeking to pre-empt the CPMA's process of analysis and consultation, this section provides an outline of key elements that a FSMA-style framework for consumer credit regulation might incorporate. Important areas of the current FSMA regime which might be applied to consumer credit firms under the Government's preferred option could include:

- Supporting materials required for authorisation applications (e.g. business plan, compliance procedures, balance sheets, cashflow forecasts);
- Threshold conditions elaborating on minimum standards set out in FSMA that firms must meet and continue to meet in order to carry on a regulated activity (e.g. required legal status, location of offices, adequate resources);
- Approved persons regime for those performing a role of particular regulatory significance or a 'controlled function' (e.g. director, compliance officer);
- Principles for businesses setting out the fundamental obligations of all authorised firms;
- Rule-making powers – subject to requirements for consultation and cost-benefit analysis – that reside with the regulator, unlike CCA, where rules are set out in statute and rule-making authority therefore resides with Parliament;
- Specific conduct of business and prudential rules (e.g. solvency requirement, minimum capital requirements);
- Regular reporting requirements, and

- An enforcement regime providing a broader range of sanctions than the CCA regime (e.g. higher maximum fines on firms and individuals).[36]

66. Many of these requirements have some equivalents in the CCA regime: both regimes, for example, apply tests at the licensing/authorisation stages to determine whether firms are fit to operate in the relevant market and do not pose undue risks to consumers. It is also likely that a large number of consumer credit firms would already meet such requirements if the CPMA were to consider it appropriate to impose these following consultation. Responsible and professional firms would be expected, for example, to hold adequate capital for the operation of their business, and firms already subject to the CCA regime should be treating their customers fairly and have competent and appropriate staff in key positions.

67. Some of the provisions would, however, result in more routine formal contact with the regulator for many firms not already authorised by the FSA or would represent a new formal obligation (for instance, the potential for a specified minimum capital requirement). These would need to be considered in the context of the costs and benefits they may confer and taking into account the nature of the products and services in question.[37]

68. The FSA's current risk-based approach to regulation allocates regulatory resources according to the risk a firm poses to the FSA's statutory objectives, with risk assessed on the basis of impact (scale and severity of the effect on consumers and the market if risk was to crystallise) and probability (likelihood of risk crystallising). This determines the nature and intensity of the regulatory relationship between the firm and the FSA. Medium and high-risk firms are allocated a relationship manager who carries out a risk assessment and determines a risk mitigation programme. High-risk firms are supervised on a 'close and continuous' basis and the small number of very high impact firms are subject to the most intensive and intrusive supervision. As smaller firms can pose a collective risk to the FSA's objectives, the risk-based supervisory approach has been adapted for these firms – information is collected from a variety of sources (e.g. regulatory returns, complaints data and thematic assessments); data analysed to identify collective risks; further investigation conducted where necessary, and research results communicated or enforcement action taken against individual firms.

69. The Government expects that the CPMA will also apply outcomes-focused regulatory requirements proportionately following consultation and cost-benefit analysis. For firms that are already relationship-managed (e.g. many large credit institutions and credit card issuers) consumer credit supervision could be rolled into their existing supervisory arrangements. For a small number of firms, this may change their impact categorisation. A horizontal thematic supervision programme could be considered for higher-risk activities undertaken by small firms. Small firms undertaking lower-risk activities could be monitored via their regulatory returns and complaints-led intelligence. In the event of a transfer of consumer credit responsibility, the CPMA would in a similar way consider the costs and benefits of additional requirements; ensure proportionate application of regulatory tools, and adapt current risk metrics to accommodate the diverse range of credit activities and the specific risks which may affect consumers of credit and debt services.

Costs

70. There are likely to be a range of costs associated with this option, both one-off (e.g. familiarisation costs, one-off compliance costs, reorganisation costs) and ongoing (e.g. increased costs of CPMA authorisation, monitoring and enforcement, paid through CPMA fees; costs of prudential requirements[38]). Almost all of these costs will be borne by consumer credit firms, either directly (e.g. through staff training for new rules or completing regulatory returns) or indirectly (i.e. costs recovered through higher regulatory fees). However, the nature and scale of these costs will depend on their supervisory relationship with the CPMA.

[36] Under the FSMA regime, however, breach of a rule does not constitute an offence, nor does it make a transaction void or unenforceable (two important sanctions for breach of a statutory provision under the CCA regime)

[37] Regulatory reporting requirements, for example, can be an important tool for effective supervision, helping to identify areas of concern early, reducing the potential for detriment to consumers, and enhancing availability of information on market activity. Adequate resources requirements would, among other things, provide funds to enable a more orderly wind down of a firm, thereby helping to protect its customers and other businesses.

[38] Prudential requirements for small firms are normally not much in excess of what a sensibly-run business would retain to deal with contingencies. Further consideration would be needed to determine what prudential requirements (if any) would be appropriate for firms currently regulated by the OFT, as the CCA does not currently require the prudential regulation of OFT licence holders.

71. Whilst a rulebook approach brings with it a greater ability to be more proactive and react effectively and quickly to market developments, it is also likely to result in new obligations on some firms in a number of areas. The precise elements of a credit rulebook would be subject to further consultation.

72. There is no doubt that additional requirements placed upon FSMA-regulated firms can be beneficial, conferring advantages in consumer protection and improved market oversight. However, the Government recognises the importance of ensuring that compliance burdens for lenders and intermediaries remain proportionate and appropriate to the risks posed by the consumer credit sector, and that any increases in costs reflect real and justifiable benefits for consumers and the market. Mitigating the effect of increased compliance costs – particularly where these could have a disproportionate impact on small firms – would be essential in minimising the risk of market exit and the resultant possibility of reduced competition; restricted supply of regulated credit, and increased unauthorised trading.

Current authorisation under FSMA

73. A transfer of consumer credit responsibility to a FSMA-based regime could also provide an opportunity to explore how models provided for under FSMA that have proved successful in other regulatory contexts may be applied to consumer credit firms. These could play a useful role in protecting firms from disproportionate costs and benefit both firms and consumers. It may be possible, for example, to mitigate compliance burdens through an appointed representatives model for certain categories of credit activity or provisions akin to the OFT's current group licensing regime.[39]

74. For those OFT-licensed firms who are also directly authorised by the FSA (of which there are estimated to be 16,000), there will be one-off costs in applying for a variation of permission to account for the additional consumer credit-related activity, and ongoing costs associated with potential additional compliance requirements. For OFT-licensed firms who are currently Appointed Representatives of an FSA-authorised firm (see below) there may be additional ongoing costs associated with compliance requirements.

75. For those OFT-licensed firms who are not already authorised by the FSA, the changes (and hence associated costs) are likely to be more significant. It is estimated that there are currently 40,000-70,000 such firms, but it is likely that a proportion of these are either no longer active or may not wish to renew their consumer credit licence.

76. An alternative to direct authorisation is provided by the Appointed Representatives (AR) regime.[40] An AR is allowed to carry on regulated activities on behalf of an authorised firm (the Principal), under a contract by which the Principal accepts responsibility for the regulated activities carried out by its AR (or ARs). This reduces the regulator's supervisory burden, as the authorised firm (Principal) takes responsibility for ensuring that ARs are 'fit and proper' to deal with clients on behalf of the authorised firm, among other responsibilities. Depending on the type of business and customers, an AR may have more than one Principal.

77. However, the option of an AR model will depend on the nature of the regulated activity, not the size of the firm. For example, in the current FSA regime some activities (e.g. deposit taking) will require direct authorisation, while other lower-risk activities (e.g. retail intermediaries) can take the AR option. It is not yet possible to say what consumer credit activities may be suitable for the AR model, but certain forms of credit broking may be potential candidates.[41]

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[39] The current consumer credit licensing regime allows professional and other bodies to apply for group licences to cover members of the group for specific credit activities (e.g. UK law societies, National Association of Citizens Advice Bureaux). There is currently no group licensing regime under FSMA; separate provision is made for members of professional bodies who carry on regulated activities in the course of their profession, where they are supervised by their professional body without being regulated by the FSA. Adapting the current regime to enable greater use of such models may provide a useful mechanism in contributing to a proportionate regulatory approach, with a particular focus on lower-risk categories of firm.

