CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: **1st Stop Group, Blackpool**

RESPONSE to

A new approach to financial regulation:

consultation on reforming the consumer credit regime

respond to:

financial.reform@hmtreasury.gsi.gov.uk

or

Financial Regulation Strategy
HM Treasury
1 Horse Guards Parade

London
SW1A 2HQ **16 March 2011**

Consultation response from *1st Stop Group* on "a new approach to financial regulation: consultation on reforming the consumer credit regime".

1st Stop Group is pleased to submit a response to the recent consultation on "a new approach to financial regulation: consultation on reforming the consumer credit regime." We understand and are concerned that the Governments preferred option is Option 1 which is based on the Financial Services & Markets Act [FSMA] 2000, that could see all companies involved in the credit industry, large and small, operating under FSA styled 'rule' based regulation. Consumer credit has undergone root and branch changes over the last 35 years culminating in the latest piece of regulation, the Consumer Credit Directive implemented in February of this year. We believe that the current regulator of consumer credit, the Office of Fair Trading [OFT] has been provided with the appropriate tools of regulation and enforcement which means that they have more than adequate means of controlling the market, in a proportionate and appropriate way whilst taking action against any 'rogue traders' within the market. The consultation paper proposes the transfer of the OFT to operate under the Financial Conduct Authority, alongside the FSA. We fail to see why a successful model for regulating consumer credit is potentially once again facing further major change thereby creating concerns for the Industry and consumer alike.

The consultation paper goes much further than the transfer, as it proposes to apply to the consumer credit market the FSA's current approach in the retail deposit market. Without a more proportionate approach this is unlikely to work, because of the fundamental difference between credit [where the risk lies with the lender] and banking/saving [where the main risk lies with the depositor]. Needless to say, compliance costs will increase significantly, and supervision will intervene far more under the new regulator.

We do not feel that the consultation document, or the impact assessment, presents any compelling evidence to move to a FSMA style regime for businesses currently wholly regulated by the OFT, especially those that are considered to be SMEs. We feel that many unintended consequences could arise as a result of the change. Increased costs and regulation could force some smaller organisations, or sole traders to exit the market.

The provision of consumer credit has risen considerably in recent decades and enabled consumers to access products and services to suit their lifestyles. As a direct result of the negative impact of 'credit crunch', bank funding to the SME sector in particular has been severely curtailed, resulting in a significant downturn in lending. Consumer credit has hugely contributed to the positive growth of the UK economy over the last twenty years, within a highly competitive and innovative market. The cessation of many credit products is currently stifling growth, and further regulation, or even uncertainty about regulation going forward will stifle much needed growth even more.

Used wisely, consumer credit also helps consumers to smooth the peaks and troughs in income and expenditure, and allows consumers to manage their finances in a way that suits them.

Our business falls into the “small to medium sized enterprise“ [SME] category
We are an independent lender based in the Northwest lending apx 3m per annum within a niche lending market

Statistics published by Business Innovation & Skills [BIS] in October 2010 (http://.stats.bis.gov.uk) show that the SMEs together accounted for 99.9% of all enterprises, 59.8% of private sector employment and 49.0% of private sector turnover. Both the number of companies and the number of sole proprietorships rose, the former for the 11th successive year, the latter for the seventh successive year. Small enterprises alone, with 1 to 49 employees, accounted for 48.2% of employment and 37.5% of turnover. Addressing the consumer credit SMEs, paragraph 3.1 of the consultation paper suggests that just over one-third of OFT licensed firms are sole traders.

The proposed new regime will be the most radical change in consumer credit regulation for a generation. We believe that the massive changes that consumer credit has gone through in 1974, 2006 and recently with the implementation of the Consumer Credit Directive should not be changed again to fit FSMA 2000. Moreover, we believe that it would create havoc in the consumer credit market, to effect a change from regulation which provides for clear legal certainty to a, principles and rules based approach such as the FSA.

The standards expected by firms in the framework of the UK regulatory regime for consumer credit are some of the highest in Europe and the burden on SMEs in ensuring compliance is a large one. Banks, building societies and large finance houses have larger staffing levels and financial resources to cope with more onerous regulation for deposit takers where the risks are greater. For the SMEs simply keeping up with the required changes is expensive, as detailed regulations can be supplanted by guidance notes and additional actions are required when dealing with other Government agencies.

The changes currently outlined within the consultation paper, would be the most complicated and costly change for all parties. Large numbers of small businesses could be expected to leave the market [over 33% of current credit licensees are sole traders]. Many other lenders would in all probability withdraw from at least part of their current markets. In consequence, the UK’s consumer credit markets would shrink considerably, credit availability would be restricted, and market competition significantly reduced. There would be an increase in the costs of borrowing as companies would have to pass on the higher cost of regulation under the new regime. The effects would almost certainly exceed those of the recent credit crunch, where availability and choice of products reduced dramatically. The low-income borrowers in particular would be most affected, with the real danger of financial exclusion becoming far greater.

As you are no doubt aware around 40% of all consumer lending is currently done by companies which are not banks. Within the body of the consultation paper is the proposal that capital adequacy requirements would be imposed on all lenders, which would impact on organisations that do not take, or use deposits to fund lending. Similarly, much of the current consumer market lending is dependent on intermediaries. Making lenders responsible for the regulatory compliance of intermediaries would have a serious adverse effect on markets such as motor finance.

Our main areas of concern are:

- further unwarranted changes to consumer credit regulation
- the extension of the new regime to small business lending
- a requirement for all existing lenders to re-apply for authorisation for both existing and past business
- significantly higher regulatory fees
- the loss of the certainty of the legal position on loan agreements
- further disruption to business during the handover and changes
- lack of experience on consumer credit in the new Authority
- potential loss of Trading Standards Authority experience

Consumer protection within consumer credit has been strengthened over the years and with the implementation of European Consumer Credit Directive, and the move towards maximum harmonisation consumers are even more protected. The level of complaints dealt with by the regulator, or the Financial Ombudsman Service [FOS] are minute in comparison to number of loan agreements written. Companies are concerned about their reputation, and treat consumers with respect and dignity. The risk lies with the lender not the consumer, as no deposits are taken by the lenders outside of the banks, large finance houses and building societies. We believe that there is no compelling reason to move towards monitoring and reporting as consumers are already well protected.

The Coalition Government are continually stating their declared policy that enterprise and the SMEs are pivotal in the UK economy avoiding the real danger of a double dip recession. The Prime Minister has also stated that bureaucracy and regulatory red tape are the enemies of enterprise and that unnecessary regulation should be avoided at all costs. We believe that the changes that consumer credit has gone through in 1974, 2006 and now the implementation of the Consumer Credit Directive in February 2010 should not be changed yet again to fit FSMA 2000. Moreover, we believe that it would create havoc in the consumer credit market to change from regulation giving clear legal certainty to a, principles and rules based approach.

We believe therefore that Option 2 is the best option and that consumer credit should remain under the current regulatory framework and body, preferably an OFT style that would allow the market to retain the legal certainty of the current regulation with appropriate and proportionate enforcement.

Yours sincerely

Steve Capewell
Group Compliance Director
1st Stop Group

ADDLESHAW GODDARD

Addleshaw Goddard LLP response to HM Treasury

A new approach to financial regulation: Consultation on reforming the consumer credit regime

Introduction

Addleshaw Goddard LLP is a law firm who routinely acts for banks, building societies and other financial services firms. We have a very strong focus and reputation for advising in relation to retail financial services. Our firm is ranked Best in UK in the legal directory Chambers and Partners for consumer finance.

We act for a wide range of clients spanning a large range of clients including the main clearing banks, building societies, major credit card issuers, non-status secured lenders, home credit providers, pay day lenders, leading aggregators, debt purchasers and debt management companies. We work closely with the British Bankers' Association, the Finance and Leasing Association, the Building Societies Association and the Consumer Finance Association. Our financial regulation team comprising lawyers who were formerly advisers to the OFT and the FSA.

Our position working alongside so many different financial services firms and trade associations means that we are well placed to provide a balanced view of the industry as a whole.

In relation to the consultation on the transfer and reform of consumer credit regulation in the UK, the interests and views of our different clients are not aligned. Whilst we do not wish to promote any one of those views over those of others, in our response we have attempted to provide an overall assessment of the genuine pros and cons of each approach and have suggested some approaches and observations that we believe the Government must take into account before finally deciding on a way forward.

In responding to the consultation, in some cases, we have grouped your questions together where we believe they have a common theme rather than answering specifically each and every question where the same points could be made in relation to a number of them.

Finally, our firm was involved in Working Groups that considered the previous two rounds of reforms to the Consumer Credit Act. We would be happy to be involved in any such Working Groups formed for the purpose of considering these changes.

Q1 Do you agree with this assessment of the consumer credit market?

Q2 Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail financial services?

Q3 The Government would welcome further evidence relating to the consumer credit regime, including in particular:

- the types of risks faced by consumers in consumer credit markets;

- key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers;

- and the incidence of regulatory duplications or burdens on firms and/or inconsistent regulation of similar types of business.

Q4 Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?

In our view, this group of questions is focussed on establishing and testing what is the case for reform of the consumer credit regime in the UK?

We understand that the primary driver for the Government in considering reform of the consumer credit regime is one of consolidating or bringing together the regulation of financial services in a single regulatory regime (of course, it cannot be said that these reforms will, for the biggest players in the industry bring regulation within a single regulator since the new regulatory structure sees the creation of the FCA, PRA and FCA which will all have a role in regulating banks). The benefits of doing so can be summarised as:

(a) simplification of a single regime removing duplication

(b) a coordination and "single regulatory view" of the whole financial services market and, in the case of banks, a better and more coordinated view of the whole business of the bank rather than leaving pockets of regulation of some of their activities to other regulators.

We understand that this has support from many of our bigger bank and building society clients who are currently affected by the split in regulatory responsibilities. Of course, for a (larger number) of lenders (or "creditors" using the wider Consumer Credit Act definition which would capture debt purchasers) and ancillary credit providers in the market, they are currently not affected by regulatory duplication. Whilst some of these industry players may be authorised for insurance mediation by the FSA (which is not invariably the case) in the main, their day to day activities are all regulated by the OFT. Rarely does any significant problem occur for the vast majority of licence holders who are all regulated by the OFT.

Indeed, for many licence holders, the selling of credit is a secondary part of a much wider business – more likely to be focussed on the sale of goods or services to consumers. They may be introducing customers who want to buy their goods to lenders who provide the finance (store cards, in store credit, car finance providers etc) or they may simply be structuring the sale of their own goods and services in instalments (such as DIY stores providing trade credit to builders or gymnasiums allowing for their services to be paid for over a year).

For these businesses, their main activities are as retailers and their main regulator is the regulator of consumer protection – currently the OFT. Splitting credit into a different regulator for these organisations in fact significantly complicates their regulatory status and will only add to their regulatory burdens. No financial services regulator will ever be likely to be created in such a way as to really recognise those businesses as being outside the "real world" of financial services. Indeed, we would comment that, even at EU level, historically consumer credit had been dealt with as part of the remit of consumer protection. It has never been treated at EU level as a financial service as such. This is why

Directives such as the Banking Consolidation Directive, MIFID etc have never traditionally sought to deal with or include the provision of credit within their remit.

In our view, whilst we recognise the significant benefits bringing consumer credit regulation within the remit of a single financial services regulator could have for banks and building societies, we would stress that any reforms of the regulatory regime must be considered, not just in relation to their impact on a handful of main players in the industry, but on the industry as a whole – including all players in that industry. The case for simplification and rationalisation across that entire industry has not been made out – at least not by a blanket shift of consumer credit regulation to the FCA. That is not to say that there may be some case for consolidation for some industry players – but this should be weighed against the disadvantages of splitting regulatory responsibility according to the type of lender or other market participant involved.

We recognise that the Government has announced its intention to dissolve the OFT – which means that the Government will need to re-house the OFT's regulatory responsibilities. However, great thought needs to go into whether, for many (if not most) businesses involved in consumer credit, there is greater alignment to a consumer protection regulator (or other industry regulator, for example, in the case of debt management activities) than there is to a financial services regulator. The question is really one about how the Government defines financial services for the purposes of wanting to achieve a single regulatory approach (we return to this below).

This brings us back to the question of why the Government is reforming consumer credit. Whilst there is clear potential de-regulatory / simplification for some part of the industry, that is not universally the case. Thus, there must be other compelling reasons to reform consumer credit.

The Government has put forward the additional suggestion that the current regulation of consumer credit (and indeed financial services) is fundamentally weakened by the fact that no single regulator has an overall view of the financial services industry. Although the consultation does not expressly state what that weakness is – or at least how it has manifested itself – the financial crisis is alluded to as being, to some degree, the product of this regulatory weakness.

Of course, the causes of the financial crisis have been and continue to be the focus of detailed analysis and debate. However, fundamentally, the crisis occurred because residential mortgages were sold to those who struggled to repay and those assets were packaged and sold into the markets making them impossible to ring fence and identify. Whilst that may be analysed fundamentally as caused by "irresponsible lending", it is noteworthy that this occurred when residential mortgages and financial market regulation were all in a single regulator (the FSA) who had full market oversight of every aspect of the market that failed. There is no evidence to suggest that unsecured consumer lending added in any way to the crisis. While some unsecured assets may historically have been packaged up and sold into the market (in the form of securitisations) these particular vehicles were not at the heart of any financial crisis. Nor is it likely that some level of default on unsecured lending (which is, in any event to some degree predictable and factored in) would be likely to trigger the same level of economic turmoil since they are generally lower value and not directly linked to the housing market (itself a pillar of the economy).

As the economy is now in difficulty and as that will inevitably bring greater financial pressure on consumers, it is right to ensure that the right balance of lending and spending is maintained and that consumers and small businesses are not placed under undue additional hardship as the result of the management of already incurred personal debt or "irresponsible lending" now or in the future. However, it is not clear from the Government consultation how or why it is considered that those inherent risks with consumer credit are not currently being adequately addressed by the current regulatory framework and how a change to the FCA will inevitably provide any greater degree of protection in this regard.

Indeed, we would suggest that very little work has yet been done to assess what actual failings or risks the Government proposals are actually targeting. The consultation suggests that, rather than focus on the problems caused by the market and then legislate to address them by creating a better regulatory framework targeted at those risks, instead the Government is seeking to box consumer credit regulation into an existing regime simply because it suits the cost saving agenda of closing down the OFT.

What is more, the regulatory regime that is being proposed is one that is being created and consulted on quite separately from the question of it regulating consumer credit. Not only was the FSA never designed as a regulator for consumer credit, the FCA similarly is being modelled on a regulator never designed for consumer credit and itself being now adapted for regulating markets other than consumer credit. By the time consumer credit comes to be regulated by the PRA/FCA it will be an established regulator with established ways of working and regulatory objectives. It is not likely to be the sort of regulatory framework that can then be simply adapted to meet the needs of a very different market.

In the same vain, we expect any day a consultation on consumer protection regulation. That consultation will result in the establishment of a regulatory regime with no consideration for aspects of consumer credit that may end up being more suited to that regulator. This fragmented approach to the establishment of the regulatory framework is particularly problematic and does not enable the Government to truly create a regulatory framework for consumer credit. Instead, it rather looks like consumer credit will inevitably be pulled into one of more regulatory frameworks never designed for it.

In our view, before any decision is taken as to a new regulatory structure, a proper and thoughtful analysis of the risks posed by the consumer credit market and its function in the economy and society as a whole needs to be carried out.

As stated above, consumer credit does not pose a particularly significant systemic risk to the economy. If a consumer loan is not paid, the risk rests with the lender who does not recover its capital. This is fundamentally different to investment and deposit taking activities where the economic risk is borne by the customer. Even in the case of secured lending, again, the risk is borne by the customer whose property is at risk of repossession. In addition, in the case of secured lending, there is a direct correlation between lending and house prices.

The real risks in the case of consumer credit might be identified as follows:

- consumers at an individual level taking on too much credit and suffering financial detriment
- lending decisions that push individual consumers into hardship
- heavy handed enforcement of loans by lenders
- exploitation of vulnerable consumers who are tempted into credit they cannot afford
- small scale lenders who may operate as "loan sharks" who operate without or outside regulation
- consumers lack of consideration of credit decisions because they have already decided on a retail purchase
- consumers continuing to be committed to credit lines where funded goods or supply contracts go wrong
- credit being used as a tool to entice a sale which may not have been possible without it (e.g. large purchases such as home improvements or mobility aids where credit makes the purchase affordable)
- consumers being unable to compare across different products the best funding approach and inappropriately using available credit lines (such as unauthorised overdrafts when a credit card or pay day loan may have been a better choice).

These risks are not posed by a handful of large lenders (such as banks and building societies). Although a bad bank decision may affect several million customers and cause, across the consumer population, significant combined financial detriment, in consumer credit often the greater risk is posed by businesses operating outside regulation, on the margins, or within particular niche markets.

For example, when credit card issuers set default charges at around £30 per default, the OFT took action and limited charges to around £12 per default. That was something larger players in the industry were involved in and that decision meant that several million customers paid charges that the OFT would say they should not have paid. The amount of financial detriment was significant in economic terms. However, at an individual consumer level, many customers who paid those charges lost £18 in a month. To some customers that was significant, but not to all.