[40] http://www.fsa.gov.uk/pubs/other/factsheet_appointed.pdf

[41] In this case, it may be possible that creditors could appoint certain brokers as ARs – who would then be exempt from authorisation and for whose compliance the creditor would be liable – reducing compliance burdens for retail credit brokers compared to full authorisation. Experience of the current regime suggests that finance companies often already lead on or support the legislative compliance of, for example, franchised motor dealers undertaking credit brokerage activities and as such that this approach might be applicable to these sorts of firms, subject to further analysis of feasibility and potential risks to consumers. It is estimated that a significant proportion of the nearly 30,000 FSA appointed representatives currently active as retail intermediaries are also licensed by the OFT

78. It would be important to ensure that the design and scope of an ARs model retained sufficient leverage over firms to avoid consumer protections being compromised (in line with the current obligation for Principals to be authorised firms and to have adequate controls and resources to ensure that their ARs are fully compliant with relevant regulatory requirements) and in particular to consider risks associated with an AR regime for activities which are considered high-risk under the current OFT risk model.

79. Any AR model would also have to satisfy the requirements for regulation of credit intermediaries contained in the Consumer Credit Directive and it would be essential to assess carefully burdens on business that might arise where a Principal contracts a large number of intermediary firms and possible effects on competition and availability of credit if they consequently restrict their networks.

80. For those businesses that merely introduce customers to credit and/or ancillary services (or distribute marketing material), becoming an Introducer Appointed Representative (IAR) may be more appropriate. Fewer rules apply to an IAR, but the relationship with the Principal is the same and both parties have the same responsibilities.

81. In extreme cases, it may be that the burden of compliance for some firms to continue with their existing credit-related activities is too high. In this case, such firms may leave the market.

Benchmarking

82. As we do not have detailed data on the likely costs associated with this specific change – both for regulated firms and consumers – we have sought to identify a suitable comparator that may be used to help benchmark our estimates. In terms of previous analysis that has been conducted, it is felt that the analysis conducted by the FSA for the establishment of a statutory regime for first-charge mortgage lenders and insurance intermediaries[42]may be relevant, however the comparison is not without its flaws.

83. The above regulatory change shares some similarities with this proposed change, as it reflects a mix of relatively few high-impact firms that the FSA already supervises closely, combined with a larger number of small firms with which the FSA previously had no relationship. However, there are also significant differences: for example, the population of mortgage/general insurance intermediaries and firms currently holding a consumer credit licence differ in terms of size, distribution, sophistication, systems and activities performed. In addition, such firms were not previously subject to an extensive statutory regime along the lines of CCA, so the precise compliance challenges faced, particularly in terms of systems changes, will have been different. Finally, the data for this analysis was gathered in 2002 and could therefore be significantly out-of-date. Notwithstanding such potential drawbacks, in the absence of better comparators we believe that this provides a useful indicator of potential costs.

Q1: Do you have any views on the extent to which the above markets are comparable with the consumer credit market?

Transition costs for extending CPMA responsibilities (institutional change costs)

84. Under this option, there would be one-off costs to the regulator (generally recouped through fees levied on the regulated population). A recent report by the NAO looked at the costs associated with central government reorganisation.[43] By modelling 51 of the 90-plus organisational changes that have taken place between May 2005 and June 2009, they estimate that the average one-off cost per reorganisation is around £15m.[44] In terms of the composition of these costs, the largest proportion (just over 40%) was made up by staff costs[45], followed by IT costs (almost 20%) and accommodation (15%).[46] However, it is likely that some of these costs would be incurred through establishing the CPMA in any case – for example, the recent HM Treasury consultation on the

for credit brokerage activities (for example, independent financial advisers; motor dealers; and other retailers brokering both credit and insurance).

42 http://www.fsa.gov.uk/pubs/cp/cp174.pdf

43 http://www.nao.org.uk/publications/0910/reorganising_government.aspx

44 The most costly reorganisations were those involving mergers of multiple organisation or units that were removed from existing organisations, which typically involved gross costs of around £25 million

45 Including 17% on redundancy costs and 12% on increases to staff salaries as a result of pay harmonisation

46 However, this estimate does not include all relevant (direct and indirect) costs, such as impacts on third parties (e.g. stakeholders and customers) and losses of institutional memory and strategic focus; in addition, it does not encompass 42 (mainly smaller) reorganisations

creation of the CPMA (along with other bodies, such as a Prudential Regulation Authority) estimates that transition costs could amount to around £50m.[47] It is therefore important to consider only those costs which are associated with specifically transferring the consumer credit responsibilities of the OFT to the CPMA.

85. In relation to this proposed transition, the FSA has recently estimated that one-off IT costs associated with updating existing systems to accommodate all OFT-licensed firms would be £3m-4m. If the above cost proportions calculated by the NAO are taken to be representative, this would imply an overall one-off cost for transferring consumer credit to the CPMA of £15m-20m. However, feedback from organisations who have recently undergone transitions similar to the one considered here implies that the likely cost could potentially be significantly less than this, i.e. **up to £5m in one-off costs**.[48]

Q2: Do you have any evidence on the likely transition costs associated with extending CPMA responsibilities that could help to inform this estimate?

Costs for creating FSMA-style rules for consumer credit (regime change costs)

86. An additional cost incurred by the regulator (again, paid for by regulated firms) will be those associated with developing rulebook-based material to replace the CCA, which would be repealed under this option. Preliminary analysis indicates that such an exercise may take at least 2 years and require substantial input of legal expertise, but without more detail it is not possible to quantify this.

Q3: Do you have any evidence about the likely level of costs associated with creating FSMA-style rules for consumer credit?

Costs to lenders already regulated under FSMA (regime change costs)

87. There would also be costs incurred under this option for regulated firms, the scale of which depends on whether they already have some form of supervisory relationship with the FSA. As set out above, for those firms that are directly authorised by the FSA (of which it is estimated that there are 16,000) there are likely to be both one-off costs – associated with a variation of permission of their existing FSA authorisation to account for the additional consumer credit-related activity – and ongoing costs through any increase in compliance burden from the expansion of their CPMA-regulated activities. Costs for those firms that are currently Appointed Representatives would only incur increases in ongoing costs, unless they subsequently sought direct authorisation.

Q4: Are there any other sources of cost that may be incurred by firms already regulated under FSMA?

88. Currently, the application fees associated with a variation of permission range from £750 to £12,500, depending on the complexity of the relevant activity (and hence what 'fee block' the firm belongs to).[49] For example, fees for variations to accommodate 'straightforward' activities (e.g. friendly societies, insurance intermediaries) are much less than for 'complex' activities (e.g. deposit taking, insurance provision). Preliminary analysis indicates that around 16,000 directly-authorised firms are also OFT licence holders. Classification of these firms into fee blocks based on their primary category of activity suggests that the majority of these dual-regulated directly-authorised firms are likely to be 'straightforward' variation of permissions, as will some Principals (e.g. small retail intermediaries with a handful of ARs), while other Principals are likely to be 'moderately complex'. Matching these categories to application fee levels implies a total **one-off cost of £12m-15m**. An implicit assumption has been made that all relevant firms (i.e. around 16,000) would apply for a variation of permission, but this may not be the case.

Q5: Do you agree with this estimate for application fees paid to CPMA for direct authorisation? Please provide any evidence that could help to refine this.

89. These firms would also be subject to changes in regulatory requirements in relation to their consumer credit-related activities (following the repeal of the CCA and re-writing of rules) that may

[47] http://www.hm-treasury.gov.uk/d/consult_financial_regulation_ia.pdf
[48] The FSA estimated that establishing a regulatory regime for first-charge mortgage lenders and insurance intermediaries would cost £15m [source: http://www.fsa.gov.uk/pubs/cp/cp186_vol1.pdf].
[49] http://www.fsa.gov.uk/pages/Doing/Regulated/Notify/Permissions/pdf/fee_blocks.pdf

lead to additional costs being imposed on them. It may be expected that such costs are unlikely to be significant given their compliance with existing FSMA-style supervision in other areas, but it has not been possible to quantify these costs at this stage.

Q6: Do you have any evidence about the likely level of compliance costs associated with supervision of additional consumer credit-related elements?