On the other hand, consumers who may have made small purchases on credit accounts associated with catalogue spend may have purchased an item of clothing for £25. Their payment may have been £1.50 for that month. If they missed that payment, in some cases there was the potential for the catalogue company to charge the customer £30 for the default. This left the customer owing £55 plus interest for clothing that should have cost them £25. The potential detriment here for that customer within that industry was far greater than for the generality of credit card customers.

Regulation in the consumer credit market must not therefore be systemically targeted, but instead should be focussed at where the real individual harm is likely to occur. We fear that the style of regulation by the FCA will not achieve this approach.

Q5 The Government welcomes views on the impact a unified regulatory regime for retail financial services may have in terms of clarity, coherence and improved market oversight.

The consultation papers focuses significantly on the desirability of having a single regulator for all financial services. However, there is no thought given to what precisely that means and why a "whole market" view would necessarily assist or what problems are associated with the split regulatory approach.

There are a handful of credit products where it might make sense to bring regulation together. For example, it makes no sense to split out the regulation of overdrafts from the regulation of the current account itself. Equally, it may make more sense to regulate credit cards (perhaps as opposed to store cards) by the FCA who is charged with the regulation of banks and payment institutions (since entities will need to hold such authorisation to members of the payment schemes and payment services regulation is a significant part of those products.

However, for other types of credit or roles in relation to consumer credit, it is not clear how the boundaries to a new regulatory regime should best be defined. The following are illustrative of the difficulties:

- Those involved in debt advice and debt management are part of the financial services market only insofar as the customer owes a debt or a series of debts. However, financial services debts are no different in consumer and market terms to any other debts the customer may owe (whether for rent, utilities, phone costs, consumer purchases etc). Many providers in that market are also regulated (for example as Insolvency Practitioners).

We do not see how the regulator of financial services is necessarily any better placed to regulate this industry nor how regulating activity in relation to only some of the debts those businesses deal with can be particularly helpful;

- For similar reasons, debt collection activities may also be considered to be more closely associated with the debt market rather than the financial services market. Like debt advisers, debt collectors collect on debts other than consumer credit debt.
- To add to the complexity, in some cases, debt collection firms actually buy the debts from the original originator of the debt. Under the Consumer Credit Act (CCA), such debt purchasers of consumer credit debts might become "creditors" under the CCA. They then take on regulatory obligations post contract that the original creditor would have had. It is clearer for these bodies that they might need regulating (at least for some of their activities) by a regulator of consumer credit. However, they would clearly be at competitive disadvantage if their regulatory regime was different to the regime applicable to other third party debt collection firms.
- Certain types of hire to consumers is regulated under the CCA. It would make sense to regulate some forms of hire alongside financial services. Hire purchase (which is treated as a credit transaction under the CCA) is legally a hire agreement with an option to purchase. Similarly, many asset finance providers (some of whom are linked to larger banks) will provide credit sale, hire purchase and conditional sale alongside pure hire arrangements. To them, it would make little sense to split the regulator for hire from the rest of the asset finance market. However, participants in the hire industry would not regard their business as related to financial services (for example the car hire industry).

There is mention in the paper around the possibility of confusion for consumers. However, it is not clear to us that it is a significant issue to the consumer to understand which regulator regulates which products (over and above needing to fix the split product difficulties referred to above) so long as there are signposts to the regulator. Indeed, we suspect that the brand of the FSA in the consumer's eyes and the consumer's awareness of the FSA is far less than the consumer's awareness of the OFT.

Q6 The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.

These responses need to be read alongside our responses to Qus 10 and 12 below which consider the important function of local regulation.

We believe that there is unhelpful "layering" and duplication of regulatory responsibilities. By way of example, there are a multitude of "regulators" appointed under Part 8 of the Enterprise Act and Unfair Terms in Consumer Contracts Regulations (including bodies such as Which?). On top of this, there are several consumer bodies all charged with the similar function of protecting consumers.

We believe that there is a strong case for streamlining those bodies. However, in doing so, we would stress:

- It is not appropriate for a regulator – who must weigh up cases impartially – to be some sort of consumer voice. The FSA relationship historically worked well because it is based on a more open and balanced style of regulation where there is a greater degree of dialogue between a business and its regulator. A regulator who uses information obtained in good faith in the interests of transparency and openness to champion a cause would not be appropriate.
- In the consumer credit market, it is imperative to retain some form of local regulatory bodies who are suitably funded and well placed physically to understand, visit and assess the impact of both small and large creditors within their local communities. Removing regulation to a large building in Canary Wharf will not address the very real and serious consumer harm that can be caused by smaller players in the market. Retaining local regulation will also assist the regulator to really understand and develop an open and approachable relationship with those it regulates.

Q7 The Government welcomes views on factors the Government or the CPMA may wish to consider in the event of a transfer of consumer credit regulation relating to how the overall level of consumer protection might best be retained or enhanced.

We refer to our response in relation to Qus 1 - 4 for a consideration of the risks that any new regulatory regime for consumer credit must target and address. Given that these risks posed in the consumer credit market are largely conduct risks and given that banks and building societies generally:

- have very large legal and compliance departments to seek to keep businesses operating fairly and compliantly;
- lend in the relatively mainstream market where questions of affordability and consumer vulnerability tend not to be so prevalent;

it is generally not the case that banks and building societies do, in fact, pose the greatest risk to consumers in this market. Indeed, it is for this very reason that the consumer credit activities categorised as "high risk" by the OFT do not typically involve mainstream lenders. Those categories cover activities such as debt collectors, fee paying debt management and certain types of non-status lending.

Whatever regime the Government chooses to put in place, it must be genuinely capable of regulating those parts of the industry that pose the greatest risk. These are often smaller market players whose margins are tighter and whose legal and compliance resource is significantly less. This is not to suggest that all small lenders or players in "niche" markets are rogues, but those businesses are generally the ones whose customer base starts off with a greater degree of vulnerability (whether through lack of education, social mobility, age etc). Their costs compared to the amounts being borrowed may also be higher – therefore causing the proportionality of debt to more likely spiral when things go wrong and they are businesses who, by their nature, must take a greater degree of risk in making a lending decision.

Creating a very heavy handed regulatory regime could, for example, push those who would otherwise apply to be regulated (and who can then be actively monitored properly) away from obtaining the necessary approvals. This may cause those lenders to operate below the radar and increase the social problems and costs associated with tackling loan sharks.

Equally, a regime that requires too much by way of investment in legal and compliance support may push lawful businesses out of the market. By way of example, some of the largest pay day lenders have very small legal and compliance departments due to the relative scale of the businesses involved. This could result in markets no longer being served by credit providers and increase the risk of loan sharks backfilling that market. The risks of market contraction and exit are very real. Both mortgage regulation and insurance regulation when they went to be regulated by the FSA resulted in significant market contraction with small industry players leaving the market. In the case of consumer credit, those products simply will not be supplied by the more mainstream and larger credit providers.

Similarly, creating a regulatory system that then places more ongoing scrutiny and requirements on the main players (such as banks and building societies), but providing for a "light touch" approach for smaller players will unfortunately miss the point of where regulatory activity needs to be targeted in the credit market. It is also inefficient in targeting resource at the areas of real detriment. Whilst such an approach will plainly be likely to prevent the next "default charges" case and save millions of customers a few pounds over a long period, it does nothing to address the areas where significant detriment is being suffered by fewer customers, but to a much greater degree. The current FSA regimes (and so the FCA regime) is predicated as a system on the fact that a few large players pose greater risk than the smaller players do.

Whatever decision is taken, it would be wrong to simply layer ever greater scrutiny on a handful of players in the market who do not pose the greatest risk and fail to target those large players' competitors in the market thereby creating a distorted competitive environment for lenders and other players in the market.

Q8 The Government would welcome further evidence relating to:

- the use of consumer credit by small and medium sized enterprises (SMEs);

- whether the protections currently afforded by the CCA are appropriate and cover the right groups of businesses; and

- the costs and benefits of considering extending FSMA-style conduct of business rules to a wider group of SMEs.

The regulation of SME lending under the CCA is not well thought out, has very little logical approach and now produces a highly complex regime made up of sporadic exemptions to some provisions of the CCA. The produces a fragmented regulatory approach which does not appear to have a sound rationale for being the way it is.

Although we talk in terms of SME lending being covered by the current CCA, the current scope of the CCA in relation to business does not produce this result. Business lending is caught where the borrower is not incorporated or is a partnership of 3 or less persons (defined in the CCA as an "individual"). The test is not one measured by turnover (which is the approach taken in other legislation dealing with businesses, where the definition of a "micro-enterprise" is used). Furthermore, the removal of partnerships of 4 or more partners from regulation happened only a couple of years ago meaning that there are significant back books of agreements which are regulated where the partnership is a very large organisation.

SME lending is not covered by the Consumer Credit Directive. In implementing the Directive, the UK Government gold plated the requirements by applying some of the new requirements to SME lending,

SME lending needs to be removed from the CCA and a proper and thought out approach to the necessary regulation of SME lending needs to be made. For example, whilst all banks understand the importance of "responsible lending", businesses are being actively encouraged by Government to extend lending facilities to SMEs in circumstances where there is a level of risk associated with the lending decision. In this case, regulatory obligations around responsible lending are potentially not appropriate and the requirements on lenders to businesses need to reflect that greater subtlety.

Q9 The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.

The consultation paper appears to be based on an assumption that a Rule Book style approach to regulation is generally more flexible in addressing the difficulties and adapting to the market. This is, no doubt, because for amendments required to primary legislation, Parliamentary time generally needs to be secured and, with competing priorities, some initiatives inevitably take longer to deal with.

We have sympathy with this position. As the consultation paper raises, the issues around sending statutory notices to customer who have gone away or are deceased is a good example where Government recognises an error was made that needs correcting, but the error (it is claimed) requires an amendment to primary legislation and Parliamentary time cannot be secured.

In principle, we believe this to be correct and that greater flexibility is achieved where requirements are not prescribed in primary legislation.

However, we do not believe that it follows that a Rule Book approach is therefore the best option. History has not demonstrated that a Rule Book provides for greater flexibility or clarity:

- PPI was a product openly sold in the market and sold at the time the FSA took on insurance regulation and throughout FSA regulation. Rules were made and then amendment only once during this period. Those rules did not apparently address or respond to the issues with the product now focussed on which the FSA and others were aware of at the time;
- The Government was the first to introduce an express requirement to lend responsibly under the CCA. MCOB contained various requirements around affordability, but no express responsible lending duty. This requirement came in to force on the credit industry relatively recently. Since then, the OFT has conducted widely scoped consultation, issued 3 updated versions of its Irresponsible Lending Guidance and more detailed guidance in what it referred to as a Frequently Asked Questions Guidance. Contrast this to the position on regulated mortgages where the FSA has been carrying out a review of the mortgage industry since 2009, has made very few changes yet to MCOB and continues to consult on question of responsible lending in relation to mortgages.

We believe the following problems are associated with the current Rule Book style approach:

- The FSA (quite rightly) is under an obligation to carry out proper and thorough consultation on issues before making or changing rules. This process can be long and drawn out.
- The ability to engage with the FSA's consultations is very difficult when the volume (and length) of CP, DPs and PDs that are issued is so great. This places very significant difficulties on smaller businesses who are simply not resourced to track and deal with all that information.
- The style and length of the current Handbook makes it hard to follow and piece together. Distinctions between rules and guidance place firms in an unsatisfactory position and introduce uncertainty. Furthermore, because the FSA both makes and enforces the rules, in practice, the FSA makes rules or advocates new approaches when they make a speak, by issuing a DP etc. This not only leaves firms with significant uncertainty and changes rules overnight, it also means that historic agreements are placed at risk as the rules (or more normally, the approach of the regulator) are changed retrospectively.
- The fact that legislation is interpreted by a court provides greater certainty (and fairness) for businesses who has the comfort of being able to obtain a legal decision on a point of importance. There is now a good body of case law which provides clear guidance on areas of the CCA and the industry would lose that certainty if those rules were

transcribed into a Rule Book where the same worded rules would not benefit from the same interpretation since the legislative context and approach will have changed.

It would generally be better if either:

- the CCA became a framework Act which simply provided for legislative powers to contain prescriptive requirements regulating the detail. This is the way that FSMA works. In many cases, it is also the way the CCA works with, for example, the detailed requirements for agreements, advertisements, pre-contract information etc being prescribed by SIs. There are, however, areas where the CCA could be slimmed down further – for example, the power to determine what agreements, lending, lenders or ancillary credit activities were regulated could be set out in SI and a more general power enabling Government to prescribe by SI what post sale notices were required and when could be created. Taking this approach, the CCA would require some amendment to create a more general framework with the current detailed provisions simply being moved into new SIs. This would provide the flexibility without removing or amending substantial current CCA requirements in relation to which lenders have clarity and certainty about what is required from them.
- the CCA in totality is, in effect, copies out into an SI along the lines adopted by the Payment Services Regulations and E-Money Regulations. We expect that, to achieve this, the Regulations would need to be based on an implementation of the Consumer Credit Directive (so as to utilise the powers under the European Communities Act). E-Money is, in fact, an interesting example which Government should think more carefully about. The regulation of e-money used to be dealt with by rules in the FSA Handbook (ELM). However, the new E-Money Directive has caused the handbook approach to be rethought and ELM is being repealed with the EMD being transposed into a set of Regulations instead. Presumably Government took the view that it was more appropriate in all the circumstances to implement EU requirements in legislation rather than through a Rule Book.

Q10 The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.

Q12 Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the Government's objectives (as outlined in paragraph 1.18 of Chapter 1)?

As stated above in relation to Qu 7, we fear that moving to an FSA style regulatory model will miss the targeting of resource at businesses who actually pose a greater risk.

The FSA model is based on a supervisory regulatory model. What that means in practice is that the regulator does not work at arms length from those they regulate. Instead, the regulator "gets inside" the business. The scrutinise and understand the firm's business plans, they have a say in who runs the business and has controlling responsibilities, they understand and influence businesses structures and reporting lines, they are told when a business does something wrong, the regularly meet with the business and discuss difficult issues, they gather information regularly from the business (through reporting) and someone who understands the business scrutinises that data to ensure things are staying on track.

Of course, this works for large banks and building societies who have those sort of relationships. They have an appointed supervisor who they can turn to and who assessed their business with that full understanding. However, for those who do not reach the required risk target and are small firms, their experience is very different. They generally deal with random people in a contact centre, there is no continuity and no understanding of them as a business. The supervisory relationship for these firms is much more at arms length.

Of course, this is right for firms who, by their scale and activities, pose a much lesser risk to the economy and to consumers. However, we are not sure how this can be made to fit a market with opposing characteristics where the smaller players are likely to pose the greater risk.

Certainly, the FSA is not resourced to manage closely on an individual supervisory basis these firms. In addition, these firms are not resourced to manage the ongoing requirements that such a current FSA regime would place on them. Even on current standards, it is likely that many firms would need to invest substantially in legal and compliance functions and in systems to be able to achieve regulatory reporting obligations.

For many of these firms, they will often operate out of localised offices (rarely based in London). Their best and closest relationships may be their local trading standards department who will visit their offices, see the way they run their business on the ground and who will receive consumer complaints (passed to them by other trading standards departments).

Clearly firms that pose significant customer risk must be effectively regulated, but there is no point creating a regulator that, through the very way it regulates, has no way of adapting – and is not resourced or set up to be able to adapt – to effectively and proportionately regulate a very different market.

Q11 The Government welcomes views on the synergies afforded by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.

The current consumer credit licensing regime is a highly effective consumer protection tool, not simply for those financial services firms who hold them, but for retailers who sell their goods, often on credit.

Large value goods and services contracts are the area where there is evidence that there can be greater levels of consumer detriment. These may be contracts for home improvements (double glazing, kitchens, building work), high value goods (cars, mobility aids or other products sold to vulnerable consumers). It is an essential part of these businesses that they hold a consumer credit licence to be able to sell those goods and services on credit (otherwise the purchase price is prohibitive of a sale).

The OFT has used the need to hold a licence to take effective action against firms it believed were operating businesses offering poor levels of service or selling practices or where the goods or services were generally of an inferior quality. The OFT is not restricted to the financial services contract itself in deciding fitness to hold a consumer credit licence. It will look more broadly at the wider selling practices of a firm. For example the OFT issued licensing guidance to car dealers which focussed, not on the sale of credit, but on the standards expected when selling cars. Because the OFT is a regulator of both general consumer protection and of credit, it is well placed to take this holistic approach to the regulation of this type of firm.

We do not believe that the same effective level of consumer protection is likely to be achieved by the splitting out of the regulation of the credit sale from the regulation of the broader business. Nor do we see that lenders (if an Appointed Representative regime were favoured) could provide the same level of effective product regulation over firms that it deals with. We fear that a very important and effective consumer protection will therefore be lost by such a change in approach.

Q13 Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?

Q14 Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?

See also our response to Q5 above.