Costs to lenders not already regulated under FSMA (regime change costs)

90. For those firms who are not already authorised by the FSA, the changes (and hence associated costs) are likely to be more significant. In terms of one-off costs, the most important would be those associated with authorisation and systems overhaul to achieve compliance. Additional one-off costs will be incurred as a result of familiarisation/training of staff. The major sources of ongoing costs will be annual fees to cover CPMA costs, the provision of information to consumers and reporting requirements imposed by the CPMA.

Q7: Are there any other sources of cost that may be incurred by firms that are not already regulated under FSMA?

91. Although it is estimated that there are currently 40,000-70,000 OFT-licensed firms that are not regulated in any way by the FSA, the actual number seeking authorisation from the CPMA could be significantly lower. For example, it is likely that – based on experience over the last couple of years – the overall total of OFT-licensed firms will decline through natural wastage. Based on an extrapolation of recent trends in ‘churn’ of consumer credit firms, OFT estimate that this may be around 8%, which would imply a reduction in those potentially seeking authorisation to 37,000-64,000.

Q8: Do you think the above figures are a reasonable estimate for the number of firms that would potentially seek authorisation from the CPMA?

Q9: How many of these firms do you think might exit the retail financial services market?

92. As stated above, there are no good comparators to use as benchmarks for the likely impact of introducing FSMA-style regulation to those currently licensed by the OFT. Although there are instances of FSA taking over the regulation of certain sectors (e.g. travel insurance, general insurance/mortgage intermediaries, credit unions), these sectors are not that similar to the current OFT-licensed population across a variety of characteristics (e.g. size, distribution, systems, activities undertaken). Trying to estimate what proportion of the above 37,000-64,000 firms may seek some form of authorisation from the CPMA is therefore very difficult, if not impossible. However, we are working with OFT and FSA to improve the evidence base on likely outcomes through analysis of firms currently regulated by OFT who may be regulated by the CPMA.

93. Current FSA fee-raising arrangements provide for the flexibility to ensure that fees are proportionate and reflect variations in the resources employed by the regulator for different firms. Application fees vary according to the complexity of the application – £1,500 for ‘straightforward’ applications; £5,000 for ‘moderately complex’ applications, and £25,000 for ‘complex’ applications.[50]

94. Exceptions to the general approach are also permitted where these can be justified (as is currently the case for smaller credit unions and non-directive friendly societies, which offer support to those with limited financial resources). This is only possible, however, where other regulated firms subsidise these exemptions and following consultation on this basis – for example, much lower authorisation fees are charged to credit unions (between £200 and £1,800) and transitional arrangements have been made for previous regulatory transfers (e.g. a 30% fee discount for travel insurance, 50% discount for additional licence applications by credit unions). It should also be noted that the above fees reflect current business-as-usual costs, which take no account of potential economies of scale resulting from a large migration of firms.

95. Unfortunately, it has not been possible to classify those firms that currently only hold an OFT consumer credit licence into these different categories, as sufficient information about the nature of the business and their licensed activity is not available. A further complication is introduced by the

[50] http://fsahandbook.info/FSA/html/handbook/FEES/3/Annex1

fact that one-off application and annual regulatory fees are relevant for direct authorisation only, so those seeking to be Appointed Representatives do not pay. Similarly, it has not been possible to estimate what proportion of firms might be eligible (and hence might apply) to be Appointed Representatives.

Q10: What proportion of firms do you think might apply for direct authorisation from the CPMA?

Q11: What proportion of firms do you think might apply to be Appointed Representatives under a FSMA-style regime?

96. These difficulties in estimating the proportion of firms in different categories feeds through into quantifying the one-off costs associated with systems changes to achieve compliance. Significant regulatory changes are likely to entail substantial IT implementation costs – for example, PWC estimated that the average cost for implementing the Consumer Credit Act in 2006 was £6m-9m for a large lender.[51] The research also estimated one-off 'business change' costs, which included training and communications. As lenders suggested that such costs would be roughly equivalent to those for IT implementation, these were also estimated to be £6m-9m for a large lender. This would imply a total one-off cost for a large lender of £12m-18m.

Q12: Do you think the above figure is a reasonable estimate of the likely one-off costs for a large lender associated with CPMA authorisation? How do you think this figure might change for smaller firms?

97. As for the authorisation fees above, annual fees imposed by the CPMA are likely to vary considerably across the different types of regulatory activity. Currently, FSA periodic fees are determined by three key factors: the fee block that a firm belongs to; the scale/size of a firm's activities, and the cost of regulating those activities.[52] These periodic fees are allocated differentially across fee-blocks to mitigate cross-subsidy between regulated activities. As HM Treasury guidance states that fees for publicly-provided goods and services must be set at a level to cover costs[53], such fees change in line with the overall funding requirement from year to year. Indeed, changes to FSA funding requirements across fee blocks for 2010/11 range from 44% to -14%.[54]

98. In December 2009, the OFT issued a consultation on revising its consumer credit licensing fees in response to concerns around the current charging structure's ability to reflect the differential costs of regulating different types of activity and the risk-based regulatory approach.[55] In setting fee levels for authorised credit activities, the CPMA would take a proportionate approach and consider the appropriate level for minimum fee requirements for different categories of firm. Such decisions would be subject to many of the same processes currently undertaken by the FSA in setting its fees – i.e. cost-benefit analysis, consultation with the public as well as consumer/small business panels and moderation frameworks (which allow for discounts to existing fees). However, it has not been possible to undertake the detailed analysis (split by business activity) to determine the likely regulatory costs (and hence corresponding fee levels) associated with supervising newly-regulated firms.

99. Currently, the costs of administering the OFT consumer credit licence regime are £9m-10m per year.[56] However, this is not indicative of the potential costs under the CPMA; as the legislative basis for enforcement by the OFT (i.e. CCA) is entirely different, the regulatory framework under a FSMA-style regime and hence the compliance requirements placed on regulated firms are likely to be substantially different.

[51] http://www.berr.gov.uk/files/file38292.pdf (NB: this was a significantly higher figure than the estimate included in the original impact assessment, which was £20m-90m (equivalent to £10,000-£50,000 for a large lender)
[52] For further detail, see http://www.fsa.gov.uk/Pages/Doing/Regulated/Fees/Periodic/
[53] http://www.hm-treasury.gov.uk/d/mpm_whole.pdf
[54] Table 12.1 of http://www.fsa.gov.uk/pubs/policy/ps10_07.pdf
[55] 'Review of consumer credit licensing fees: a consultation', OFT (December 2009)
[56] However, it is difficult to make consistent estimates due to the fluctuations in licence applications and changes to the licence renewal process in 2008 (source: OFT annual reports from 2008-9 and 2009-10, available at: http://www.oft.gov.uk/about-the-oft/annual-plan-and-report/annual-report/)

100. In the event that risk is used to allocate supervisory resources (at least in part), it is likely that a large number of firms that are new to FSMA-style regulation would be 'low impact' and therefore the costs to them would not be as high as those currently incurred by many other firms authorised by the FSA. Nevertheless, other activities (e.g. debt collection, home-collected credit) – whilst posing a low level of financial risk – may pose significant risk of other harm to consumers, including physical and mental harm in extreme cases.[57] Such activities may therefore deserve relatively stringent requirements and close oversight, despite low financial risk.

101. Overall, it is likely that the level of annual fees for firms currently regulated by the OFT will be higher under the CPMA. Currently, the maximum fee for an OFT consumer credit licence is £820 for a 5-year period (£330 for sole traders), while the FSA have recently introduced a minimum annual fee of £1,000 from 2010/11.[58] In addition to the absence of information about the level of costs on a per-firm basis (and how these costs might vary across firms according to their regulated activity), we do not have the necessary information about the number of firms that might be likely to seek authorisation from the CPMA to reach an aggregate view on overall costs of periodic fees.

102. Similarly, it is not possible from the available information to estimate the ongoing costs associated with potential additional disclosure requirements (i.e. provision of information to consumers) and reporting requirements (i.e. provision of information to the CPMA). These will depend on the risk posed by their regulated activity, which is unknown at this stage. Previous analysis commissioned by the FSA estimated the administrative burden associated with FSMA compliance to be around £600m per year across all regulated firms, while provision of information to third parties (e.g. consumers) under FSMA were estimated to total £255m per year across all regulated firms.[59] Unfortunately, it is not possible to break these down to a cost per firm and we do not know which precise requirements newly-regulated firms would be required to meet (or how many firms this may apply to), so we cannot use these as a basis for making estimates in this case.[60]

Benefits

Compliance cost savings to firms and consumers from deregulation/simplification

103. Bringing the regulation of consumer credit under a FSMA-style regime would require the repeal of the Consumer Credit Act and associated regulations, which currently impose substantial compliance costs on business. Based on initial calculations by the Better Regulation Executive[61] and subsequent analysis, it is estimated that current consumer credit regulation imposes a regulatory burden of around £235m per year.[62]

104. However, as previously mentioned, there are some existing burdens under the current regime which would have to be retained under a FSMA-style regime, such as those associated with maximum-harmonisation European Directives. For example, provisional estimates have been made about the burden associated with the Consumer Credit Directive, which is calculated to be £115m per year (though this could be reduced to £80m, depending on the degree to which the CPMA wishes to apply obligations to lending outside the scope of the Directive).[63]

105. Therefore, the best estimate of the quantified net impact of the repeal of existing consumer credit legislation is **£120m per year**. Although this would seem to imply a net reduction in the regulatory burden on firms, there are likely to be additional compliance requirements introduced by the CPMA.

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[57] This is reflected in their current status as 'high risk' activities within the OFT's risk model
[58] http://www.fsa.gov.uk/pubs/policy/ps10_07.pdf
[59] FSA admin burden assessment available at: http://www.fsa.gov.uk/pubs/other/admin_burdens.pdf; third party admin burden assessment available at: http://www.fsa.gov.uk/pubs/other/Admin_Burdens_Report_20060621.pdf
[60] The FSA estimated that mortgage and general insurance intermediaries would incur ongoing costs of £72m-206m per year (including purchase of professional indemnity insurance, maintaining capital adequacy requirements and the cost to new firms of becoming authorised)
[61] https://www.abcalculator.bis.gov.uk/index.php
[62] Total admin burdens associated with consumer credit up to 2005 (as assessed by PWC) were estimated to be £234m per year; this has since been amended by Consumer Credit Act 2006 (estimated admin burden of £38m), the Consumer Credit Act Legislative Reform Order 2008 (estimated admin burden reduction of £13m) and the Consumer Credit Directive (estimated admin burden reduction of £24m), which gives an overall total of £235m
[63] Comprising: Consumer Credit (Advertisement) Regulations [£8m]; Consumer Credit (Disclosure of Information) Regulations [£86m]; early settlement requirements [£9m]; withdrawal/cancellation requirements [£2m]; credit reference agency/database access obligations [£9m], and adequate explanations [£1m] (source: https://www.abcalculator.bis.gov.uk/index.php and subsequent calculations). If it is assumed that around 70% could be attributable to agreements within scope of the Directive (as it would be open to the CPMA not to apply CCD rules), this would lead to a lower bound impact of £80m

However, as outlined above, these additional burdens are not yet quantified, so we cannot say what the net effect of the overall compliance burden placed on firms is likely to be.[64] For example, the individual compliance burden for some firms may increase if they become subject to additional requirements (e.g. through enhanced reporting requirements).

106. The creation of a new rulebook for consumer credit regulation could provide an opportunity to explore how the regime could be made simpler and more transparent, and in particular to consider specific opportunities for deregulation of certain categories of activity.

107. As part of its consultation on its rules, the CPMA would consider whether the regime could be simplified through removing provisions that may result in undue burdens or complexity. This should also be considered in the context of the Government's call for evidence in support of the consumer credit and personal insolvency review, which invited views on issues raised by stakeholders including deregulatory proposals.[65] The flexibility of a rulebook regime would also enable more rapid resolution of any unintended consequences that may arise in the future, or to respond to market developments.

108. Scope for deregulation is constrained by a number of important factors, foremost among which is risk to consumers given the link between certain types of credit provision and significant, infrequently repeated consumer transactions. As such, consideration of exempting certain categories of activity from regulation would only be appropriate where the risk of consumer detriment is low and can be tackled effectively via other means. Further legislative constraints also exist as a result of the requirements of EU law (in particular the CCD), as well as practical challenges of drawing workable legal distinctions in some areas (for example between different forms of 'credit').

109. Nonetheless, the creation of a new FSMA-style regime provides the opportunity to remove some of the constraints to which the current regime is subject and to consider where the CCA regime may currently place unnecessary burdens on firms which are not justified by the risks to consumers, or where it could be rationalised within a CPMA regime to minimise burdens and better align with CPMA objectives.

110. Further analysis is needed to determine – in the light of the constraints mentioned above – the extent to which deregulation would be feasible or desirable, but areas in which scope for this might be considered include:

- Low-risk categories of business where other legislation may address consumer detriment. Careful consideration would of course have to be given to how potential associated risks may be mitigated (e.g. that firms may redesign their business models in order to evade regulation);
- Categories where effective parallel regulation or control via professional standards exists (e.g. consideration might be given to whether Charities Commission rules provide adequate safeguards for the clients of free debt advice provided by charitable organisations), and
- Tightening up definitions of licensable activity so that certain firms are excluded[66].

<u>Cost savings to firms from not having to pay for OFT consumer credit licence</u>

111. Under this option, firms will only have to pay for a single authorisation, which means cost savings for firms who currently pay for an OFT consumer credit licence (of which there are estimated to be 96,000, but not all of these firms may wish to renew their licence). On the basis of current costs associated with an OFT consumer credit licence (£330 for a 5-year period for sole traders, £820 for a 5-year period for others), this would imply a cost saving of £66 per year for sole traders (who

[64] Firms that currently offer services and products that are subject to dual-regulation are particularly likely to benefit from a more harmonised regime but any reduction in burden resulting from simplification are likely to feed through into savings for all consumer credit lenders and brokers. There may be more limited savings to firms engaging in other activities, which are subject to fewer detailed provisions of the CCA

[65] http://www.bis.gov.uk/Consultations/consumer-credit-call-for-evidence

[66] For example, while only a few credit reference agencies provide reports on consumers' creditworthiness to support underwriting decisions by lenders, the current definition creates uncertainty as to whether a much larger group of businesses are caught. There may be a question as to whether the latter group should be regulated, or whether they would be better regulated within a different category of businesses, appropriately reflecting the risks they pose to consumers

constitute around one-third of total licensees) and £164 per year for other types of firm. This would therefore imply a **potential cost saving of up to £11.6m per year**.[67]

<u>Benefits for business and consumers from improved oversight</u>

112. Bringing consumer credit within the remit of the CPMA should have an advantage in addressing cross-sector issues more efficiently and effectively. Improvements in oversight and increased supervisory resource allocated to consumer credit-related firms may potentially help to reduce the incidence of problem debt, which imposes costs on both businesses and consumers. For example, in the first half of 2010, over £5 billion was written off on unsecured lending, while costs to individuals from financial difficulty can arise through health problems, relationship breakdown, lost earnings/reduced productivity due to absence from work and potentially eviction or bankruptcy.

Q13: Are there any other costs that may be avoided by business or consumers as a result of improvements in oversight and increased supervisory resources for consumer credit?

113. In addition, granting the CPMA authority to make rules with the force of secondary legislation (constrained by consultation and impact assessment requirements) would enable a more rapid and flexible response to emerging issues. This could lead to benefits for both consumers and businesses, as detriment and costs resulting from such issues could be dealt with more quickly, reducing the overall costs.

114. Additional enforcement powers available to the CPMA – such as requirements on non-compliant firms to compensate consumers for their losses (which currently apply to other financial products) and stronger sanctions in case of breaches – may also help to increase compliance through a stronger deterrent threat, which may ultimately benefit consumers. This may also extend to dynamic benefits in the future from necessary legislative adjustments – for example, if changes are required to implement EU Directives, these can be made with minimal disruption and cost to business.

<u>Benefits from improved consumer confidence</u>

115. There may also be benefits accruing to consumers from increased confidence in dealing with regulated firms, which may then help to drive competition in the consumer credit and ancillary markets. A parallel can be drawn with credit unions, as the FSA assumed responsibility for their regulation in 2002; since then, although the number of credit unions has almost halved, the number of members has doubled and the value of the assets held across all credit unions has tripled.

Q14: Do you have any evidence which might help to quantify this impact?