As stated above, we believe that any regulatory system must be designed to tackle the actual consumer harm posed by the industry. We do not believe that sufficient thought has been given to this by the Government. The factors and risks which must be addressed are:

- consumers at an individual level taking on too much credit and suffering financial detriment
- lending decisions that push individual consumers into hardship
- heavy handed enforcement of loans by lenders
- exploitation of vulnerable consumers who are tempted into credit they cannot afford
- small scale lenders who may operate as "loan sharks" who operate without or outside regulation
- consumers lack of consideration of credit decisions because they have already decided on a retail purchase
- consumers continuing to be committed to credit lines where funded goods or supply contracts go wrong
- credit being used as a tool to entice a sale which may not have been possible without it (e.g. large purchases such as home improvements or mobility aids where credit makes the purchase affordable)
- consumers being unable to compare across different products the best funding approach and inappropriately using available credit lines (such as unauthorised overdrafts when a credit card or pay day loan may have been a better choice).

We reiterate that these risks are not posed by a handful of large lenders (such as banks and building societies). Although a bad bank decision may affect several million customers and cause, across the consumer population, significant combined financial detriment, in consumer credit often the greater risk is posed by businesses operating outside regulation, on the margins, or within particular niche markets.

Q15 If you do not agree with the Government's preferred option 1, do you have views on the factors set out in paragraph 2.4 that the Government should consider in determining the most appropriate regulatory authority for the CCA regime under option 2?

As set out above, we do not believe that sufficient thought has been given to what is trying to be achieved by the reform of consumer credit. Although there may be merits for some lenders to be regulated by a single regulator (and that approach ought to be considered for those larger players in the market) such an approach does not bring universal benefit and risks making the regulatory system over the entire market less effective. Indeed, it is difficult to see how the regulatory regime being proposed (as a full handbook style FSA approach) goes anywhere near targeting properly the actual risks in the consumer credit market – and more importantly those who pose them.

Q16 The Government welcomes views on the suitability of the provisions of a FSMA-style regime, such as those referred to in paragraph 3.6, to different categories of consumer credit business.

Q17 Do you agree that statutory processes relating to CPMA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?

We refer to our responses to Qus 7, 11 above (as well as the section incorporating our response to Q5). An FSA style regulatory regime is really only effective as a regulator of large scale business who already invest substantially in compliance and who pose large scale systemic risk. In our view, the FSA has not shown that it has found an effective way of regulating smaller scale organisations without simply assuming that, as smaller firms, the comparatively pose less risk and consequently get significantly less scrutiny. That model will not work for consumer credit and for the large number of players in this market.

Although the proposals for FCA regulation provide for some "tweaks" to that regulatory approach, we cannot see how such an approach will achieve the right level of scrutiny at the right types of firms. This involves a very different approach to risk – something which is not articulated in the consultation paper. However, given the costs of running a regulator the size of the FSA (which are comparatively very substantially higher than the costs of the OFT which currently also uses that more limited budget to regulate competition and general consumer protection) it is inevitable that the fees for that will need to be paid by those who can afford to pay them – even where those firms do not carry the greatest consumer risk. This means that larger banks will be required to subsidise the regulation of the industry as a whole and the more extensive work needed to regulate smaller businesses.

Q18 The Government welcomes views on key factors that would need to be assessed in considering fee arrangements for consumer credit firms.

Other than our response to Q18, we have nothing further to add on fees.

Q19 The Government welcomes:

- evidence relating to experiences of the current appointed representatives regime;

- views on how an appointed representatives model might be applied to different categories of consumer credit activities, including how current business models and networks might lend themselves to such an approach; and

- evidence relating to the implications an appointed representatives regime might have for firms and consumers.

In our view, the AR regime only really works well where the AR is acting on behalf of another party and not, in effect, for its own ends. This is because the principal regulated firm takes regulatory responsibility for all of the activities of its AR. It is hard, if not impossible, for firms to shoulder that responsibility where it is not in a position to assert any real influence or control over the way that the business is being run or the activities carried out.

On this basis, in our view, the only likely candidates for using an AR approach would be:

- the brokerage of credit products (where a firm introduces a consumer to a source of credit) and
- third party debt collection where the debt is still owned by the original creditor, but the collection of that debt has been outsourced.

However, there are difficulties with the above.

Firstly, loans are often brokered by firms for a number of different credit products at the same time. For example, a car dealer often will not have an exclusive relationship with one lender. The types of loans available, the terms of the loans, the processes for selling the loans etc may all vary for different lenders. In addition, those lenders only have any control over the manner in which its own credit deals are sold. It has not control over the wider business of the dealer, nor of the way the dealer sells credit offered by other firms.

Furthermore, although the lender may be able to ensure decent levels of audit are carried out for the brokers it does business with, that will normally be limited to inspecting areas of the business which will be directly relevant to the activities the broker will be undertaking for that lender. A lender would not be qualified to make a wider assessment of the business. Similarly, there may be arrangements which are commercially sensitive or where a broker may be uncomfortable enabling a lender to inspect. A lender in a commercial relationship does not have inspection or disclosure powers, cannot enter and inspect premises without notice, and is not an effective regulatory substitute. Given that one of the greatest risks posed by consumer credit lending is at point of sale and the mis-selling of loans inappropriately, it does not seem an effective targeting of that risk to "outsource" regulatory supervision to lenders under an AR model.

In relation to debt collection, in addition to the above (it is very normal for third party debt collectors to collect debt for numerous lenders using its own developed processes and procedures rather than those of the lender), it would seem wrong to us that the regulation of this industry would be split according to whether a debt collector had or had not purchased the debt.

Q20 The Government welcomes:

- evidence relating to experiences of the current group licensing regime; and

- views on how the professional bodies regime might be adapted for different categories of consumer credit activities.

We have no view on the manner in which group licensing generally works. However, we would note that the group licensing regime has, in the past, helpfully been used slightly wider to deal with particular problems. For example, when the Government introduced a Cycle to Work scheme in the workplace, these arrangements works on the basis of a hire agreement with the business. In order to ensure that all businesses who wanted to take advantage of this scheme did not all need to become holders of OFT licences for hire, the OFT created a group licence to cover those types of businesses.

Due to the very wide scope of consumer credit regulation, these types of arrangements frequently arise. The ability to deal flexibly or to grant an exemption from regulation should be retained. Consideration would also need to be given to how to maintain any such exemptions for these types of activities under any new regulatory regime.

Q21 The Government welcomes views on the extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises.

We are supportive of the idea behind self regulation and believe that it is important that trade associations and other industry bodies are able to introduce code requirements which enhance the level of regulation.

However, fundamentally, we believe that codes should set standards that go beyond what the Government or regulators believe to be the acceptable level of practice. In recent years, there has been a move away from clear and certain regulatory standards – breach of which give rise to regulatory action – in favour of a higher level of uncertain regulation with codes being used by Government and regulators to implement standards of regulation that they require on the industry. Examples of this approach are:

- Breathing space requirements
- Risk based re-pricing
- Various aspects of the lending code
- Provisions dealing with payment allocation, minimum payments, credit card statements
- Current account charging

This makes the process of securing compliance arbitrary. Only firms represented by strong trade associations tend to get a voice in these discussions and these types of discussions tend to be carried on with no open consultation. The requirements are only an effective regime where all firms belong to the trade association whose code has implemented or endorses the requirement. This leaves open the ability of firms who are not members of a trade association not to comply.

The result is also that codes do not raise standard below an acceptable level, but become the setter of that minimum benchmark. In our view, this is not an appropriate way to regulate. Therefore, whatever legal structure is decided upon for the regulation of consumer credit, it must be sufficiently clear, applicable to all, and set an appropriate and certain level of consumer protection that does not rely on codes to fill in gaps in that regulation. If industry then chooses to maintain codes that go beyond that level, that should be seen as a positive approach – but not a necessary one to achieve that right degree of regulation.

Q22 Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.

The Government is limited in what activities can be deregulated as a result of the Consumer Credit Directive which regulates all loans between EUR 200 and EUR 75,000. However, the UK generally chose to regulate loans above this level.

There are a large number of organisations (such as private banks) who lend to ultra high net worth customers, normally very large loans, who now find that they need full CCA lending processes in place. These types of customers use legal advisers and other agents to negotiate the loans and are generally well equipped to look after their own affairs. The requirements of CCA regulation do not sit well with the type of customers these are and the type of relationship these banks have with them. For example, having to explain the basics of a credit deal, the fact that their home may be repossessed etc in a face to face discussion is not appropriate where the loan is being taken out by a person who is using lawyers and who owns several properties all of a high value etc.

We believe, therefore, that there would be merit is reviewing the need to regulate (or at least regulate in the same way) large value loans.

As set out in relation to Qu 8, there is also a need to re-consider the regulation of business lending to ensure a better and more coherent and appropriate form of regulation for these products.

Q23 Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approach?

See our responses to the other questions.

Q24 The Government welcomes views on how the treatment of agreements already in existence could be approached.

We are very concerned about any suggestion that back book agreements also move regulatory regime and become, from the point of new regulation, regulated by a different regulator and different rules.

We can see that there may be certain products where the length of the loans means that it would make sense for them, after a certain period, to be transitioned over into a new regime. An approach like this has been taken to certain product in the past. However, we would stress that this has happened in relation to a discrete number of changes to a regulatory regime and not where an entire regime (and possibly all of the rules and requirements) have changed in relation to that product. Products are created and priced in accordance with the regime applicable at the date of the making of the agreement. While some changes may be capable of being accommodated within the structure of that product, that is not necessarily always the case.

One way of dealing with this difficulty would be to enable lenders during the transitional period to place customers on new agreements without requiring the them to obtain a customer signature or express agreement. This would enable lenders to place new customers on the same or similar terms to any new customers going forward without needing to be concerned about how to achieve that by way of forced variation or obtaining express customer sign in.

For shorter term agreements, we would be far more concerned about any regime change which resulted in either:

- a new regulator taking a different approach to historic compliance or the requirements that should be in place for such products going forward which were not in place at the time of product design;

- a set of new rules applicable to these products which change the costs associated with running or offering those products going forward or which might make new regulatory requirements inconsistent with current terms and conditions of agreements which may not be capable of being varied under limited contractual rights of variation.

However, regime change is achieved, it must not create any level of uncertainty for agreements already entered into. Such re-opening of requirements for portfolios of agreements already entered into creates serious potential financial exposure if such an approach would open up risk of challenge by customers, a change in or new approach by the FOS, or a new line of potential focus for claims management companies looking for the next revenue generator.

Q25 The Government welcomes views on:

- how existing licensees could be dealt with; and

- factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms.

Given the large number of licences involved, we would have thought the only reasonable and sensible course would be to grandfather into the new regime existing licensees. Not to do so would open up very significant risk and uncertainty for certain types of business who operate in niche sectors (for example, debt management firms, small scale pay day lenders, some debt collection firms etc). Furthermore, if those firms currently operate with a certain level of bank or private equity funding, any level of uncertainty over their ability to obtain a new authorisation under the new regime could result in funding lines being withdrawn or, certainly not being renewed. That could force some firms out of the market.

Of course, the new regulator should then, taking a reasonable approach to risk, inspect and consider whether any of those businesses should no longer be authorised under any new regime – allowing for a reasonable period of adjustment for firms. It may be that there could be a faster track route for the suspension or removal of authorisation during a transitional period if the new regulator considered a firm who had been grandfathered into the new regime was no longer fit and proper to be authorised under the new regime.

We do not think that it is appropriate to take a differentiated market sector approach to this issue.

Q26 The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.

We have no comment on this question.

Q27 Are there other factors the Government should take account of in considering transitional arrangements?

The Government will need to consider how to deal with the following types of scenarios:

- Licensees who have in the recent past have has their licence revoked.
- Ongoing Minded to Refuse or Revoke licence cases (including appeals). Do the proceedings continue but before the same or a different composition of adjudicators or tribunal? How does that translate into a new regulatory regime?
- How do ongoing case involving the voluntary or mandatory imposition of requirements transition into the new regime?
- Will files of historic information on licensees be capable of being transferred to the new regime and how will any of that information be treated by any new regulator?
- How should information which is currently on the public register be retained within the new regime – for example, in relation to Minded to Revoke or Refuse actions, historic licence information, requirements imposed etc;
- How will any informal or formal undertakings given to the OFT be treated – particularly where obtained under other powers, such as Part 8 of the Enterprise Act, if the OFT no longer exists?

Q28 The Government would welcome evidence on the experience of firms, consumers and their representatives in relation to similar previous transitions, for example the extension of FSA jurisdiction to new markets since 2000.

The type of transfer of the whole of the consumer credit regime to a new regulatory regime is very different to what happened previously where insurance mediation and regulated mortgages transferred regulators and where new Handbook rules have been implemented. This is because of the following:

- The scale of the industry transitioning is substantially wider than the previous industries where this has happened. The market participants are also far more diverse than any other market regulated by the FSA;
- Never before has the Government sought to transfer over a very detailed legislative regime into a rule book approach. Where mortgages became regulated by the FSA, the majority of these were not covered by the CCA due to the financial limit in place at the time. For most of these, the regime that applied was the Mortgage Code – a much easier document to transpose into a rule book approach. The same was also true of insurance where GISC applied previously and for bank accounts where the Banking Code previously applied;
- The regulation of mortgages and insurance by the FSA was not retrospective – it applied only to products entered into after the date of regulatory change. We are not aware of situations where back books have been transitioned over into a new regime and into a new regulator as is being proposed in this consultation.

Advertising Association response to the Treasury consultation on reforming the consumer credit regime

1. **The Advertising Association**

   The Advertising Association is the only organisation that represents all sides of the advertising and promotion industry in the UK - advertisers, agencies and the media. In the UK, the advertising industry employs nearly 250,000 people. In 2009, advertising expenditure was £14.5bn.

   We promote and protect advertising. We communicate its commercial and consumer benefits and we seek the optimal regulatory environment for our industry. Our goal is that advertising should enjoy responsibility from its practitioners, moderation from its regulators, and trust from its consumers.

2. **Overview**

   The Advertising Association supports any moves towards less and better regulation. As such, the overriding policy objectives of simplification and deregulation set out in the consultation paper are ones that we as an industry support. The Government's drive towards greater clarity, appropriate consumer protection and proportionality when undertaking this structural reform is something that we would support.

   We establish in this paper our view on the broad approach to the reform of the consumer credit regime; we anticipate that as this process continues there will be a need for the Advertising Association to engage with the Treasury to address some of the specific technical issues relevant to advertising. We look forward to working with the Treasury -and the Financial Conduct Authority (FCA) when it is created - to ensure that self-regulation for credit advertising is not undermined by the reform of the consumer credit regime.

3. **The current regime for consumer credit advertising**

   Any advertising by a lender must comply with the Consumer Credit (Advertisements) Regulations 2004 (CCAR). This is supported by OFT Guidance, as well as the broader requirements of the broadcast and non-broadcast advertising codes, upon which the Advertising Standards Authority (ASA) adjudicates. These advertising codes approximate the provisions of the Consumer Protection from Unfair Trading Regulations 2008. Article 4 ("Standard information to be included in advertising") of the Consumer Credit Directive contains provisions aimed at further enhancing protection in respect of the advertising to consumers of credit products. For broadcast advertising, the system benefits from having advance central clearance for credit advertising, provided by Clearcast and the RACC, who pre-vet advertisements prior to them being broadcast.

   In non-broadcast advertising, the ASA will refer advertising complaints for technical issues to Local Trading Standards Departments for a view under the CCAR, rather than adjudicating on them themselves. In broadcast advertising the ASA is responsible for regulating all aspects of credit advertising, including both the 'softer' issues and the technical aspects. The ASA works closely with both the FSA and the OFT (depending on the product) when dealing with complaints about financial advertisements. The current system is very effective and we urge Treasury to protect this self-regulatory structure for advertising when reforming the broad consumer credit regime.

4. **Consumer protection**

In the Government's paper, references made about the benefits for consumers of moving regulation to the FCA are not specified, and nor is there substantial evidence-base to the assertions made in this paper which suggest that the consumer is not protected in the current system.

The current market for consumer credit works well both for businesses and for consumers. Indeed, there is a range of different types of products on offer for consumers. The full range of consumer credit products are marketed in different ways and, as one would expect, are targeted to the consumers who are most likely to be interested in such products.

The advertising and marketing of consumer credit enables this important component of the economy to grow, increasing competition between businesses as consumers choose between different providers. In an economic environment in which credit is in short supply, advertising has an important role in informing consumers about where credit is available. Competition is a highly effective means of protecting consumers' interests. The FCA should have creating a competitive market place as a primary objective.

High-cost credit products (and its advertising) are much maligned in the press and by some politicians. We believe that such credit providers meet an important need for many people who cannot access credit elsewhere. The prices of credit reflect market realities and the Government should look at the macro-economic environment before assessing this particular sector, and the advertising it uses to promote its operation. When assessing consumer protection, it is imperative that any policy is evidence-based, and not reactive to media-hysteria.

5. **Self-regulation**

Consumer protection can often be best delivered through self-regulation which drives up standards and promotes good practice. The reputation of the financial services sector has undoubtedly been assisted by the work of the Advertising Standards Authority (ASA), which makes sure that consumers are given legal, honest, truthful, and decent information. This helps consumers are able to make the right decisions on credit. The (relatively few) consumer complaints to the ASA in this area are effectively dealt with by the ASA who have a good understanding of the "soft" issues – such as making judgments on whether credit is treated too "light heartedly" in advertising. We believe that the system in place is effective and works in the interest of both business and consumers. In reforming the consumer credit regime, it is essential that the role of the ASA is fully understood, and that unnecessary new layers of statutory legislation are not introduced.