<u>Cost savings to CPMA from improved efficiency/economies of scale</u>

116. Finally, there are likely to be opportunities for rationalisation within the CPMA, arising from economies of scale (e.g. moving to a single set of central support services).[68] The NAO report found evidence that certain reorganisations had led to such savings and, in some cases, improved levels of customer satisfaction. There is previous evidence to support this theory as the operating costs of the FSA in the four years after its establishment were less than the sum of the predecessor bodies that had been brought together to create it.[69] There are also potential benefits from a more unified approach to standard-setting, authorisation, supervision and enforcement in relation to retail financial services.

Q15: Do you have any evidence which might help to quantify this impact?

[67] Based on the total number of firms declining by 8% and all sole traders (one-third of 89,000; paying £66 per year, totalling £1.95m) and non-sole traders (two-thirds of 89,000; paying £164 per year, totalling £9.7m) renewing their licence

[68] Further details can be found in Briault, 'Revisiting the rationale for a single national financial services regulator' (February 2002)

[69] Briault, 'Revisiting the rationale for a single national financial services regulator' (February 2002)

Cost savings for related bodies

117. There may also be benefits to related bodies – such as the Financial Ombudsman Service and Consumer Financial Education Body – through administrative savings from only dealing with a single sponsor body, though these are difficult to quantify.

Q16: Do you have any evidence which might help to quantify this impact?

Risks and assumptions

118. As set out above, it has been assumed that around 8% of firms currently licensed by the OFT will choose not to renew their licence due to external circumstances independent of the potential changes analysed here. Depending on how changes in these external circumstances (e.g. macroeconomic conditions) have affected different firms, this assumption may prove to be a substantial under- or overestimate.

Q17: Do you agree with this assumption? Do you have any further evidence which might help to refine this estimate?

119. A potential risk is market exit – i.e. firms choosing to cease their current licensed activity due to increases in compliance burdens. If a significant number for firms choose to exit the market, this may result in a substantial reduction in competition (see competition impact test below), with potentially adverse effects on consumer choice, innovation and incidence of illegal trading (see wider impact section below).

Q18: Do you consider the above risk – of increased unlicensed activity as a result of market exit – to be significant?

120. In addition, a further risk is that firms may pass on increased costs to consumers in the form of higher prices. If these consumers are low-income or vulnerable, they may be least able to afford any increase in price. Further evidence is required to fully assess the impact of this option on SMEs (both consumer credit firms and businesses that access working capital from unsecured lenders[70]) and consider ways in which costs to SMEs could be minimised.

Q19: Do you have any evidence which might help to assess the degree of pass-through?

121. Although we do not know the relative proportion of firms who may seek different forms of authorisation, this is in any case likely to change over time. For example, evidence from the FSA shows that, since 2006, the number of directly-authorised insurance intermediaries has fallen by over 35%, while the number of Appointed Representatives has increased by over 45%.

122. As set out above, the option of becoming an Appointed Representative will not be available to all consumer credit licensees, as it depends on the type of regulated activity undertaken and requires an authorised person (the Principal) to accept responsibility for compliance with the CPMA rules by the AR. This may ultimately lead to market developments and/or the emergence of mutually beneficial networks of organisations to achieve economies of scale in authorisation, as well as supervision and compliance.

Q20: Do you have any evidence to help assess this impact?

123. This option would entail supervision by the CPMA across a different spectrum of products and services than that currently overseen by the FSA. A potential risk is that the necessary expertise within the CPMA is not developed sufficiently to make appropriate and timely interventions in the consumer credit market. There is also concern on the part of some stakeholders that moving from prescriptive legislation (under the CCA) towards a more flexible outcomes-focused system increases scope for interpretation, which may require firms to engage greater legal expertise and hence increase costs. The extent of these costs would depend on the scope for interpretation provided in

[70] Unsecured loans worth less than £25,000 are regulated by the CCA, regardless of whether the borrower is an individual consumer or a business

the FSMA-style rulebook for consumer credit when it is developed, but it is not possible to estimate such costs at this stage.

Q21: Do you have any evidence on the comparative experience between compliance under CCA and FSMA?

124. Lastly, there will also be transitional arrangements to consider in the event of any decision to transfer responsibility for consumer credit regulation to the CPMA; the NAO noted in its report that it can take two or more years to complete a significant reorganisation. The consultation document includes some of the key considerations, including what should happen in respect of credit agreements already entered into and how fee structures should be handled.

Summary

125. Under this option, consumer credit – incorporating both lenders and ancillary service providers (e.g. debt collection, credit reference services) – would be regulated under a FSMA-style regime by the CPMA. This would give the CPMA the ability to supervise the sector more flexibly than is currently possible under the CCA, with rule-making powers that should help to deal with issues in a more timely and efficient manner. In addition, any uncertainty resulting from the current regulatory overlap between FSMA and CCA would be eliminated.

126. Assessing this option against the four objectives set out earlier:

- **Clarity, coherence and improved market oversight**: The Government believes that bringing together all retail financial services under one regulatory regime will bring a number of key benefits, including: removing the inconsistency in the regulatory treatment of retail financial services and eliminating a layer of complexity that can cause confusion; delivering greater clarity and coherence for consumers and businesses, as they will be assured of a single point of contact in their regulatory queries or concerns; simplifying compliance and removing unnecessary duplications, administrative complexity and burdens for firms currently regulated under both the CCA and FSMA; improving market oversight, and strengthening the CPMA's role as part of the wider regulatory architecture.

- **Effective and appropriate consumer protection, including through a responsive and flexible framework**: A key cornerstone of any transfer of responsibility for consumer credit would be to at least maintain – and where possible strengthen – overall levels of consumer protection, while recognising the role of consumer responsibility and that all risk will not be eliminated. The Government recognises that the current CCA regime provides for a number of important consumer protections that are valued by many stakeholders. The Government expects that the CPMA will build on the work already undertaken by the FSA as part of its new consumer protection strategy, and anticipates that in its role as a focused conduct regulator it will be even more proactive and effective in identifying and tackling the causes of consumer detriment.

- **Simplification and deregulation**: Opportunities for simplifying and deregulating the consumer credit regime (subject to the constraints of EU law) exist, whether consumer credit regulation is transferred to a FSMA-style regime or not. However, the Government believes that the opportunities for simplification and deregulation are clearer and more comprehensive under a FSMA-style regime, as the process of designing a new rulebook would involve a full review of existing consumer credit regulation.

- **Proportionate and cost-effective**: While a rulebook approach would confer a number of advantages, firms regulated under FSMA are subject to different requirements from those that exist under the CCA, and a transfer of consumer credit to the CPMA may therefore result in new obligations for firms in some areas. The precise content of a credit rulebook would be subject to detailed consultation. There is no doubt that application of FSMA-style requirements to consumer credit firms could lead to important consumer protection and market oversight benefits. However, the Government recognises that it will be essential to design a regime that ensures that costs to regulated firms are proportionate, fair and recognise the risks posed by particular elements of the consumer credit market.

127. There are likely to be a range of costs associated with this option, both one-off (e.g. familiarisation costs; one-off compliance costs; reorganisation costs) and ongoing (e.g. increased costs of CPMA authorisation, monitoring and enforcement, paid through CPMA fees; costs of prudential requirements). Almost all of these costs will be borne by firms, either directly (e.g.

through staff training for new rules or completing regulatory returns) or indirectly (i.e. costs recovered through higher regulatory fees). However, due to a lack of information about the existing OFT-licensed population and uncertainty about the level of CPMA regulatory oversight (and hence associated costs of regulatory resource) required, most of these costs remain unquantified at this stage. The costs that have been quantified are one-off transition costs for extending CPMA responsibilities (up to £5m) and one-off costs to firms already regulated by both FSA and OFT from application for variation of permission (£12m-15m).

128. Under this option, there are also a range of potential benefits, such as: compliance cost savings to firms from the repeal of the Consumer Credit Act; cost savings from not paying for an OFT consumer credit licence; administrative cost savings to CPMA and related bodies due to efficiency improvements/economies of scale, as well as the avoidance of costs incurred by business and consumers from improved oversight. Again, most of these are unquantified, though the compliance burden associated with consumer credit regulations is substantial, at £235m per year. Some of these will have to be reflected in a FSMA-style rulebook, such as burdens associated with the Consumer Credit Directive (estimated to total £115m per year), giving a net reduction of £120m per year.