6. **Restructuring the system**

Clearly with any fundamental restructuring of a system, there is a concern that the new entity may not be as clear for businesses. We would, therefore, support a model that retains as much of the existing legislation as possible. To encourage consistency, we support the CBI's recommendation that the OFT consumer credit team should move across to the FCA and should be tasked with responsibility for developing a new regulatory regime based closely on the current statutory regime and with a light touch approach.

Given that the ASA works closely with both the OFT and the FSA, plus the clearance houses Clearcast and RACC, the streamlining of the consumer credit environment may present an opportunity for providing both consumers and businesses with greater clarity. A new single regulator with a degree of continuity could improve the consumer credit market. However, this is an understandably complicated system and when the specific issues relating to advertising are raised, we would urge for the Government to engage with the Advertising Association, the ASA, and BCAP/CAP, Clearcast and RACC. There is naturally a concern that a "simplified" approach may inadvertently undermine the self-regulatory process and, in effect, make the entire system complicated.

The Government must provide industry with clear information on the interim arrangements between the current system and the new regime. All organisations, and particularly the OFT, must be adequately funded before they are dismantled or created, and clear lines of responsibility must be created. The Government must work to minimise costs for business which will be very significant if the regulatory rules and approach are changed, particularly for SMEs.

7. The future of the OFT

The Advertising Association is greatly concerned about the future location of certain competition and general consumer functions that currently fall to the OFT as part of the Public Bodies Act. While this specific issue does not relate to consumer credit products, it is an example of how attempts to simplify a system can inadvertently threaten to undermine self-regulation. The proposal to dismantle the OFT will have a significant impact on the work of the Advertising Standards Authority (ASA) as the OFT currently acts as the ASA's legal backstop for misleading non-broadcast advertisements.

The Government is proposing that Trading Standards could be given responsibility for enforcement of almost all consumer law, and that expert teams from within Trading Standards could be coordinated at a national level for national and regional threats. The AA is keen to ensure that the new structure for enforcing consumer law retains within it a strong, national body that is able to serve effectively as a legal backstop to the ASA.

It is such measures as this which would inadvertently damage the self-regulatory structure for advertising and we encourage the Government to ensure that the new regime does not weaken the strong statutory backstop for consumer credit advertising, nor is this statutory body unnecessarily strengthened. We do not support any strengthening of statutory powers of the OFT, the FSA or, when it is created, the FCA. Nor would we support ASA's expansion into what is currently the statutory enforcement role of trading standards officers. A careful balance is required and we would want to work with Government to ensure that the correct balance is met.

8. Conclusion

The Advertising Association encourages the Government to ensure that the new regime for consumer credit is strong, transparent and effective. To do so, we believe that new regime must retain as much of the existing legislation as possible and, while we support the Government's proposal to simplify the regime, we urge for this to be done carefully to ensure that there are no unintended consequences. Thus, we are very keen to engage with the Government on the specific issues relating to advertising as the process of reforming these integral organisations goes forward.

For further information, please contact William Blomefield – 020 7340 1109 / william.blomefield@adassoc.org.uk

<u>HM Treasury Consultation Paper:</u>

<u>A New Approach to Financial Regulation – consultation on reforming the consumer credit regime</u>

Age UK Enterprises Limited

Age UK Enterprises Limited is a wholly owned trading subsidiary of the charity Age UK. Its aim is to offer products and services to people in later life specifically meeting their needs. Profits are gift aided back to the charity, nationally and locally.

Age UK Enterprises markets and sells the following products and services:

- Home Insurance provided by Ageas Insurance Limited
- Car Insurance provided by Ageas Insurance Limited
- Travel Insurance provided by Ageas Insurance Limited
- Motor Breakdown Insurance provided by Europ Assistance Holdings Limited
- An Equity Release Advice Service provided by Just Retirement Solutions
- An Annuity Comparison Service provided by Premier Retirement Services
- Gas and Electricity provided by Eon
- Funeral Plans provided by Dignity
- Age UK Weekly Lottery
- Charity Flowers

The products and services offered have been tailored to meet a specific target audience, namely the over 55s.

Age UK Enterprises Limited is authorised and regulated by the Financial Services Authority in relation to its activities involving financial services. It has approximately 135 appointed representatives. These consist of local trading Age Concerns/Age UKs who are charities or trading subsidiaries of charities. Profits made from the sale of products and services are ploughed back into the charity to help deliver charitable services.

Age UK Enterprises has a consumer credit licence primarily in relation to the facility to pay by monthly direct debit offered on some of the insurance products (all of which are offered at 0% APR at present). Because of the commercial nature of the activity, even though profits are gift aided back to the charity we are not able to take advantage of the group licensing scheme meaning that all 135 appointed representatives are also required to be licensed individually to sell insurance by monthly direct debit. Some make very little money from trading (£15,000 a year) or conduct very limited introductory only type activities but still pay the same price for a Consumer Credit Licence. In 2010 many of our appointed representatives had to renew their Consumer Credit Licence. In excess of £100,000 was diverted away from delivering charitable services to pay for Consumer Credit Licences. The credit facility is provided by the insurer, Ageas Insurance Limited. Age UK Enterprises and its appointed representatives simply offer the facility to customers purchasing the product. There is no charge to customers who wish to use this facility and the APR is currently 0%.

Summary of response to consultation paper

In its paper the Treasury has proposed two options for the reform of consumer credit. These are:

- Option 1 – a regulatory regime for consumer credit under the new FCA (Financial Conduct Authority); or

- Option 2 – a specific consumer credit regime based on the Consumer Credit Act 1974

Age UK Enterprises would prefer option 1. It is already directly authorised by the Financial Services Authority and has adopted the necessary governance and compliance structures to ensure that it is meeting those requirements. It will already be caught by other proposals to transfer regulatory supervision from the FSA to the FCA and will need to be authorised by the new body regardless of these proposals. Having one regulatory body will significantly decrease the burden on the firm.

In addition, transferring consumer credit to the FCA will also be beneficial in terms of the licensing regime if Age UK Enterprises were able to add its appointed representatives to a licence and remove the need for 135 appointed representatives to be individually licensed by the OFT. Currently the proposals seem only to allow the creditor to appoint these individuals which doesn't reflect the FSA's current appointed representative approach.

Response to specific consultation questions

<table>
<tr><td colspan="2">Chapter 1: The case for reform of the consumer credit regime</td></tr>
<tr><td>1.</td><td>Do you agree with this assessment of the consumer credit market?</td></tr>
<tr><td colspan="2">Yes. Under the current system many firms are required to be authorised and regulated by the FSA as well as the OFT. In many cases the licensing requirement under the Consumer Credit Act is simply due to the fact that a credit facility is offered alongside a financial product. For example, many insurance intermediaries will sell car or home insurance which has the option to pay in instalments. This requires a licence from the OFT, even if the intermediary is not the one providing the credit (this is usually the insurance provider).</td></tr>
<tr><td>2.</td><td>Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail firms?</td></tr>
<tr><td colspan="2">The current regime means that firms have to manage two regulators who operate in different ways. This can increase the regulatory burden on firms and can result in inconsistency and confusion among firms and consumers. This is particularly the case where a firm may be registered as a principal with the FSA and have a network of appointed representatives, who it can take responsibility for. Under the Consumer credit regime it cannot do this and appointed representatives are individually required to obtain licences direct from the OFT. This causes a significant burden on the appointed representatives as well as the principal, who in most cases, will end up providing significant assistance to the appointed representative.</td></tr>
<tr><td>3.</td><td>The Government would welcome further evidence relating to the consumer credit regime, including in particular:

• The types of risks faced by consumers in consumer credit markets;
• Key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers; and
• The incidence of regulatory duplications or burdens on firms and/or inconsistent regulation of similar types of business</td></tr>
<tr><td colspan="2">The key risks faced by consumers in the consumer credit arena relate to the fact that the OFT do not regulate those firms offering credit or debt advice in the same way that the FSA does. Where firms are regulated by both the FSA and the OFT, it results in very different systems and controls needing to be put in place. Often a consumer credit specialist is needed in addition to any compliance function solely to manage the different requirements and regime in place.

The clearest example of regulatory burden relates to FOS fees. Age UK Enterprises pays these fees</td></tr>
</table>

through the FSA for itself and business conducted by its appointed representatives. As a directly authorised firm we are not required to pay FOS fees when we apply to renew our Consumer Credit Licence; however, our appointed representatives have to pay FOS fees to the OFT (they have recently paid in the order of £20,000) even though they make no money from credit brokerage (the facility to pay monthly is offered at 0% APR).

4.	Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?

Yes. Given the changes currently occurring to the regulation of financial services now is a good time to make these changes to consumer credit. It is appropriate that the regulation of consumer credit and other credit services, such as mortgages, be considered by one regulator. This will allow for much better oversight without overburdening firms.

Chapter 2: Options for the future of consumer credit

5.	The Government welcomes views on the impact a unified regulatory regime for retail financial services may have in terms of clarity, coherence and improved market oversight.

The impact of a unified regulatory regime for retail financial services firms is likely to reduce the regulatory burden on firms already authorised and regulated by the FSA. The benefits include:

- Reduced regulatory burden as firms will only have one regulator to deal with;
- Improved authorisation process and greater use of the appointed representative network
- Greater consistency in terms of approach in how sales around similar products are conducted;
- Greater clarity for customers as linked products will fall under a similar set of rules and will not require a complete new set of disclosures, for example general insurance sold by monthly direct debit.

6.	The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.

No comments

7.	The Government welcomes views on factors the Government or the CPMA may wish to consider in the event of a transfer of consumer credit regulation relating to how the overall level of consumer protection might best be retained or enhanced.

Any amendments to the Consumer Credit Act will need to consider the impact on existing consumer agreements. The transfer should aim to ensure that consumers are not confused by their obligations or their rights in the event of a disagreement.

In addition to differences in enforcement action, consideration should also be given to the sales process, particularly where the credit is an add-on to the main purchase (i.e. insurance).

8.	The Government would welcome further evidence relating to: • The use of consumer credit by small and medium sized enterprises (SMEs); • Whether the protections currently afforded by the CCA are appropriate and cover the right groups of business; and • The costs and benefits of extending FSMA-style conduct of business rules to a wider group of SMEs.

Age UK Enterprises is a wholly owned trading subsidiary of the charity Age UK. It sells products and services to specific targeted money with all profits donated to the charity. It is directly authorised by the FSA and has an appointed representative network of approximately 135 local trading offices. These consist mainly of local trading Age UKs/Age Concerns.

Age UK Enterprises sells (amongst other things) general insurance products such as home and car

insurance. The insurer provides a credit facility allowing for the payment of these payments to be made by monthly direct debit. As a result of the above setup, Age UK Enterprises is regulated by both the FSA and is required to have a consumer credit licence. The proposals under Option 1 would greatly simplify the regulatory approach and burden for Age UK Enterprises. This is particularly the case given that the appointed representative network would also be adopted under the new proposals.	
9.	The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.
For those firms directly authorised by the FSA as well as the OFT there is unlikely to be any significant impact. Firms regulated by the FSA are already subject to rules-based regulation. The flexibility provided by this approach means that consumers are able to benefit much quicker where there are clearly problems with the rules. Firms are able to provide their feedback and comments during the consultation process and these are considered as part of any proposed changes.	
10.	The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.
A more consistent approach is likely to result in greater consumer protection. A greater emphasis on supervision and risk prevention by the regulator will lead to improved outcomes for consumers as firms think more about what they need to do to ensure fair outcomes for consumers.	
11.	The Government welcomes views on the synergies by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.
No comments.	
12.	Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the Government's objectives?
The Government's objectives of clarity, coherence and improved market oversight, effective and appropriate consumer protection, simplification and deregulation and proportionality and cost effectiveness would all be better achieved under single retail financial services regulation. A single regulator would have much greater oversight of the consumer credit market, including mortgages which are regulated by the FSA. It would also be able better supervise firms and impose additional requirements where these are needed for consumer protection.	
13.	Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?
Potential disadvantages will be for those firms not currently regulated by the FSA, who will need to adapt to a new approach to regulation.	
14.	Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?
Under the current Consumer Credit Act regime, firms apply for to undertake specific types of consumer credit business, for example credit brokerage or debt advice. Consideration will need to be given as to how this will operate under option 1. Will firms seek permission solely for consumer credit or will it be types of consumer credit business? Consideration will also have to be given to how the Approved Persons regime will apply.	
15.	If you do not agree with the Government's preferred option 1, do you have views on the factors set out in paragraph 2.4 that the Government should consider in determining the most appropriate regulatory authority for the CCA regime under option 2?

No comments. Age UK Enterprises agrees with the Government's preferred option 1.	
Chapter 3: Achieving a proportionate and effective regulatory approach	
16.	The Government welcomes views on the suitability of the provisions of a FSMA-style regime, to different categories of consumer credit business.
Many firms subject to FSA regulation are already required to follow these requirements and will merely be extending the controls within their businesses to include consumer credit. Age UK Enterprises has an Approved Person for each of its appointed representatives. Under FSA rules it is only required to have one Approved Person in place as the only regulated activity carried out by the appointed representatives is insurance mediation. If Age UK Enterprises had to appoint additional Approved Persons for each of its appointed representatives this would result in a significant increase in the regulatory burden. Age UK Enterprises would want to continue to be able to rely on this FSA rule in relation to Approved Persons.	
17.	Do you agree that statutory processes relating to CPMA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?
Yes, different firms posed different risks and the current system of one fee regardless of size does not take into account the resources that the regulator will need to allocate to firms of different sizes. In addition the activities undertaken by different firms also varies considerably, with some firms engaging in more risky aspects of consumer credit. Fees should proportionate to avoid smaller firms subsiding larger firms.	
18.	The Government welcomes views on key factors that would need to be assessed in considering fee arrangements for consumer credit firms.
Key factors that the Government would need to consider include: • Type of activity • Income generated from consumer credit business	
19.	The Government welcomes: • Evidence relating to experiences of the current appointed representative regime; • Views on how an appointed representatives model might be applied to different categories of consumer credit activities, including how current business models and networks might lend themselves to such an approach; and • Evidence relating to the implications an appointed representative regime might have for firms and consumers.
Age UK Enterprises has an appointed representative model with approximately 135 appointed representatives. As principal it takes responsibility for the actions of its appointed representatives. All appointed representatives (including Age UK Enterprises) have licences with the OFT to carry out credit brokerage activity (i.e. offer payment by monthly direct debit for insurance products). The credit provider is the insurer and not Age UK Enterprises. The proposal put forward in paragraph 3.31 suggests that brokers would need to be appointed representatives of the creditor. In the scenario described above, this would require Age UK Enterprises' to be registered as appointed representatives of the insurer (who is the creditor). This would undermine Age UK Enterprises current set up in that it is the Principal and delivers certain services, such as appointed representative status and products. Age UK Enterprises contracts with the insurer to deliver products and services via the appointed representative network and takes	

responsibility for compliance of its appointed representatives with FSA and other regulatory frameworks, such as consumer credit. The proposal where brokers would need to appointed representatives of the creditor (i.e. the insurer) would undermine Age UK Enterprises current set up. It would mean that in addition to the 135 individual contracts we have with our appointed representatives the insurer would need to enter into 135 contracts and that the insurer would need to replicate the compliance arrangements we already have in place. Feedback from the appointed representative network has suggested that they find the process of obtaining a consumer credit licence complicated and very time consuming. In the majority of cases, guidance and assistance is provided by the Compliance Department within Age UK Enterprises. Having an appointed representative network for consumer credit would significantly reduce the burden on both appointed representatives and the principal. However this would only be workable if Age UK Enterprises were able to be directly licensed and appoint its own appointed representatives, as with the current set up with the FSA.	
20.	The Government welcomes: • Evidence relating to experiences of the current group licensing regime; and • Views on how the professional bodies' regime might be adapted for different categories of consumer credit activities.
No comments.	
21.	The Government welcomes views on the extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises (SMEs).
No comments.	
22.	Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.
There is some justification for arguing against the deregulation of credit brokerage in the cases where the credit facility is offered alongside a regulated product and particularly where the APR is 0%. For example, customers are frequently able to pay for their home and car insurance by monthly direct debit. Both of these products are already heavily regulated by the FSA. In addition, the credit facility does not usually last more than one year when the insurance cover expires and the customer is required to either renew their policy or purchase a new policy. In scenarios such as this the risk to the consumer of detriment is relatively low. It would be a relatively simple process to enhance the terms and conditions of the cover to include relevant clauses relating to this facility, without the need for a credit agreement.	
23.	Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approach?
No comments.	
24.	The Government welcomes views on how the treatment of agreements already in existence could be approached.
No comments.	
25.	The Government welcomes views on: • How existing licences could be dealt with; and • Factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms.
No comments.	

26.	The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.
Key factors that would need to be considered in transitioning from the current to a new fee structure would include: • How much firms already authorised by the FSA are contributing; • Considering the impact on firms who are within their 5-year maintenance period and have already paid up front fees • Considering the different maintenance periods held by firms who are appointed representatives of an FSA regulated firm.	
27.	Are there other factors the Government should take account of in considering transitional arrangements?
No comments.	
28.	The Government would welcome evidence on the experience of firms, consumers and their representatives in relation to similar previous transitions, for example the extension of FSA jurisdiction to new markets since 2000.
No comments.	

We, the Association of Bridging Professionals (AOBP), are writing in response to the consultation papers to provide our view as to how the issues highlighted in the papers would affect us.

We represent a large proportion of the intermediary market through our body of brokers, lenders, legal and compliance experts. All of our members have first-hand experience of the short-term lending/bridging market and think it is necessary to make you aware that the issues being raised within the consultation papers will have different effects on the short-term lending market to that of the mainstream mortgage market.

We provide a service to intermediaries, master brokers and packagers in the short term lending industry by providing a forum for discussion on non-competitive issues, acting as a trade body to help promote a favourable operating environment and providing information to assist them in their business.

Our objectives are:

- To be a central representative body to put the views of Bridging Professionals to the FSA, OFT, Treasury and any other relevant Government body or organisation which impacts on the operation of the Bridging industry.
- To provide members with information to enable them to keep up to date with matters affecting the Bridging industry.
- To work closely with the Association of Short Term Lenders to iron out any disputes between AOBP and ASTL members.
- To promote a forum for the exchange of non-competitive information.
- To encourage members to deal with customers in a clear and transparent manner and to treat them fairly

Our response to the consultation is as follows:

1. Do you agree with this assessment of the consumer credit market?	Yes we broadly agree with the assessment
2. Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail financial services?	Yes – particularly with the different formats and requirements for secured loans on residential property, the complexity of the CCA regime and the OFT's less intrusive regulatory methods.
3. The Government would welcome further evidence relating to the consumer credit regime, including in particular: • the types of risks faced by consumers in consumer credit markets; • key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers; and • the incidence of regulatory duplications or burdens on firms	Short term lending, commonly known as bridging finance, is, by its very nature, generally required urgently. Much of this lending is exempt from CCA as it is for business purpose, to high net worth individuals or secured against an investment property but often requires firms to obtain the correct exemption certificate. An anomaly is that there is no exemption certificate required if the loan is secured on an investment property. It is quite typical of this type of lending for the

and/or inconsistent regulation of similar types of business.	amounts required to vary shortly before completion which does not allow time for a new pre-offer to be issued. Indeed, a lot of loans would typically be completed in less than a week. This makes CCA lending generally non-viable, thus restricting consumers access to urgent funds. This has often been a source of frustration to consumers and those seeking to advise them. The general inflexibility and complex rules of CCA carries significant risk for lenders and the investment required in compliant automated systems and expert staff makes it an unattractive proposition. Likewise intermediaries need to understand and have in place compliant systems to sell CCA loans. Many intermediaries find this too much of a burden and lenders are concerned that the actions of intermediaries can be binding on them, reducing the attractiveness of this type of lending. The paperwork required for CCA loans is typically less clear for consumers than that for FSA loans. More short term lenders would be willing to offer secured lending under FSA regulation rules than CCA rules and there is no evidence that consumers would be worse off under FSA regulation than under CCA regulation. Some examples of inconsistencies include: The CCA generally focuses on the purpose of the loan, making business lending secured against a home as a second charge exempt. However if it was a first charge this would be regulated by the FSA. Why should one consumer have the protection of a regulated loan for business purposes just because he has no mortgage (and thus would be FSA regulated) and another consumer not have a regulated loan because he has a mortgage already? A loan secured on an investment property is exempt regardless of the purpose. A loan secured against a home to purchase an investment property would not be exempt unless it was a second charge and the borrower could demonstrate that this was his business (in which case it falls under the CCA regime). A loan secured on an investment property to buy a home would not be regulated. As loans of less than £25,000 for business purposes are not exempt from the CCA many

	firms set minimums above this which means customers may have to borrower more than they need. This also impacts further advances which are also often set with minimums above £25,000 in order to save the lender costs and the risks of writing CCA regulated loans. This is not beneficial to the borrower.
4. Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?	The AOBP would very much like to see these reforms take place. We believe that these would be both beneficial and appropriate even if only applied to second charge lending.
5. The Government welcomes views on the impact a unified regulatory regime for retail financial services may have in terms of clarity, coherence and improved market oversight.	We believe that unification should provide the consumer with a simpler and clearer regime. Only having one regulator should also lead to better oversight, especially for those firms currently dually regulated.
6. The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.	No comment on this topic
7. The Government welcomes views on factors the Government or the CPMA may wish to consider in the event of a transfer of consumer credit regulation relating to how the overall level of consumer protection might best be retained or enhanced.	AOBP believes that the removal of the 7 day cooling off period for secured lending against property should occur when combining the two regimes. This will allow borrowers to access funds for traditional bridging finance. Introduction of the 7 day cooling off period to loans currently under the FSA regime would destroy the viability of the short term finance industry and have a significant negative impact on consumers. We would urge the CPMA to rely more on the current MCOB regulatory regime than the highly complex and costly CCA regime.
8. The Government would welcome further evidence relating to: • the use of consumer credit by small and medium sized enterprises (SMEs); • whether the protections currently afforded by the CCA are appropriate and cover the right groups of businesses; and • the costs and benefits of considering extending FSMA-style conduct of business rules to a wider group of SMEs.	Generally short term lenders avoid loans to businesses of less than £25,000 due to the complexity and cost of running CCA regulated loans. This can cause a negative consequence for SME's who require a further advance. They may have to borrow over £25,000 to get it as the lender will not offer CCA loans. Even if they are willing to borrower the higher amount it may not be available to them due to lack of sufficient equity to secure the higher amount. This is to the detriment of the consumer. There does not appear to be any logic in applying protection to loans for business purposes based

	only the size of the loan or further advance being below the £25,000 limit. Consumers who put their home on the line should receive adequate protection.
9. The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.	More short term lenders would be willing to offer secured loans that currently fall under CCA regulations if they were under MCOB based rules. More intermediaries would be capable of advising under an MCOB style regime than CCA regime thus providing greater choice and support for consumers. There would be more competition which should lead to better outcomes for consumers. Dually regulated firms could achieve significant cost savings by operating only one scheme.
10. The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.	AOBP believes that FSMA style supervision should enhance the current CCA regime leading to greater consumer protection
11. The Government welcomes views on the synergies afforded by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.	No comment on this matter
12. Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the Governments objectives (as outlined in paragraph 1.18 of Chapter 1)?	Yes
13. Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?	If the business and high net worth exemptions are removed then more lenders currently operating outside of both the CCA and FSA regulations would need to be regulated which would reduce the potential for consumer detriment. Likewise intermediaries operating in the non-regulated space would either have to become regulated if they were not already or see their business opportunities reduced. This would increase the level of consumer protection and help stamp out any bad practices. Regulated firms are likely to be more careful with their non-regulated activities.

14. Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?	Removal of the cooling off period for secured loans would be beneficial in encouraging more lenders to provide short term loans under an MCOB style regime.
15. If you do not agree with the Government's preferred option 1, do you have views on the factors set out in paragraph 2.4 that the Government should consider in determining the most appropriate regulatory authority for the CCA regime under option 2?	N/A
16. The Government welcomes views on the suitability of the provisions of a FSMA-style regime, such as those referred to in paragraph 3.6, to different categories of consumer credit business.	There is a logic in requiring all firms offering secured loans to meet the same standards and comply with the same rules of business. Non-secured lending may require some additional checks and balances given the often vulnerable nature of the borrowers but his should be able to be built into the new regulations.
17. Do you agree that statutory processes relating to CPMA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?	Yes
18. The Government welcomes views on key factors that would need to be assessed in considering fee arrangements for consumer credit firms.	Whilst the costs will be an important factor the bigger issue is likely to be how easily and quickly intermediary firms that are not already FSA authorised can transfer to the CPMA and what support may be offered to come to terms with FSA requirements. This is important given that intermediaries in this position will not necessarily have all the background information on historic consultations and reports on topics such as TCF and may need some clear guidance and pointers.
19. The Government welcomes: evidence relating to experiences of the current appointed representatives regime; views on how an appointed representatives model might be applied to different categories of consumer credit activities, including how current business models and networks might lend themselves to such an approach; and evidence relating to the implications an appointed representatives regime might have for firms and consumers.	No comment
20. The Government welcomes: evidence relating to experiences of the current group licensing regime; and views on how the professional bodies regime might be adapted for different categories of consumer credit activities.	No comment
21. The Government welcomes views on the	These could be incorporated into the treating

extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises.	Customers Fairly requirements
22. Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.	No comment
23. Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approach?	No comment
24. The Government welcomes views on how the treatment of agreements already in existence could be approached.	Short term lenders would find this aspect relatively easy to cope with given that agreements are for less than 12 months and could be run off of the books in existing format. AOBP sees the benefit of one regime being only having to run one system and logically, therefore, loans should be transferred. Running two systems side by side for a lengthy period would not be beneficial. The key is to ensure consumers do not lose any of their rights, but repealing of the regulations could reduce administrative burdens. AOBP believes a 3 year transitional period should be long enough for firms to complete transfers with an option for any firm not wishing to transfer or meet the new CPMA requirements to continue to run off their book but not write new business.
25. The Government welcomes views on: • how existing licensees could be dealt with; and • factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms.	AOBP would be mainly concerned with the treatment of intermediaries. Those with current FSA permissions in this area should not be required to change their permissions to offer second charge loans. Those who only have CCA licensing will need to prove they meet the standards applied for Home Finance Arranging so must apply. There will also be firms who hold neither CCA or FSA regulation who may require to become authorised if the high net worth and business purposes exemptions are removed. Some form of fast tracking may be appropriate subject to CRB checks.
26. The Government welcomes views on key factors that would need to be considered in	No comment

transitioning from the current to a new fee structure.	
27. Are there other factors the Government should take account of in considering transitional arrangements?	No comment
28. The Government would welcome evidence on the experience of firms, consumers and their representatives in relation to similar previous transitions, for example the extension of FSA jurisdiction to new markets since 2000.	No comment

HM Treasury & Department for Business, Innovation and Skills

A new approach to financial regulation: consultation on reforming the consumer credit regime

Response from the Association of British Credit Unions Limited (ABCUL)

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HMT & BIS – reforming the consumer credit regime

ABCUL Association of British Credit Unions Limited

1. Introduction

1.1 We welcome the opportunity to respond to this consultation. ABCUL is the main trade association for credit unions in England, Scotland and Wales, and our members serve around 80% of Britain‟s credit union membership. Credit unions are not-for-profit, financial co-operatives owned and controlled by their members providing safe-savings and affordable loans facilities. Increasingly credit unions offer more sophisticated products such as current accounts, ISAs, Child Trust Funds and mortgages.

1.2 At the end of September 2010, credit unions in Great Britain were providing financial services to 780,251 adult members and held almost £634 million in deposits with more than £502 million out on loan to members. An additional 111,035 young people were saving with credit unions.[1]

1.3 At 30 September 2010, the 325 credit unions belonging to ABCUL were managing around £512 million of members‟ savings on behalf of over 611,037 adult members.

1.4 The Credit Unions Act 1979 sets down in statute the objects of a credit union; these are four-fold:

- The promotion of thrift among members;
- The creation of sources of credit for the benefit of members at a fair and reasonable rate of interest;
- The use and control of their members‟ savings for their mutual benefit; and
- The training and education of members‟ in the wise use of money and in the management of their financial affairs.

1.5 Credit unions in Britain are small, co-operative financial institutions often extending financial services to those unfairly excluded from the financial services the majority take for granted. They are owned and controlled by a restricted membership and are operated for the sole benefit of this membership. The Credit Union Act 1979 sets down these operating principles in law.

2. Government support for the expansion of credit unions

2.1 The central, local and devolved governments of the UK have consistently supported credit union expansion and development in recognition of the benefit that they provide.

2.2 Since 2005, credit unions have been the principal delivery partners of the Department for Work and Pensions‟ Financial Inclusion Growth Fund which has provided £98.5 million in capital for on-lending to those at risk of financial exclusion and without fair access for affordable credit services. The 317,798 loans made under the scheme to September 2010 represented a total interest saving of between £119 and £135 million compared with alternative, high cost lenders.[2]

[1] Figures from unaudited quarterly returns provided to the Financial Services Authority
[2] HM Treasury – Evaluation of the DWP Growth Fund: http://www.hm-treasury.gov.uk/d/evaluation_growth_fund_report.pdf

2.3 In recognition of the excellent work that the credit union sector had done in delivering the Growth Fund, a £73 million modernisation fund has now been set up by the Department for Work and Pensions which will provide both direct support to the credit union sector and – pending feasibility studies – make capital investment including the possible development of a shared banking platform, for which funding has already been set aside. Subject to successful feasibility studies, this will open up opportunities for many more people to access credit union services, including through the Post Office network so that millions more people can access their credit union‟s services on their local high street.

2.4 Alongside direct investment, the coalition continues to press ahead with the legislative program begun by the previous government with a view to unleashing the potential which has until now lain dormant under the strain of a restrictive legislative framework. The Legislative Reform (Industrial and Provident Societies and Credit Unions) Order, the Co-operative and Community Benefit Societies and Credit Unions Act 2010 and a forthcoming order to enable credit unions to benefit from some electronic communication powers already enjoyed by companies are all set to provide the credit union sector with the strong, proportionate and flexible legislative framework that they require to play a greater role in the provision of financial services in society.

2.5 In addition, steps have been taken to support credit unions through the proposal to enshrine within the new regulatory framework, set to replace the Financial Services Authority, a requirement that any proposed new regulation is evaluated to ensure that it does not unduly disadvantage the mutual model and therefore contributes to a level playing field.

2.6 These are a selection of the proposals which are being brought forward in the current context to support the development of a strong credit union sector in line with the government‟s commitment in its Programme for Government „*to foster diversity in financial services, promote mutuals and create a more competitive banking industry'*.[3]

2.7 As Mark Hoban, Financial Secretary to the Treasury, said in his speech to the All-Party of Parliamentary Group on Credit Unions shortly after taking office last summer: "*We are determined to help credit unions grow and expand into the future. But growth and expansion must be established on the basis of credibility – credibility that can only come as credit unions build sustainability. And it is in the interests of credit unions, the members of credit unions and the movement as a while that sustainability is built. This Government believes strong credit unions will greatly enrich British society, so it is in our interests to do whatever we can to help the credit union movement to prosper.*"[4]

2.8 It is in this context of enthusiastic and consistent support for the expansion and development of the credit union movement that the current proposals find themselves. Ensuring the proportionate regulatory treatment of credit unions in support of their continued expansion is a key element in

[3] The Coalition: our programme for government: http://www.direct.gov.uk/prod_consum_dg/groups/dg_digitalassets/@dg/@en/documents/digitalasset/dg_187876.pdf
[4] Speech by Mark Hoban, FST, to the APPG on Credit Unions (30.06.2010): http://www.hm-treasury.gov.uk/speech_fst_300610.htm

implementing the government‟s vision of a diverse financial services industry with a strong mutual presence.

3. Credit unions and consumer credit regulation

3.1 Credit unions‟ core activities are providing deposit and lending facilities to their members.

3.2 As deposit-takers they are regulated under Part IV of the Financial Services and Markets Act 2000 and as such are primarily regulated by the Financial Services Authority which has created the proportionate, specialist regime outlined on page 28 of the consultation document.

3.3 Credit unions‟ lending activity, on the other hand, is exempt from the Consumer Credit Act under the Consumer Credit (Exempt Agreements) Order 1989 as amended by the Consumer Credit (Exempt Agreements) (Amendment) Order 2006. These Orders provide that loans made by credit unions are exempt from the regulation of the Consumer Credit Act by virtue of being the sole loan agreements in the UK jurisdiction operating under an interest rate cap and the fact that the terms of the cap prevent any extra charges being levied in respect of a loan. The 2006 Order brought the exemption into line following the raising of the credit union cap from one percent per month on the reducing balance of a loan to 2 percent per month.

3.4 Furthermore, the EU Consumer Credit Directive 2008, which was transposed into UK law earlier this year, provides for the exemption of certain organisations described by the directive as follows:

5. Member States may determine that only Articles 1 to 4, 6, 7 and 9, Article 10(1), points (a) to (h) and (l) of Article 10(2), Article 10(4) and Articles 11, 13 and 16 to 32 shall apply to credit agreements which are concluded by an organisation which:

(a) is established for the mutual benefit of its members;

(b) does not make profits for any other person than its members;

(c) fulfils a social purpose required by domestic legislation;

(d) receives and manages the savings of, and provides sources of credit to, its members only; and

(e) provides credit on the basis of an annual percentage rate of charge which is lower than that prevailing on the market or subject to a ceiling laid down by national law, and whose membership is restricted to persons residing or employed in a particular location or employees and retired employees of a particular employer, or to persons meeting other qualifications laid down under national law as the basis for the existence of a common bond between the members.