Wider impacts

129. As stated above, a potential reduction in the number of firms could lead to a decrease in choice of available credit services and products, which may adversely impact on consumers. This may reduce the borrowing options for such consumers, who may be most in need of credit to meet everyday expenses and may therefore seek credit from other sources, such as unlicensed lenders. One-off costs associated with authorisation and ongoing compliance costs may potentially prove particularly burdensome for smaller firms and non-lenders, who may be more likely to serve customers towards the high-risk end of the credit spectrum. This could also impact negatively on consumers through an increase in unlicensed trading, particularly through online channels.

Annexes

Annex 1 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

Basis of the review: [The basis of the review could be statutory (forming part of the legislation), it could be to review existing policy or there could be a political commitment to review]

This impact assessment includes a commitment to review within 5 years of implementation (which is expected to occur in 2014) – i.e. a review to be undertaken by 2019. If the decision is taken to make any changes to the regulatory framework, this will require primary legislation, which will include a commitment to review arrangements in due course.

Review objective: [Is it intended as a proportionate check that regulation is operating as expected to tackle the problem of concern?; or as a wider exploration of the policy approach taken?; or as a link from policy objective to outcome?]

The primary objective of the review would be to assess whether changes to the regulatory framework for consumer credit have been successful in addressing the concerns set out earlier – i.e. confusion/uncertainty resulting from overlaps in regulation of consumer credit/related services and an insufficiently flexible/responsive regulatory regime for consumer credit.

If such action was successful, we would expect to see a consumer credit regime that responded quickly to emerging threats and risks to consumer protection. This is likely to result in a more stable and resilient credit market, with firms that are less prone to failure, which could then lead to improvements in consumer confidence and consequent positive impacts on competition. A further potential outcome is an improvement in the overall quality of lending – which could reduce the level of write-offs for unsecured lending (over £5bn in the first half of 2010) – as well as better treatment of consumers in financial difficulty, which could reduce the incidence of over-borrowing (with its associated adverse economic and social consequences).

In addition, the review could address costs and benefits associated with the proposed reform of the regulatory structure for consumer credit regulation. This could act to verify the level of transition and ongoing costs of compliance for firms and the extent to which potential economies of scale/scope had been realised within any new body.

Review approach and rationale: [e.g. describe here the review approach (in-depth evaluation, scope review of monitoring data, scan of stakeholder views, etc.) and the rationale that made choosing such an approach]

The review would evaluate the effectiveness of any potential changes to the regulatory architecture for consumer credit that might be taken forward in light of this consultation. Such an evaluation would incorporate the views of stakeholders – businesses, lenders and consumers – as well as making use of monitoring data on any emerging problems in the consumer credit market (see below).

Baseline: [The current (baseline) position against which the change introduced by the legislation can be measured]

Information about the current situation regarding consumer credit-related regulation can be obtained from OFT management information – for example, action taken by the OFT to correct poor behaviour by licensed lenders – and complaint data relating to consumer credit, either from the Financial Ombudsman Service or consumer bodies (e.g. Citizens Advice). Care must be taken in interpreting this data, however, as complaints may not always be a good indicator of consumer satisfaction – for example, this may simply reflect increased awareness of rights and/or an increase in the ability or opportunity of consumers to exercise them.

Aggregate data on lending and write-offs is available from Bank of England and Office for National Statistics, while household survey data should give an indication of the extent to which problems resulting from current regulatory arrangements persist and create problems for consumers.

Success criteria: [Criteria showing achievement of the policy objectives as set out in the final impact assessment; criteria for modifying or replacing the policy if it does not achieve its objectives]

Given the quantity of recent changes in the area of consumer credit regulation, it will be very difficult to isolate and then assess solely the impact of the changes proposed here. In addition, changes due to the prevailing economic climate at the time of the review may have a strong influence over some factors that may be used to measure ‘success’.

In relation to the objectives set out earlier, feedback from regulated firms should determine whether any new regime results in improvements to accountability and consistency. Similarly, feedback from business and consumer groups should help to assess whether reforms have strengthened consumer protection and market oversight. Feedback from both sides of the market should also help to evaluate whether any new regime has resulted in a more flexible and responsive regulatory framework.

Any potential future modifications to the policy would be informed by regular contact with the responsible bodies, in combination with the feedback outlined above.

Monitoring information arrangements: [Provide further details of the planned/existing arrangements in place that will allow a systematic collection systematic collection of monitoring information for future policy review]

Information for the review will be collected through the everyday workings of the regulator. Feedback from businesses, lenders and consumer groups will be achieved through regular engagement, in addition to a more formal consultation process (e.g. workshops, working groups).

Reasons for not planning a PIR: [If there is no plan to do a PIR please provide reasons here]

N/A

Annex 2: Specific Impact Tests

Competition Test

Moving the regulation and enforcement of consumer credit to a FSMA-style regime may have a significant effect on competition. An increase in operating costs – either as a result of increased authorisation fees or systems/training costs associated with compliance and/or reporting requirements that may be imposed by the CPMA – may indirectly limit both the number and range of suppliers. This could potentially affect the range of credit and credit-related services offered by both lenders and non-lenders.

It is difficult to anticipate how different types of firms might be most affected, but OFT analysis suggests that certain sectors are more likely to be regulated in some way by FSA already than others, as set out in the table below. For example, it is estimated that the proportion of OFT-licensed firms that are also FSA-regulated in the category of 'professional & financial services' is quite high, while the proportion of OFT-licensed firms that are FSA-regulated in the category of 'household goods & services' is quite low.

Table: FSA coverage of OFT licence-holders

Sector	Total Sector size	Number of OFT licence holders also regulated by FSA[71]	
		Lower Bound	Upper Bound
Housing	9,500	0	1,500
Household goods & services	2,500	0	500
Personal goods & services	6,500	0	1,500
Professional & financial services	56,500	21,000	42,000
Transport	14,500	2,000	5,500
Recreational goods & services	6,500	0	1,000
Total	**96,000**	**23,000**	**52,000**

Source: BIS estimates based on OFT data[72].

It is not possible to break these figures down by size of business, but if there is a high fixed component of the costs associated with regulation under a FSMA-style regime, then these could fall more disproportionately on smaller firms. As such firms may be more likely to serve sub-prime customers (given the size and nature of this niche market segment), if the burden of these costs leads to market exit this would reduce the range of credit and credit-related products available to these customers. A particular risk associated with this potential outcome is that, if credit supply to these individuals is reduced, they may be more likely to borrow from illegal lenders, which could have significant adverse social and financial consequences. As set out above, this is difficult to quantify at this stage, as the level of fees under this option would be set by the CPMA. However, it is likely that this risk would be significantly mitigated by the processes involved with the setting of fees (analogous to those undertaken by FSA currently) – i.e. consultation, cost-benefit analysis as well as input from consumer and small business panels.

An additional potential impact on competition will depend on the extent to which any increases in costs are passed on to consumers, which may indirectly limit the ability of firms to compete on price. Finally, another indirect impact that may result from potential increases in the burden of compliance requirements and authorisation fees is the potential for hindering entry by future lenders or providers of ancillary credit and/or debt services.

In contrast to these, a potential positive effect on competition may result from possible increases in compliance requirements, by raising the overall quality of lending and related services (in terms of transparency and certainty). This may, in turn, lead to increased consumer confidence in making decisions about credit use, which could increase the effectiveness of competition with attendant benefits on lowering prices and incentivising innovation. For example, since the FSA took over the regulation of credit unions in 2002, even though the number of credit unions has decreased (from about 700 in 2002

[71] This includes AR s and firms that are directly authorised
[72] These are provisional estimates

to around 400-450 today), the number of members has doubled and the value of assets held by credit unions has tripled over the same period.

Q22: Do you have any evidence to help inform the competition assessment?

Small Firms Impact Test

There is considerable variation in the size of firms across the respective populations regulated by both the OFT and FSA. For example, it is estimated that one-third of current OFT licence holders are sole traders, while previous analysis by the FSA states that around 95% of the firms they regulate are small firms.[73] However, we do not have detailed data on the distribution of these regulated populations by size of firm, so this analysis will necessarily be subject to imprecision.

This proposal should not impose any additional requirements that might impact disproportionately on small firms already regulated by the FSA. Most of the potential impacts will be on those firms that are not already regulated by the FSA (i.e. OFT licence holders only) that seek authorisation from the CPMA. Although we do not have detailed information on the distribution of these firms (i.e. the OFT-licensed population) by size, we do know roughly what proportion of firms are sole traders by licence category. For example, estimates suggest that over half of firms holding licences for debt counselling are sole traders, while only one-fifth of those with licences for 'consumer hire' are sole traders.

Of critical importance to determining the impact on small firms is the extent of fee differentiation by firm size. However, as the FSA operates a risk-based approach to allocating supervisory resources (which will determine the variation in fees and compliance/reporting requirements), it cannot necessarily be assumed that smaller firms will be subject to a lower burden of compliance and/or authorisation fees. In extreme cases, if such increases are particularly significant, this may ultimately lead to market exit.

A priori, it is difficult to assess whether compliance under a FSMA-style regime would be more or less burdensome than under the current CCA-style regime. On the one hand, the current system is based on a set of relatively prescriptive regulations, about which it may be difficult to stay informed. However, a FSMA-style regime based on a broader set of outcome-focused rules could potentially be more subject to interpretation, which may mean that smaller firms need to spend more time and resource on legal expertise to ensure that they are compliant. The FSA has previously argued that an outcomes-based approach to regulation can be easier to comply with for smaller firms, given the frequent engagement of management directly with customers.

As a very significant proportion of firms currently regulated by the FSA are small firms, that would suggest no disincentive for firms to become regulated under a FSMA-style regime just because of their size. Furthermore, since 2007 the FSA has introduced measures to increase its contact with small firms, such as targeted information and resources for small firms, payment by instalments, e-learning packages, dedicated web pages for small firms[74] and improvements to the Firm Contact Centre. In addition, the FSA has established a Smaller Businesses Practitioner Panel (SBPP)[75], which it has made a commitment to consult in the same way as its two other (statutory) panels – the Financial Services Practitioner Panel (FSPP[76]) and the Financial Services Consumer Panel[77].

Q23: Do you have any evidence to help inform the assessment of effects on small firms?

Equality Impact Test

We do not have detailed data on all aspects of credit use by protected groups. However, survey data suggests that credit use does vary by age, with younger households making greater use of credit than older households.[78] Changing the regulatory regime should have an overall positive effect for credit users – in terms of consumer protections and increased confidence in making purchases involving credit – which may therefore be disproportionately beneficial to younger groups.

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[73] For example, the FSA-regulated population includes credit unions, of whom it was estimated (in 1999) that more than half had fewer than 200 members and/or assets below £50,000
[74] http://www.fsa.gov.uk/smallfirms/index.shmtl
[75] http://www.sbpp.org.uk
[76] http://www.fs-pp.org.uk
[77] http://www.fs-cp.org.uk
[78] 'Over-indebtedness in Britain: Second follow-up report', BIS (March 2010)

Although low-income households do not constitute a "protected characteristic", it may give some insight to the prevalence of characteristics associated with low income. For example, evidence suggests that disabled adults are twice as likely to live in low-income households as non-disabled adults.[79] However, analysis of survey data suggests that credit use does not vary significantly by income, but the type of credit used does change – those at lower incomes are more likely to make use of 'non-mainstream' loans (e.g. home credit, payday loans), the supply of which could potentially be adversely affected by high compliance burdens imposed by the CPMA. However, this is likely to be counterbalanced by potential improvements in consumer protection for credit users under a new regulatory regime, which could lead to beneficial effects on some protected groups.

However, in relation to many other protected groups (e.g. gender reassignment, pregnancy and maternity, race, religion and belief, sexual orientation), we do not have the necessary data to make a preliminary assessment of the likely impact of the proposed policy. Nevertheless, we do not expect such impacts to have a disproportionate impact on these protected groups.

If the option of transferring consumer credit to a FSMA-style framework is taken forward, a further consultation on detailed rules for consumer credit would be conducted by the CPMA. This consultation will take into account representations on the potential impacts of policies and practices, which will include the need to consider implications for equality and diversity.

Q24: Do you have any evidence to help inform the assessment of effects on equality and protected groups?

[79] http://www.poverty.org.uk/40/index.shtml

Annex 3: OFT-licensed and FSA-authorised populations

Office of Fair Trading consumer credit licences

The process for issuing consumer credit licences by the OFT changed in 2008. Prior to 2008, businesses would apply for a single consumer credit licence to cover all categories of business. However, since 2008 businesses are required to apply for specific categories of licence covering each type of business they are involved in. Therefore, many firms are licensed for multiple categories, of which there are 9 high-level classifications.

Category A – Consumer credit business

Category A comprises firms that offer consumer credit lending, including:

- 'Mainstream' lending (e.g. bank accounts, credit cards, overdrafts, personal loans);
- Credit unions
- Pawnbrokers
- Logbook lending
- Home credit providers
- Retailers and service providers who make their goods and services available on credit, covering a wide range of activities (e.g. gyms, veterinarians, shops, builders)
- Insurance providers
- Payday loan companies
- Store card providers
- Debt purchasing organisations
- Hire purchase companies
- Cheque cashing companies
- Share dealing companies

Category B – Consumer hire business

Category B comprises firms that offer consumer hire services, which include:

- Consumer hire businesses
- Car hire
- Tool hire
- Employers –e.g. where they offer bike-to-work or home computing schemes

Category C – Credit brokerage

Category C comprises firms that offer credit brokerage services, but is not limited to specialist brokers of credit. It covers all who act as intermediaries – such as retailers and service providers which offer credit to the customer to finance the primary purchase. Brokerage is by far the largest category applied for and a considerable majority of such firms will hold another category of licence. Typical businesses in this category include:

- Retail finance (advice & referral)
- Doorstep/in-the-home retail
- Independent Financial Advisers
- Loan finders
- Mortgage brokers
- Debt advisers (commercial and non-commercial)
- Introducers
- Solicitors
- Price comparison websites
- Accountants

Category D/Category E – Debt adjusting/Debt counselling

Categories D and E comprise firms that offer debt adjustment and/or debt counselling services, including:

- Debt management companies
- Commercial debt advice
- Free-to-client advice
- Consumer Direct
- Claims management companies
- Solicitors
- Accountants
- Car dealerships
- Independent Financial Advisers
- Lead generators
- Insolvency Practitioners

Category F – Debt collecting

Category F comprises firms that offer debt collecting services, including:
- Debt collection agencies
- Bailiffs
- Vehicle repossession services
- Solicitors
- Accountants

Category G – Debt administration

Category G comprises firms that offer debt administration services, including:
- Loan administrators
- Securitisers
- Lenders

Category H – Credit information services

Category H comprises firms that offer credit information services, including:
- Debt advisors
- Debt counsellors
- Credit repair companies

Category I – Credit reference services

Category I comprises firms that offer credit reference services, including:
- Credit reference agencies
- Group data sharers

It is not known precisely what proportion of the licensed population is actively trading. As the requirement to renew and/or pay the maintenance fee only applies once every five years under new arrangements, it is highly likely that a certain proportion of current licence holders will have ceased trading.

FSA-authorised population

There are currently around 27,000 directly-authorised firms (details shown in the table below), while latest data indicates that there are approximately 35,000 Appointed Representatives, of which around two-thirds are Appointed Representatives and one-third are ‘Introducer’ Appointed Representatives.

Table: FSA-directly authorised population (2009)

Sector	Total firms
Advising, arranging & dealing as agent	15,200
Custodians	200
Deposit takers	800
Insurance firms	1,000
Investment managers	2,000
Mortgage lenders	100
Principal position takers	100
Professional entities	400
Trading, clearing and settlement systems	50
None specified	6,800
TOTAL	**26,800**

Source: FSA

Annex 4: The current regulatory regime for consumer credit

Consumer credit regulation is an area of considerable complexity and is estimated to impose a regulatory burden on business and consumers of approximately £235 million a year.

The OFT is the licensing authority and main enforcement body for regulated consumer credit (including personal loans, credit card lending and the provision of goods and services on credit as well as related activities such as debt collection and debt management) under the Consumer Credit Act (CCA) 1974, substantially amended both in 2006 and earlier this year by the implementation of the Consumer Credit Directive (CCD). The CCA is a broad Act governing most forms of consumer credit, consumer hire and debt related activity, and is supplemented by a range of subordinate legislation. Its objective is to protect consumers through the control of traders involved in credit and their transactions. It provides for core consumer protections, extended by the CCD (detailed below).