Member States may exempt from the application of this Directive credit agreements concluded by such an organisation where the total value of all existing credit agreements entered into by the organisation is insignificant in relation to the total value of all existing credit agreements in the Member State in which the organisation is based and the total value of all existing credit *agreements entered into by all such organisations in the Member State is less than 1 % of the total value of all existing credit agreements entered into in that Member State.*[5]

3.5 This description is designed to catch all organisations operating under the principles of a credit union and therefore allows the Member States to treat credit unions proportionately. The exemption allows our sector to operate without needing to comply with onerous requirements as a result of being small and being organised solely for the benefit of their membership.

3.6 The Department for Business, Innovation and Skills – in implementing the Consumer Credit Directive – took advantage of this freedom to exempt credit unions in line with pre-existing consumer credit legislation in the UK as outlined above.

3.7 On an analysis of the most recent and complete data we have available to us relating to the end of September 2008, of around 280 ABCUL credit unions – a sample including all of the largest credit unions in Britain and representing the vast majority of credit unions in operation at the time – 222 credit unions or 78% had less than 5 staff and 168 or 60% had less than £100,000 turnover. 90 credit unions, or just over 30%, employed no staff and relied entirely on volunteers for both governance and operational support. 80% of credit unions made profit of less than £50,000, 56% making less than £10,000.

3.8 As such, credit unions are predominantly small organisations with significantly limited resources and therefore any burden presented by extra regulatory compliance would limit their ability to operate sustainably and, ultimately, to grow. Given the sector‟s size, having to comply with the consumer credit regime would present a significant and disproportionate burden upon it.

3.9 It is in this context of consumer credit regulation that the current proposals present themselves. Credit unions have been afforded exemptions by way of proportionate treatment in consideration of their size and on the basis that their operations – as co-operatives – are considered naturally beneficial to their membership and are organised under an upper interest and charge limit so that the scope for consumer detriment caused by a credit union is minimal.

3.10 Our key concern with the proposals under review here, therefore, is that – whichever option is pursued – the exemption for credit union loan agreements is maintained in line with the current legislative provisions of both the UK and EU. Credit unions – as explored in section 2 – have been explicitly identified as capable of „enriching‟ British society and, as such, policy development has been geared to their extension and growth. Were the proposals here, which are explicitly intended to create a more responsive but *proportionate* regulatory regime, to increase the burden of regulation upon the credit union movement they would be inconsistent with the government‟s overall credit union policy.

[5] DIRECTIVE 2008/48/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:133:0066:0092:EN:PDF

4. Other issues arising from the proposals

Auxiliary credit activities

4.1 Whilst credit unions are not required to gain a consumer credit licence for their lending activity, they are required to gain approval for money advice and credit referencing activities undertaken auxiliary to their core lending business and in line with their statutory objects; educating members in the wise use of money and creating a source of credit for the benefit of members.

4.2 At present, there is an onerous process through which credit unions are expected to pass in order to be approved for these activities. This process acts as a deterrent both to responsible lending practices and to providing informal support to credit union members with, for instance, basic, free advice – preparing a personal budget, for example, or negotiating with a single high cost creditor to enable the member to move his or her debt to the credit union at a much lower interest rate.

4.3 We feel that there is deregulatory scope, were option one to be pursued, to nuance the requirements around credit unions" auxiliary credit activities so that the true nature of the activity – i.e. altruistic support and responsible lending for the benefit of members – can be taken account of and the burdens presented by the application process therefore reduced.

4.4 One obvious means of reducing this burden, as we have previously expressed to the Office for Fair Trading, would be to allow credit union approval under the non-commercial category.

Group Licensing

4.5 We are also concerned that under the proposed new Financial Conduct Authority there presently would be no way of providing a group licence regime comparable to the regime under the OFT. One means of relieving the current burden presented by the consumer credit regime is for ABCUL – as a trade association – to hold a group licence on behalf of our membership. It would be a considerable concern were this option to be closed to us.

4.6 The group licence option under the OFT is an important relief for smaller firms and we feel that any replacement regime should take steps to ensure that a comparable option remains in place.

Enforcement and consumer protection

4.7 Credit unions, as ethical, member-oriented organisations which exist solely for the benefit of their membership are often involved in supporting members who are experiencing financial difficulties and may be suffering as a result of another firms" misselling or non-compliance.

4.8 We are concerned, therefore, that there is a risk of consumer detriment during transition to and following implementation of the new system of enforcement and this could easily result in damage to the financial wellbeing of the public. As ever, any such burden is likely to fall on those with the least and those in the most vulnerable financial position – groups disproportionately represented amongst credit union members.

4.9 Should option 1 be pursued, steps must be taken to ensure that the rights consumers enjoy presently are not watered down or lost and that consumer awareness of where they need to go for redress is not diminished.

4.10 In a recessionary economy, with unemployment at high levels especially amongst the young, there is considerable scope for the firms to act against the best interest of vulnerable consumers. It is important that any reforms of the consumer credit regulatory regime do not exacerbate this but instead work to the advantage of consumers in the market.

Fees

4.11 Currently, under the OFT consumer credit regime, credit unions do not have to pay a fee for the consumer credit licences they hold for their auxiliary credit services. This measure exists in the name of proportionality. As has been touched upon, we still have concerns that the process of application for approval is burdensome but this would be further exacerbated were fees to be introduced. Many credit unions" total annual profit can be just a few hundred pounds. This is typically retained to build their capital base.

4.12 In 2008, of approximately 280 credit unions for which we have full data, 52% had less than £500k in assets and 56% made less than £10k in pre-tax profit. Furthermore, almost 80% had less than 5 staff. 30% had no staff at all, relying entirely upon volunteers. These are small organisations struggling for financial sustainability and which pose relatively little risk to the financial system.

4.13 Under the FSA"s current fee settlement, which was reviewed in 2009/10, credit unions are afforded unique exemption from the £1,000 minimum fee where they are below certain size thresholds. This is in recognition of the socially valuable role credit unions play and in support of the FSA"s statutory responsibility to ensure that its regulatory role is applied proportionately.

4.14 We have concerns that there is the potential, under option one primarily, that credit unions" proportionate fee treatment may be lost. Any increase in fees, especially for our smallest members, would have an extremely detrimental impact on their potential to grow and could potentially force more credit unions out of business. This in turn could lead to an increase in credit unions being declared in default and remove credit union services from significant numbers of consumers.

5. Conclusion

5.1 The coalition government, like its predecessor, has been clear and consistent in its support for the credit union sector. It committed in its Programme for Government to promote diversity in financial services including a greater role for mutuals. Credit unions have been explicitly identified as part of this agenda consistently by Ministers from across government.

5.2 A key element of credit unions" current proportionate settlement is their statutory exemption from the Consumer Credit Act under UK law and upheld under the EU"s Consumer Credit Directive.

5.3 If credit unions are to be supported to grow it is imperative – given the size of much of the sector – that regulatory and supervisory burdens are minimised. This provides the requisite room for credit unions to invest time and resource into building sustainability and maximising growth.

5.4 We also seek assurances that a proportionate regime will be maintained and extended for our sector in relation to auxiliary credit services, group licensing and fees. Furthermore, we hope that appropriate steps are taken to ensure that consumer detriment – which is a great potential threat in this process of transition – is not caused by mishandling the move or by a dilution of rights and awareness of these rights under the new system of enforcement.

5.5 Credit unions play a vital role in providing an alternative financial service to the people of Britain. It is imperative, if this role is to be extended in line with government‟s policy intention, that the erosion of the sector‟s proportionate treatment is not allowed.

March 2011

ABI RESPONSE TO BIS CONSULTATION ON REFORMING THE CONSUMER CREDIT REGIME

1. Introduction

The UK Insurance Industry

1.1 The UK insurance industry is the third largest in the world and the largest in Europe. It manages investments amounting to 24% of the UK‟s total net worth, contributes the fourth highest corporation tax of any sector, and employs over 275,000 people in the UK alone.

1.2 Insurance helps individuals and businesses protect themselves against the everyday risks they face, safe in the knowledge that problems can be handled and risks carefully managed. Every day, our members pay out £155 million in benefits to pensioners and long - term savers as well as £58 million in general insurance claims.

The ABI

1.3 The ABI is the voice of insurance, representing the general insurance, investment and long-term savings industry. It was formed in 1985 to represent the whole of the industry and today has over 300 members, accounting for some 90% of premiums in the UK.

1.4 The ABI‟s role is to:

- Be the voice of the UK insurance industry, leading debate and speaking up for insurers.
- Represent the UK insurance industry to government, regulators and policy makers in the UK, EU and internationally, driving effective public policy and regulation.
- Advocate high standards of customer service within the industry and provide useful information to the public about insurance.
- Promote the benefits of insurance to the government, regulators, policy makers and the public.

2. General Comments

2.1 The ABI welcomes the Government‟s commitment to reform the consumer credit regime.

2.2 We support the Government‟s objectives to create a simpler, more responsive regime, to remove unnecessary duplication of regulation for business, and to address anomalies that currently mean that similar products can be regulated under different regimes. It makes sense for one regulator to be responsible for conduct regulation of all retail financial services. We do not think it is in the customer‟s interest for consumer credit to be subject to a very different approach and level of regulation from, for example, savings products.

2.3 In light of these goals, the ABI hopes that the proposed structural changes will allow a more reasoned and coherent approach towards annual insurance contracts paid in instalments which, contrary to other European member states, continue to be regulated within the UK‟s consumer credit regime. Such inclusion provides customers with no greater protection than they are already afforded by virtue of FSA regulation, as at no point are they left with a debt. It does, however cost the insurance industry, and therefore, insurance customers, in excess of £50m per annum.

2.4 We would also ask the Government to consider exempting equity release mortgages from the consumer credit regime. These are single premium products that do not act in the same way as other credit agreements but still fall under the Consumer Credit Act (CCA). Firms providing these products also suffer dual regulation, resulting in a costly regulatory burden which has no positive customer outcome.

2.5 The Government‟s preferred option of bringing all regulation of the consumer credit regime together under a single regulator is a sensible one and is, we believe, the best option for tackling some of the problems we have experienced through dual regulation. However, it is crucial that the cost of any changes to the existing framework are proportionate, and that any assessment of cost takes into account those costs incurred by firms having to make systems changes, update documentation etc.

2.6 We believe that the cost of funding the new regime should be borne by those firms who fall within it, and not spread across other firms regulated by other parts of the Financial Conduct Authority.

3. Specific Comments

Q3. The Government would welcome further evidence relating to the consumer credit regime, including in particular:

- **the types of risks faced by consumers in consumer credit markets;**
- **key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers; and**
- **the incidence of regulatory duplications or burdens on firms and/or inconsistent regulation of similar types of business.**

Risks faced by consumers

3.2 The ABI is pleased that the Government recognises that the current division of regulatory responsibility for the consumer credit regime can lead to duplication and divergence of regulation, which in turn imposes disproportionate costs on industry without ensuring increased customer benefit. This is certainly in line with the industry‟s experience of the current regime.

Payment of annual contracts in instalments

3.3 Customers who choose to pay the premium for an annual insurance contract upfront are afforded the protection of FSA regulation. Customers who opt to pay that premium in instalments are also protected under the CCA. This means the latter are subjected to onerous checks on their credit.

3.4 Payment for insurance by instalment does not expose customers to the same risk as other types of credit agreements. Under conventional credit agreements, customers are obliged to make regular instalments over a determined period of time until their debt is repaid in full. Customers who pay for annual insurance contracts in instalments are free to cancel the contract at any time and will not be liable for settling the outstanding balance (subject to notification of cancellation periods).

Equity release mortgages

3.5 Equity release mortgages (ERMs) are regulated under both the FSA and the CCA, depending on whether a customer has decided to take further borrowing under their mortgage or not.

3.6 Customers who have bought an ERM are essentially not buying any credit, as they have made one deposit (their house) to pay for the service they receive, and will not be required to make any further payments in future. It is therefore not clear why they need the protection of the CCA.

Key consumer protection provisions

Payment of annual contracts in instalments

3.7 The insurance industry‟s experience of the consumer credit regime has shown that regulatory bodies tend to err on the side of caution by maintaining their own customer protection provisions, despite the fact that such protections are afforded elsewhere and are therefore unnecessary. We see this is in relation to the payment of insurance premiums in monthly instalments (PBI) and to ERMs.

3.8 Customers paying for annual insurance contracts in instalments are currently covered by existing FSA regulations:

- ICOBS 2.2.2 - when a firm communicates information, including a financial promotion, to a customer or other policyholder, it must take reasonable steps to communicate it in a way that is clear, fair and not misleading.
- ICOBS 4.1.9 - that all information to be provided to a customer must be communicated in a clear and accurate manner, comprehensible to the customer.
- ICOBS 4.2.4 - a firm must take reasonable steps to ensure a customer understands he is responsible for deciding whether a policy meets his demands and needs and that a policy's main characteristics include its significant benefits, its significant exclusions and limitations, its duration and price information.

- ICOBS 6.1.5 - a firm must take reasonable steps to ensure a customer is given appropriate information about a policy in good time and in a comprehensible form so that the customer can make an informed decision about the arrangements proposed.
- TCF Outcome 3 - Customers are provided with clear information and are kept appropriately informed before, during and after the point of sale.

Equity release mortgages

3.9 ERMs are currently covered by the CCA, although further borrowing under them is covered by FSA regulations in the Mortgage Conduct of Business Sourcebook (MCOB). The ABI believes the MCOB provisions are sufficient for customers buying an ERM.

Regulatory duplications and burdens

Payment of annual contracts in instalments

3.10 As of 1st February 2011, insurers are required to perform credit worthiness checks for PBI customers. This provides no added benefit for customers, as credit worthiness checks are usually necessary in cases where a customer enters a contractual agreement, under which they will be required to pay regular instalments for a certain amount of time until their debt is paid. In the case of insurance payment by instalments, the customer is free to cease payments at any time without owing the remaining balance, in the same way as they might do for utilities bills or a newspaper delivery service (both of which fall outside the CCA). Given that payment by instalments increases access to policies for the young and financially vulnerable, especially for motor insurance policies, reducing unnecessary burdens for such products should be a priority for the government.

3.11 These requirements add considerable cost to the industry, which is passed onto customers in the form of higher premiums. Prior to the introduction of credit worthiness checks, compliance with the CCA cost insurers in excess of £50million per annum; the new credit worthiness check requirements will increase those costs still further. The Government‟s insistence on treating insurance in instalments as credit is not risk-based, increases costs significantly and goes against better regulation principles.

3.12 Currently, the CCA goes beyond the requirements of the Consumer Credit Directive (CCD), where “agreements for the provision on a continuing basis of services or for the supply of goods of the same kind where the customer pays for such services or goods for the duration of their provision by means of instalments”[1] do not fall under the definition of a credit agreement (Article 3 (c)). This definition is further clarified in Recital 12, which states that "an insurance contract where the insurance is paid for in monthly instalments" should not be regarded as a credit agreement, and should therefore fall outside the scope of the CCA. Article 2, paragraph 2(f) of the CCD also

[1] Article 3 (c), DIRECTIVE 2008/48/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC

exempts “credit agreements where the credit is granted free of interest and without any other charges”[2]. This means that annual insurance contracts paid in monthly instalments with no interest or any other charges are clearly out of scope of the CCD. It is unfortunate that the UK government has chosen to gold-plate this Directive, which in theory is supposed to ensure maximum harmonisation amongst member states, but in reality appears to put the UK at odds with other Member States.

3.13 Analysis conducted by the UK Government found that of the 22 EU member states for which data is available, all have exempted payment of insurance instalments where no interest is payable from their national legislation, and 20 have also exempted payment of insurance instalments with interest (in accordance with the exemptions listed under Article 2, paragraph 2(f)). This puts UK firms at a competitive disadvantage compared to their European neighbours. Bringing the CCA in line with the Directive would reduce costs for insurers, without decreasing protection for customers, who are provided for under existing FSA regulation. This is in line with the Government‟s commitment to remove gold-plating of EU directives.

3.14 As from 1st February 2011, annual contracts paid for in four or fewer instalments without interest or any other charge (such as utility bills) are exempt from the CCA. Prior to 1st February 2011, four or fewer instalments were exempt from the CCA even if interest and other charges were included. We do not believe that customers paying for annual contracts in more than four instalments are exposed to greater risk than those paying in four or fewer instalments

3.15 Further, strict compliance with the CCA exposes insurers to risk. The CCA requires the customer to return a signed credit agreement to the insurer (or lender). Until the insurer holds an executed copy of the credit agreement, there is no binding agreement between the insurer and the customer for the provision of credit and the insurer will not legitimately be able to collect payments by direct debit nor serve a Default Notice should the customer default.. However, most insurers allow cover to start before the signed agreement has been returned. This is in the customers‟ interest, as any delays could at best expose them to excessive risk while they wait for the cover to start, and at worst put them in breach of the law (e.g. where the type of insurance is compulsory, such as motor). Yet this approach exposes insurers to the risk that the customer never returns a signed credit agreement, makes a claim, cancels the contract, and then demands his premiums be returned in the absence of a signed credit agreement. While this is not a common occurrence, we are aware of several instances of this happening in the past. The Government‟s recent proposal to allow credit agreements to be concluded online addresses part of the problem, but it does not address the whole problem, particularly for those customers who do not buy insurance over the internet.