The wide scope of the CCA means that many licensees are not financial services businesses themselves, but provide access to credit, allow payment in instalments for goods and services, or provide ancillary services such as debt advice or credit reference information. The licensed population therefore includes high street retailers, car dealers and suppliers of general goods and services.

Oversight of the CCA forms part of the OFT's broader mission to make markets work well for consumers by promoting and protecting consumer interests throughout the UK and ensuring that markets are fair and competitive. Certain other pieces of related legislation also form part of the consumer credit regime, including the Bills of Sale legislation (England and Wales only) and Part 8 of the Enterprise Act 2002. In addition to consumer credit regulation, the OFT also discharges its functions under other legislation covering competition policy and general consumer protection legislation, including the Unfair Terms in Consumer Contracts Regulations 1999 (UTCCRs) and the Consumer Protection from Unfair Trading Regulations 2008 (CPRs).

The OFT shares responsibility for enforcement of the CCA regime with local authority Trading Standards Services and the Department of Enterprise, Trade and Investment in Northern Ireland (DETINI), which have powers to prosecute certain offences under the CCA and general consumer law such as the CPRs. Trading Standards Services also undertake a wider role, monitoring compliance and providing intelligence and evidence to the OFT on consumer credit firms operating in their locality, investigating consumer complaints, and providing advice to businesses offering credit and debt services to consumers. Trading Standards Services collaborate on a regional basis in the delivery of the specialist Illegal Money Lending enforcement teams in England, Scotland and Wales.

Self-regulation is also a part of the regulatory regime for consumer credit, and in many instances can provide a preferable alternative to regulation. The self-regulatory Lending Code applies to banks, credit card companies and building societies in their dealings with consumers, micro-enterprises and charities with an annual income of less than £1 million. The code sets minimum standards of good practice in relation to loans, credit cards, charge cards and current account overdrafts. Compliance is monitored and enforced independently by the Lending Standards Board, funded by industry subscribers. A revised code is expected to be launched at the end of March 2011. As announced by the British Banking Association (BBA) Taskforce report Supporting UK Business, the new code will include the commitments made by the BBA in June 2010 to cover small businesses or micro-enterprises. Other parts of the consumer credit industry are also covered by codes, such as the Finance and Leasing Association Lending Code and the Debt Managers Standards Association Code. These are typically overseen by the relevant trade associations themselves rather than an independent body.

Of the approximately 96,000 firms regulated by the OFT, an estimated 16,000 are also authorised by the FSA for financial services activities regulated under FSMA. The current FSMA framework, which the Government has announced will form the basis of the CPMA's powers and functions, includes a number of elements that represent a different approach to the CCA regime, as highlighted below.

Core consumer protections enshrined under the Consumer Credit Act

The following is an indicative list of the key consumer protection provisions in the Consumer Credit Act (CCA):

Advertising/canvassing

- Controls on credit advertising (CCA sections 43-47)
- Ban on canvassing off trade premises (s48-49)

- Controls on credit brokers and credit intermediaries (s55 and 160A)

Pre-contract

- Requirements on pre-contractual information (s55)
- Duty to give adequate explanations (s55A)
- Duty to assess creditworthiness (s55B)
- Right to request details of credit reference agency used to access consumer’s credit file (s157-159)
- Key information about credit arrangements must be made available to consumers before the agreement is concluded or immediately afterwards (Part 5)

Contract

- Form and content of credit agreements and provision of copy documents (s60-65)

Withdrawal

- Cooling off, withdrawal and right to cancel (s66A, 67 and 68)

Early payment/settlement and termination

- Right to full or partial early repayment on a fixed sum credit agreement (s94-95A)
- Right to terminate hire-purchase or conditional sale agreement (s99-100)
- Right to terminate open-end agreements, i.e. those with no fixed duration (s98A)

Post-contractual disclosure

- Right to request a copy of the credit agreement and specific related information (s77-79)
- Right to request a statement of account in the form of an amortisation table (s77B)
- Provision of annual and periodic statements and arrears notices (s77A, 78, 86B and 86C)
- Notification of interest rate changes (s78A)

Default /enforcement

- Provision of default notices and default sum notices (s86E, 87 and 88)
- Controls regarding enforcement of a debt or repossession of goods or land (s76, 90 and 98)
- Right to apply for a time order from the courts, which if successful, will provide consumers with more time to repay a loan (s129)

Linked credit agreements

- Liability of creditors for consumer claims against suppliers (s75 and 75A)

Unfair relationships/redress

- Unfair relationship test (s140A to 140D)
- Right to redress through Financial Ombudsman Service

Key features of the CCA and FSMA regimes

Licensing under CCA regime	Authorisation under FSMA regime
• Applications for an OFT licence require information about applicant including criminal offences, director disqualification and financial integrity. • High risk activities: Applicants are asked to	• Applications for FSA authorisation usually need to be accompanied by supporting material such as business plan, compliance procedures and balance sheet/ cash flow forecasts.

provide additional information which demonstrates their competence to undertake high-risk activities; some high risk applicants also face an inspection visit. • Assessing fitness: Applicants are assessed against a test of "fitness". The concept of fitness is broadly defined; alongside assessment of integrity and competence issues, OFT can take account of evidence of unfair or improper business practices. • Group licences: The OFT may grant group licences to cover the credit activities of members of professional and other bodies rather than requiring individual firms to apply for a standard licence.	• Threshold conditions: These are minimum conditions that FSMA-authorised firms must satisfy and continue to satisfy in order to carry on a regulated activity. • Approved persons: Individuals who perform a role of particular regulatory significance must comply with standards covering "fitness and propriety". • Appointed Representatives (AR) & Professional Bodies: An AR can carry on certain regulated activities without being authorised if entering into a contract with an authorised firm (known as the Principal) which accepts responsibility for regulated activities carried out by its AR(s). Members of the professions may carry on certain regulated activities under supervision and regulation of their professional body, with FSA maintaining oversight.
CCA regime fitness standards and supervision	**FSMA regime requirements and supervision**
• Fitness and detailed legislative requirements: OFT issues guidance on fitness, making clear the types of behaviour that may trigger regulatory action. Detailed requirements are set out in the CCA and its secondary legislation. Compliance with these forms the basis of assessing the ongoing fitness of licensees. • Supervision of high risk sectors: Sectoral approach focusing where intelligence suggests inappropriate business practices or actual/ potential consumer harm. OFT also conducts regular compliance reviews on a sectoral basis. • Information powers: Licensees required to notify OFT of changes in key information underpinning their licence application. OFT also has range of information-gathering powers which may be exercised throughout the period of a licence.	• Principles for businesses: These are high-level rules that set out the fundamental obligations of all authorised firms (e.g. conducting business with integrity and due skill, care and diligence; and treating customers fairly). • Specific conduct of business and prudential rules: Most authorised firms must meet a general solvency requirement and minimum capital requirements and/or hold Professional Indemnity Insurance cover. FSA's conduct of business rules generally focus on product lifecycle and are consumer outcomes focused. • Systems and Controls requirements: Authorised firms must put in place systems and controls necessary to support the firm's activities and comply with relevant rules; and organise and control their affairs responsibly and effectively. • Regular reporting: Authorised firms are generally required to submit reporting returns on a regular basis. The level of detail and frequency depend on factors including the type of regulated activity.
Enforcement under CCA regime	**Enforcement under FSMA regime**
• Licensing sanctions: OFT has wide powers to take action against traders, e.g. to refuse/revoke licence; impose tailored conduct requirements; and impose civil penalties of up to £50,000 per breach of requirements. • Criminal offences: CCA provides for a number of criminal offences but criminal	• Enforcement provisions: Broader range of specific sanctions than the CCA regime, including potentially higher fines on firms/individuals; prohibiting individuals from working in financial services or carrying on particular activities; public censure of firms/individuals. Carrying on regulated activities without authorisation is

prosecutions are relatively rare. OFT and Trading Standards Services can also use wider consumer enforcement powers such as CPRs. • Unenforceability: Certain breaches of the CCA by creditors, including unlicensed trading, may mean the credit agreement is unenforceable unless a court or the OFT orders otherwise.	a criminal offence. However, breach of a rule does not constitute a criminal offence, nor does it make a transaction void or unenforceable.