3.16 The inclusion of the Distance SECCI places an unnecessary burden on insurers/lenders, a burden which is not justified by risks to customers. Under

[2] Article 2, para 2 (f), Consumer Credit Directive EC 2008/48

the previous CCA regime, lenders were not required to provide distance pre-contract information which is set out in a separate document from the credit agreement.

<u>Equity release mortgages</u>

3.17 ERMs, although single premium products, do not meet the exceptions listed in Section 16 of the CCA 1974. This is probably because equity release makes up an extremely small part of this market and does not fit within the other types products of products defined in this category. However, they are also regulated by the FSA. This leads to duplication in costs (i.e. FSA licence fee), compliance and monitoring.

3.18 An individual customer will usually only be subject to one of the two regimes. However, if a customer whose product comes under the CCA wishes to take further borrowing under the mortgage, the new lending will be subject to the FSA rules. This no doubt causes confusion to the customer who has a mortgage with two elements, each separately regulated.

3.19 The treatment of customers under two different regulatory regimes can also result in regulatory creep, where it is more practical and convenient to apply the highest level of regulation (usually CCA) to all customers, even if they are not directly subject to the regulations. Transferring the consumer credit business to a new form of consumer credit regulation would solve none of the problems of dual regulation outlined above, which are faced by both firms and their customers. Rather, we should like to see ERMs removed from the scope of the CCA altogether.

3.20 ERMs are an important source of retirement funding and are increasing in popularity . Considering the challenges currently facing policymakers in terms of supporting an aging population it is in the interest of the government to ensure that the regulatory costs of providing these products are not so burdensome as to put off providers from either entering or staying in the market. Any additional costs imposed as a result of regulation must be outweighed by benefit to the customer.

3.21 ERMs and other similar products have been successfully regulated under the MCOB regime since 2004, with no systemic evidence of customer detriment. In addition, mortgage providers who are members of “Safe Home Income Plans” (SHIP) observe the SHIP Code of Conduct, which contains guarantees that go over and above FSA requirements. Bringing ERMs fully under MCOB would therefore ensure customers are appropriately protected, as this regulatory regime is specially designed for the type of product which they hold. It would also ensure that customers who take additional borrowing do not suffer from confusion resulting from both parts of their mortgage being under different regulatory regimes. It is important not to discourage providers from staying or entering into the ERM market at a time when the product is becoming increasingly important

Q4 Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?

3.22 The Government‟s objectives are appropriate. We believe that exempting payment of annual insurance contracts in monthly instalments and ERMs from the consumer credit regime would help the Government achieve its objectives of simplification and elimination of double regulation.

3.23 The ABI also stresses the importance of proportionality and cost-effectiveness. The Government should ensure that the business cost of transitioning towards a new regulatory system, including changes to fees, processes, systems, documentation, literature and staff training delivers a more streamlined, effective regulatory approach.

Q9 The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.

3.24 As the Government has observed, a key benefit of a FSMA-style regime is that it is inherently more flexible and responsive than one set out in legislation.

3.25 The ABI hopes that such a regime would lend itself to more frequent and timely reviews than the current legislative approach, thereby ensuring that it is not too onerous on firms – for example with regards to insurance premium payment by instalments and ERMs.

3.26 The Government should be mindful of the potential costs incurred by firms transitioning to a new regime (see Q8 above).

Q10 The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.

3.27 We agree that the "FSMA style" regulatory and supervisory approach that applies to other retail financial services should be extended to consumer credit (notwithstanding the likely changes to FSMA as a consequence of regulatory reform). Currently, UK regulators take a very different approach to regulating the borrowing of money relative to the detailed conduct regulation that applies when customers save or invest – while we should not move to a „one size fits all approach‟, we think more coherent regulation of retail financial services would make sense.

Q14 Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?

3.28 Moving responsibility for consumer credit from the OFT to the FCA is likely to require major changes to insurers‟ processes, systems, documentation, literature and staff training, all of which will be both time consuming and costly. The Government must take care to ensure that the benefits of the streamlined approach really will exceed costs.

3.29 Further, we believe that the costs of funding the new regime should be borne by the users of the regime in proportion to their relevant size and scale of activities rather than other parts of the FCA regime supporting this activity.

3.30 If the Government decides to pursue this option, the ABI would welcome another review of the CCA regime in order to assess whether it is the appropriate regulation for all the products and firms currently regulated under it (for example insurance premium payment by instalments and ERMS). The ABI strongly believes that both types of product should be removed from under the CCA.

Q17 Do you agree that statutory processes relating to CPMA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?

3.31 One area of concern for industry is how the Financial Services Compensation Scheme (FSCS) will operate under the new regime. The ABI would welcome assurance that the CCA would be dealt with in a separate sub-scheme with no cross-subsidy from other parts of the scheme. Current contributors to the scheme should not be retrospectively liable for the redress of customers that may have suffered from unfair commercial practices in cases caused by historical failures under the CCA regime.

3.32 The ABI agrees that responsibility for the formation of rules regarding industry funding of the Financial Ombudsman Service (FOS) should transfer from the OFT and FSA to the FCA. We also believe that legislative changes are needed to enhance the accountability of FOS and clarify the respective roles of FOS and the FCA.

Q22 Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.

3.33 We believe that the payment of insurance in instalments and equity release mortgages should both be moved outside the scope of the CCA (see Q3 above).

Q26 The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.

3.34 The costs of funding the regime should be borne by the users of the regime in proportion to their relevant size and scale of activities rather than other parts of the FCA regime supporting this activity.

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Financial Regulation Strategy
HM Treasury
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London
SW1A 2HQ

23 February 2011

Dear Sirs

A new approach to financial regulation – Consultation on reforming the consumer credit regime

We are the Association of Short Term Lenders (astl). As our name implies we are the representative trade body for the short term lending industry. Short term lending is defined as making loans for periods of one year or less. Our website is www.theastl.org.

We are pleased to provide our comments and responses to HM Treasury's recent Financial Regulation paper and would be happy to provide any supplementary information if requested.

Kind regards

Yours faithfully

Adrian Bloomfield
CEO

Enc.

astl the association of short term lenders

HM Treasury Paper – December 2010

A New Approach to Financial Regulation – Consultation on Reforming the Consumer Credit Regime

1. Do you agree with this assessment of the consumer credit market?	Yes we broadly agree with the assessment.
2. Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail financial services?	Yes – particularly with the different formats and requirements for secured loans on residential property.
3. The Government would welcome further evidence relating to the consumer credit regime, including in particular: • the types of risks faced by consumers in consumer credit markets; • key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers; and • the incidence of regulatory duplications or burdens on firms and/or inconsistent regulation of similar types of business.	Short term lending, commonly known as bridging finance, is, by its very nature, generally required urgently. Much of this lending is exempt from CCA as it is for business purposes or secured against an investment property. It is quite typical of this type of lending for the amounts required to vary shortly before completion which does not allow time for a new pre-offer to be issued. Indeed, a lot of loans are typically completed in less than a week. This makes CCA lending generally non-viable, thus restricting consumers access to urgent funds. This has often been a source of frustration to both consumers and lenders. The general inflexibility and complex rules of CCA carries significant risk for lenders and the investment required in compliant automated systems and expert staff makes it an unattractive proposition. The paperwork required for CCA loans is typically less clear for consumers than that for other loans, including those regulated by the FSA.

	More short term lenders would be willing to offer secured lending under FSA regulation rules than CCA rules and there is no evidence that consumers would be worse off under FSA regulation than under CCA regulation. Some examples of inconsistencies include: The CCA generally focuses on the purpose of the loan, making business lending secured against a home as a second charge exempt. However if it was a first charge this would be regulated by the FSA. A loan secured on an investment property is exempt regardless of the purpose. A loan secured against a home to purchase an investment property would not be exempt (unless it was a second charge and the borrower could demonstrate that this was his business). All such anomalies cause confusion and difficulties for lenders and borrowers.
4. Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?	Astl would very much like to see these reforms take place. We believe that these would be both beneficial and appropriate even if only applied to secure lending.
5. The Government welcomes views on the impact a unified regulatory regime for retail financial services may have in terms of clarity, coherence and improved market oversight.	We believe that unification should provide the consumer with a simpler and clearer regime. Only having one regulator should also lead to better oversight, especially for those firms currently dually regulated. Life would also be simpler for lenders.
6. The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.	No comment on this topic.
7. The Government welcomes views on factors the Government or the CPMA may wish to consider in the event of a transfer of consumer credit regulation relating to how the overall level of consumer protection might best be retained or enhanced.	We believe that the requirement of the 7 day cooling off period for secured lending against property should be removed from the CCA requirements when combining the two regimes. This will allow borrowers to access funds for traditional bridging finance.

	The introduction of the 7 day cooling off period to loans currently under the FSA regime would seriously affect the operation and destroy the viability of the short term finance industry and have a significant negative impact on consumers. We at the astl would urge the CPMA to rely more on the current MCOB regulatory regime than the highly complex, confusing and costly CCA regime.
8. The Government would welcome further evidence relating to: • the use of consumer credit by small and medium sized enterprises (SMEs); • whether the protections currently afforded by the CCA are appropriate and cover the right groups of businesses; and • the costs and benefits of considering extending FSMA-style conduct of business rules to a wider group of SMEs.	Generally short term lenders avoid loans of less than £25,000 to businesses due to the complexity and cost of providing CCA regulated loans. This can cause a negative consequence for SME's who require a further advance. They may have to borrow over £25,000 to get it as the lender will not offer CCA loans. Even if they are willing to borrower the higher amount it may not be available to them due to lack of sufficient equity to secure the higher amount. This is to the detriment of the consumer. There does not appear to be any logic in applying protection to loans for business purposes based only the size of the loan or further advance being below the £25,000 limit.
9. The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.	More short term lenders would be willing to offer secured loans that currently fall under CCA regulations if they were under MCOB based rules. There would be more competition which should lead to more choice and hence better outcomes for consumers. Dually regulated firms could achieve significant cost savings by operating only one process.
10. The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.	Astl believes that FSMA style supervision should enhance the current CCA regime leading to greater consumer protection. The OFT is not perceived as an active regulator.

11. The Government welcomes views on the synergies afforded by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.	No comment on this matter.
12. Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the objectives (as outlined in paragraph 1.18 of Chapter 1)?	Yes
13. Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?	No comment
14. Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?	No comment
15. If you do not agree with the preferred option 1, do you have views on the factors set out in paragraph 2.4 that the Government should consider in determining the most appropriate regulatory authority for the CCA regime under option 2?	N/A
16. The Government welcomes views on the suitability of the provisions of a FSMA-style regime, such as those referred to in paragraph 3.6, to different categories of consumer credit business.	There is logic in requiring all firms offering secured loans to meet the same standards and comply with the same rules of business. Unsecured lending may require some additional checks and balances given the often vulnerable nature of the borrowers but this should be able to be built into the new regulations.
17. Do you agree that statutory processes relating to CPMA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?	Yes

18. The Government welcomes views on key factors that would need to be assessed in considering fee arrangements for consumer credit firms.	No comment
19. The Government welcomes: evidence relating to experiences of the current appointed representatives regime; views on how an appointed representatives model might be applied to different categories of consumer credit activities, including how current business models and networks might lend themselves to such an approach; and evidence relating to the implications an appointed representatives regime might have for firms and consumers.	No comment
20. The Government welcomes: evidence relating to experiences of the current group licensing regime; and views on how the professional bodies regime might be adapted for different categories of consumer credit activities.	No comment
21. The Government welcomes views on the extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises.	These could be incorporated into the Treating Customers Fairly requirements.
22. Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.	No comment
23. Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approach?	No comment
24. The Government welcomes views on how the treatment of agreements already in existence could be approached.	Short term lenders would find this aspect relatively easy to cope with given that agreements are for less than 12 months and could be run off of the books in existing format. Astl sees the benefit of one regime being only having to run one system and logically, therefore, loans should be transferred. Running two systems side by

	side for a lengthy period would not be beneficial. The key is to ensure consumers do not lose any of their rights, but repealing of the regulations could reduce administrative burdens. Astl believes a 3 year transitional period should be long enough for firms to complete transfers with an option for any firm not wishing to transfer or meet the new CPMA requirements to continue to run off their book but not write new business.
25. The Government welcomes views on: • how existing licensees could be dealt with; and • factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms.	Astl would be mainly concerned with the treatment of secured lenders. Given that they lend against homes already they will need to fall into the Home Finance Providers category. There are also a considerable number of lending firms who do not have a CCA licence who transact secured loans currently exempt from the CCA as they are for high net worth or predominantly business purposes. These firms will also need to be regulated to achieve a level playing field. Those with current FSA permissions in this area should not be required to change their permissions to offer second charge loans. Those who only have CCA licensing will need to prove they meet the standards applied for Home Finance Providers so must apply. In gaining authorisation there should be nothing to stop them offering first charge as well as second charge lending. It is hard to see how firms could be fast tracked in without some risk occurring. One key issue that the CPMA should give consideration to is relaxing the current FSA requirement on Home Finance Provider applicants to demonstrate that they have experience at governing body level of running an MCOB regulated company.

	It seems it will be impossible for many firms to demonstrate this and the costs associated with recruiting suitable people, and the shortage of supply, could force many firms out of business.
26. The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.	No comment
27. Are there other factors the Government should take account of in considering transitional arrangements?	No comment
28. The Government would welcome evidence on the experience of firms, consumers and their representatives in relation to similar previous transitions, for example the extension of FSA jurisdiction to new markets since 2000.	No comment

Law Reform Committee

Response of the Law Reform Committee to BIS Consultation on Reforming the Consumer Credit Regime

The Law Reform Committee of the Bar Council of England and Wales welcomes the opportunity to comment on the above consultation paper. We recognise that the departmental reorganisation which is taking place provides an opportunity to consider whether simplification and consolidation may be possible as part of the exercise. Clearly there are significant difficulties with the way in which consumer credit is regulated and any attempt to grapple with these difficulties is welcome. However, a key thrust of our response reflects a concern that there may not have been sufficient consideration given to the external constraints which we consider will materially restrict the opportunity for successful reform. We expand on these views in response to the specific questions set out below.

Chapter 1

1. **Do you agree with this assessment of the consumer credit market?**

There are plainly aspects of consumer credit regulation which are, to use the language of the consultation document, "sub-optimal". Not the least of these is the complexity of the regime. That complexity arises, in part, because there have been three substantial reforms of the regime within the last six years.

The consultation document refers to two of these reforms, namely the Consumer Credit Act 2006 and the Consumer Credit Directive ("CCD"), the other being the substantial reforms which came into force in 2005[1]. Each of these changes has required considerable work by businesses in terms of regulatory compliance. Borrowers and advisers (including CABx and trading standards officers) have had to become familiar with new, and often complex, provisions on each occasion. Against that background, it is not easy to sustain an argument that further change, at least in the short term, is desirable.

It is not clear to us that the proposed reform will be able to address the consumer credit regime in a helpful fashion. The principal obstacle is the CCD, which is a maximum

[1] The Consumer Credit (Agreements) (Amendment) Regulations 2004, the Consumer Credit (Disclosure of Information) Regulations 2004 and the Consumer Credit (Advertisements) Regulations 2004.

harmonisation Directive. Accordingly the key obligations, which are now part of UK law as of 1 February 2011, cannot be expressed other than as a copy-out of the CCD. Similarly, they cannot be the subject of any de-regulation. Accordingly we do not see how this proposal will improve either clarity or de-regulation.

2. Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail financial services?

There is a duplication of regulatory regimes in some cases. The example of payment protection insurance is a case in point. However, consumer credit is an area where experience is key. It became apparent to many interested parties that the recent transposition of the CCD into UK law was handled by a department with relatively little experience of the current regime, and many difficulties arose as a result[2]. In our view it is rather more important that the regulator is expressing a knowledgeable viewpoint than it is to ensure that there is a single coherent voice.

We anticipate that many businesses would also take the view that there will be a duplication of regulation regardless of these proposed reforms. If the split between the FSA and OFT is removed, businesses will still face potential inconsistent regulatory views from the Financial Ombudsman Service and trading standards services.

3. The Government would welcome further evidence relating to the consumer credit regime, including in particular:
the types of risks faced by consumers in consumer credit markets;
key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers; and
the incidence of regulatory duplications or burdens on firms and/or inconsistent regulation of similar types of business.

The Law Reform Committee is not in a position to comment on these issues.

4. Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?

We express above our doubts as to whether simplification and deregulation are attainable objectives. The CCD also restricts the extent to which there could be any improvement in the coherence of the FSMA and CCA regimes. As for responsiveness, if the area in which a response is required is within the ambit of the CCD, the proposed reform will have no effect – change will only be possible if there is an amendment to the CCD.

[2] For example, the need to completely replace the Consumer Credit (Advertisements) Regulations 2010 before they came into force due to errors in the original Regulations.

Chapter 2

5. The Government welcomes views on the impact a unified regulatory regime for retail financial services may have in terms of clarity, coherence and improved market oversight.

We set out above our doubts that the objectives of clarity and coherence are realistic given the nature of the area. As to the last aspect, we are not aware of any significant problems arising in the consumer credit market which could be said to stem from any lack of market oversight. In the example used by the consultation document in another context, namely PPI mis-selling, it is notable that the problem arose despite the presence of FSA regulation under the ICOB/ICOBS Rules. Indeed, the recent challenge brought by the British Bankers Association to the FSA's final determination on this issue suggests that this type of regulation is no more likely to achieve either the high standard of consumer protection which is desired or the coherence and clarity of regulation which is sought by business.

6. The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.

It is our experience that consumer credit expertise is thinly spread amongst trading standards departments. Some officers have an excellent depth of knowledge and understanding of the area, others would cross the road to avoid it. It would not be likely to improve the level of expertise amongst trading standards officers for there to be any further substantial change to the regime, if such were possible in light of the CCD.

The technical aspects of the regime are less of an issue for the regional Illegal Money Lending Units ("IMLUs"), who typically deal only with the relatively simple CCA provisions relating to unlicensed trading. Their work is likely to be largely unaffected by the proposed changes. However, it is worthwhile noting that in work of this type, a regional presence, rather than a single central regulator, is important. This work involves gaining the trust of victims and co-operation from local police officers, which is far more likely to be achievable if it is addressed at a local level. The recent abolition of regional IMLUs in favour of a single IMLU for the whole of England is therefore likely to be a retrograde step.

7. The Government welcomes views on factors the Government or the CPMA may wish to consider in the event of a transfer of consumer credit regulation relating to how the overall level of consumer protection might best be retained or enhanced.

The factor of greatest significance is the CCD. We are concerned that there may not have been sufficiently detailed consideration given to the extent to which this will limit the scope for reform. The most significant consumer protection measures are now enshrined in the CCD and cannot be affected by the proposed reform. These include the provision of adequate explanations, pre-contract information in the form of the Standard European Consumer Credit Information ("SECCI") document, the form of the regulated agreement, the right to withdraw within 14 days and so on.

We do not at present see how these provisions would fit into the type of regime currently operated by the FSA. For example, a cornerstone of the FSA's mode of regulation is the obligation to "treat customers fairly" ("TCF"). If a similar requirement were to be imposed across the board in areas covered by the CCD, it would run the risk of infringing maximum harmonisation by gold-plating the CCD requirements.

There are, of course, areas outside the scope of maximum harmonisation, such as licensing. This may be an area where there would be benefits from combining the consumer credit licensing regime with the FSA's authorisation system. However, there would plainly be issues with converting the many thousands of holders of consumer credit licences into authorised persons under the FSA. The latter is a more onerous process and the requirement to go through it might lead to a reduction in competition, particularly from smaller lenders.

8. The Government would welcome further evidence relating to:

the use of consumer credit by small and medium sized enterprises (SMEs);
whether the protections currently afforded by the CCA are appropriate and cover the right groups of businesses; and
the costs and benefits of considering extending FSMA-style conduct of business rules to a wider group of SMEs.

Any extension of the protections afforded to SMEs should be very carefully considered. The CCA provisions in relation to business lending were introduced by the 2006 reforms, so the position has been considered recently. We are not aware of any substantial need to reconsider this area. It would not seem to us to be advisable to increase the regulatory burden on lenders who lend to SMEs in the current economic climate.

9. The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.

As we set out above, we remain to be convinced that there will be any material increase in flexibility as a result of the proposed reform. However, we can comment that in our view clarity is of greater importance than flexibility for all parties in this area, using the example set out below.

The Consumer Credit Act 2006 introduced a new provision into the regime, namely that of "unfair relationships" (sections 140A to D of the CCA). This introduced a flexible remedy enabling the Court to address any "unfairness" in the relationship between borrower and lender. There is no statutory definition of unfairness, nor is there any restriction of the matters which may be relevant to unfairness. Once a borrower asserts unfairness, with a sufficient evidential basis to properly raise the issue, the burden of disproving the allegation falls on the lender.

The very flexibility of this remedy creates its own problems. Borrowers (or their advisers) quite properly feel able to assert that an agreement is unfair for a plethora of reasons. Lenders are obliged to contest such allegations, regardless of the value of the claim, since an adverse finding would be frowned upon by the OFT, and because of the risk of copycat claims. There is little authority on the application of the test, and that which there is strongly suggests that it will be a matter for the judge at first instance to balance the competing factors and reach a conclusion, which an appellate court will be reluctant to interfere with[3]. Accordingly this flexibility risks generating litigation, often over trivial sums of money.

10. The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.

We express our doubts about the workability of the FSMA approach in the response to question 7 above. We are not aware that difficulties have arisen in the consumer credit sector because of the way in which the OFT supervises the area. It may be that the FSMA approach could enable a speedier response to poor behaviour by businesses than the OFT's "minded to revoke" procedure, but the recent changes to the CCA in this regard (such as the power to impose requirements on consumer credit licensees) have given the OFT greater flexibility.

11. The Government welcomes views on the synergies afforded by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.

The CCA regime allows the OFT to have oversight of all aspects of a consumer credit business. Grounds for refusing or revoking a licence include a conviction for any regulatory offence, not simply those relating to the provision of credit, offences of violence or fraud, discriminatory practices and any other business practice which the OFT considers to be deceitful or oppressive or otherwise unfair or improper. We are aware of many cases of licensing action which arise solely (or at least principally) because, for example, the OFT disapproves of the selling methods used by a trader.

This is an important protection, since it adds a further layer of consumer protection to that which is already provided by provisions such as the Consumer Protection from Unfair Trading Regulations 2008 and the Enterprise Act 2002. A business may be prepared to accept the risk of a conviction in the magistrates' court but is unlikely to be sanguine about the prospect of losing its ability to engage in lending or credit brokerage activity as a result of that conviction. Accordingly in our view this additional layer of protection is desirable and should be retained.

12. Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the Government's objectives (as outlined in paragraph 1.18 of Chapter 1)?

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[3] *Harrison v. Black Horse Limited* [2010] EWHC 3152 (QB).

13. Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?

14. Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?

15. If you do not agree with the Government‟s preferred option 1, do you have views on the factors set out in paragraph 2.4 that the Government should consider in determining the most appropriate regulatory authority for the CCA regime under option 2?

These four questions all address the same fundamental point – is it desirable to remove CCA regulation from the OFT and seek to combine it with FSA regulation of financial services? On the evidence put forward, we do not consider that a case is made for such a reform, principally for the reasons already set out. We do not see the case made for substantial reform of the area in light of the constraints imposed by the CCD

Chapter 3

16. The Government welcomes views on the suitability of the provisions of a FSMA-style regime, such as those referred to in paragraph 3.6, to different categories of consumer credit business.

There are a wide variety of persons who are required to be licensed under the CCA. These range from prime banks to debt purchasers and from major credit brokers to small car dealerships. The CCA 2006 also introduced new categories of licence, include “debt administration”, to cover those who carry out functions on behalf of regulated lenders. It is not clear to us how an FSMA-style regime could be adapted to take account of these diverse categories of business without imposing very significant regulatory burdens.

17. Do you agree that statutory processes relating to CPMA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?

18. The Government welcomes views on key factors that would need to be assessed in considering fee arrangements for consumer credit firms.

It is clear from our response to question 16 that we do not consider that a one-size fits all approach could be taken to supervision and authorisation costs. We note that the FSA fees regime is intended to operate so that it is self-financing – hence the reference to subsidy in paragraph 3.27. The OFT licensing regime is not, so far as we are aware, subject to such a requirement. It will plainly be vital to consider the extent to which high costs may be a barrier to entry into the market for smaller businesses if a similar approach were to be taken.

19. The Government welcomes: evidence relating to experiences of the current appointed representatives regime; views on how an appointed representatives model might be applied to different categories of consumer credit activities, including how current business models and networks might lend themselves to such an approach; and evidence relating to the implications an appointed representatives regime might have for firms and consumers.

20. The Government welcomes: evidence relating to experiences of the current group licensing regime; and views on how the professional bodies regime might be adapted for different categories of consumer credit activities.

21. The Government welcomes views on the extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises.

The Law Reform Committee is not in a position to comment on these issues.

22. Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.

We are not aware that the current level of regulation of consumer credit businesses is a cause for concern. Given that the ambit of regulation was considered when the 2006 reforms were put in place, we do not consider that there is any pressing need for further consideration of this area.

23. Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approach?

Chapter 4

24. The Government welcomes views on how the treatment of agreements already in existence could be approached.

We refer in our response to question 1 above to the fact that there have been three different reforms in the recent past. This has led to situations where the application of transitional provisions has proved difficult. These problems would be multiplied if a different overall regulator were to be involved with agreements made prior to any reform. Accordingly there is much to be said in favour of a single regime.

However, the devil is likely to be in the detail. We cannot at present comment on the likely difficulties of trying to fit existing agreements into a new regime, other than to comment that it is not something which has been attempted in the context of the three previous reforms already adverted to. That may itself provide some evidence of the scale of such a task.

25. The Government welcomes views on:

how existing licensees could be dealt with; and
factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms.

As a matter of common sense it would seem appropriate to reduce the rigour of the approach required for any business which previously held a consumer credit licence and which seeks to become an authorised person, since it will already have had a degree of regulatory oversight. However, we cannot comment on the detail of any proposed approach.

26. The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.

27. Are there other factors the Government should take account of in considering transitional arrangements?

28. The Government would welcome evidence on the experience of firms, consumers and their representatives in relation to similar previous transitions, for example the extension of FSA jurisdiction to new markets since 2000.

The Law Reform Committee is not in a position to comment on these issues.

IAIN MACDONALD
For and on behalf of the Law Reform Committee
16 March 2011

Billing Finance Limited

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VAT REGISTRATION NO. 443 7876 16 Consumer Credit Licence No. 565740

Financial Regulation Strategy
HM Treasury
1 Horse Guards Parade
London
SW1A 2HQ **16 March 2011**

To whom it may concern,

Consultation response from Billing Finance Ltd on "a new approach to financial regulation: consultation on reforming the consumer credit regime".

Billing Finance Ltd is pleased to submit a response to the recent consultation on "a new approach to financial regulation: consultation on reforming the consumer credit regime." We understand and are concerned that the Governments preferred option is Option 1 which is based on the Financial Services & Markets Act [FSMA] 2000, that could see all companies involved in the credit industry, large and small, operating under FSA styled 'rule' based regulation. Consumer credit has undergone root and branch changes over the last 35 years culminating in the latest piece of regulation, the Consumer Credit Directive implemented in February of this year. We believe that the current regulator of consumer credit, the Office of Fair Trading [OFT] has been provided with the appropriate tools of regulation and enforcement which means that they have more than adequate means of controlling the market, in a proportionate and appropriate way whilst taking action against any 'rogue traders' within the market. The consultation paper proposes the transfer of the OFT to operate under the Financial Conduct Authority, alongside the FSA. We fail to see why a successful model for regulating consumer credit is potentially once again facing further major change thereby creating concerns for the Industry and consumer alike.

The consultation paper goes much further than the transfer, as it proposes to apply to the consumer credit market the FSA's current approach in the retail deposit market. Without a more proportionate approach this is unlikely to work, because of the fundamental difference between credit [where the risk lies with the lender] and banking/saving [where the main risk lies with the depositor]. Needless to say, compliance costs will increase significantly, and supervision will intervene far more under the new regulator.

We do not feel that the consultation document, or the impact assessment, presents any compelling evidence to move to a FSMA style regime for businesses currently wholly regulated by the OFT, especially those that are considered to be SMEs. We feel that many unintended consequences could arise as a result of the change. Increased costs and regulation could force some smaller organisations, or sole traders to exit the market.

The provision of consumer credit has risen considerably in recent decades and enabled consumers to access products and services to suit their lifestyles. As a direct result of the negative impact of 'credit crunch', bank funding to the SME sector in particular has been severely curtailed, resulting in a significant downturn in lending. Consumer credit has hugely contributed to the positive growth of the UK economy over the last twenty years, within a highly competitive and innovative market. The cessation of many credit products is currently stifling growth, and further regulation, or even uncertainty about regulation going forward will stifle much needed growth even more.

Used wisely, consumer credit also helps consumers to smooth the peaks and troughs in income and expenditure, and allows consumers to manage their finances in a way that suits them.

Our business falls into the "small to medium sized enterprise" [SME] category. We have been trading for around 35 years and employ 22 staff. 95% of our business is car finance through CCD regulated hire purchase agreements. We lend approximately £10m a year.

Statistics published by Business Innovation & Skills [BIS] in October 2010 (http://.stats.bis.gov.uk) show that the SMEs together accounted for 99.9% of all enterprises, 59.8% of private sector employment and 49.0% of private sector turnover. Both the number of companies and the number of sole proprietorships rose, the former for the 11th successive year, the latter for the seventh successive year. Small enterprises alone, with 1 to 49 employees, accounted for 48.2% of employment and 37.5% of turnover. Addressing the consumer credit SMEs, paragraph 3.1 of the consultation paper suggests that just over one-third of OFT licensed firms are sole traders.

The proposed new regime will be the most radical change in consumer credit regulation for a generation. We believe that the massive changes that consumer credit has gone through in 1974, 2006 and recently with the implementation of the Consumer Credit Directive should not be changed again to fit FSMA 2000. Moreover, we believe that it would create havoc in the consumer credit market, to effect a change from regulation which provides for clear legal certainty to a, principles and rules based approach such as the FSA.

The standards expected by firms in the framework of the UK regulatory regime for consumer credit are some of the highest in Europe and the burden on SMEs in ensuring compliance is a large one. Banks, building societies and large finance houses have larger staffing levels and financial resources to cope with more onerous regulation for deposit takers where the risks are greater. For the SMEs simply keeping up with the required changes is expensive, as detailed regulations can be supplanted by guidance notes and additional actions are required when dealing with other Government agencies.

The changes currently outlined within the consultation paper, would be the most complicated and costly change for all parties. Large numbers of small businesses could be expected to leave the market [over 33% of current credit licensees are sole traders]. Many other lenders would in all probability withdraw from at least part of their current markets. In consequence, the UK's consumer credit markets would shrink considerably, credit availability would be restricted, and market competition significantly reduced. There would be an increase in the costs of borrowing as companies would have to pass on the higher cost of regulation under the new regime. The effects would almost certainly exceed those of the recent credit crunch, where availability and choice of products reduced dramatically. The low-income borrowers in particular would be most affected, with the real danger of financial exclusion becoming far greater.

As you are no doubt aware around 40% of all consumer lending is currently done by companies which are not banks. Within the body of the consultation paper is the proposal that capital adequacy requirements would be imposed on all lenders, which would impact on organisations that do not take, or use deposits to fund lending. Similarly, much of the current consumer market lending is dependent on intermediaries. Making lenders responsible for the regulatory compliance of intermediaries would have a serious adverse effect on markets such as motor finance.

Our main areas of concern are:

- further unwarranted changes to consumer credit regulation
- the extension of the new regime to small business lending
- a requirement for all existing lenders to re-apply for authorisation for both existing and past business
- significantly higher regulatory fees
- the loss of the certainty of the legal position on loan agreements
- further disruption to business during the handover and changes
- lack of experience on consumer credit in the new Authority
- potential loss of Trading Standards Authority experience

Consumer protection within consumer credit has been strengthened over the years and with the implementation of European Consumer Credit Directive, and the move towards maximum harmonisation consumers are even more protected. The level of complaints dealt with by the regulator, or the Financial Ombudsman Service [FOS] are minute in comparison to number of loan agreements written. Companies are concerned about their reputation, and treat consumers with respect and dignity. The risk lies with the lender not the consumer, as no deposits are taken by the lenders outside of the banks, large finance houses and building societies. We believe that there is no compelling reason to move towards monitoring and reporting as consumers are already well protected.

The Coalition Government are continually stating their declared policy that enterprise and the SMEs are pivotal in the UK economy avoiding the real danger of a double dip recession. The Prime Minister has also stated that bureaucracy and regulatory red tape are the enemies of enterprise and that unnecessary regulation should be avoided at all costs. We believe that the changes that consumer credit has gone through in 1974, 2006 and now the implementation of the Consumer Credit Directive in February 2010 should not be changed yet again to fit FSMA 2000. Moreover, we believe that it would create havoc in the consumer credit market to change from regulation giving clear legal certainty to a, principles and rules based approach.

We believe therefore that Option 2 is the best option and that consumer credit should remain under the current regulatory framework and body, preferably an OFT style that would allow the market to retain the legal certainty of the current regulation with appropriate and proportionate enforcement.

Yours faithfully,

Oliver Mackaness
Director
Billing Finance Ltd

Birmingham City Council

REGULATORY SERVICES

Date: 17th March 2011

Ref: JK/LLJ/022ACO

Edward Davey MP, Minister for Employment Relations, Consumer and Postal Affairs
Mark Hoban, Financial Secretary to the Treasury
House of Commons
London
SW1A 0AA

Dear Ministers,

Re: BIS funded Illegal Money Lending Teams
Consumer Credit Reform and the Consumer Protection and Markets Agency

As you are aware the Consumer Credit Act and the role of the Office of Fair Trading is currently subject to consultation and review in respect of the future landscape. As a result, there is potential for the Consumer Credit Act to be repealed and with this the enabling powers of the illegal money lending teams.

I know you are aware of the value the teams have delivered and the way they are now established and recognised for tackling illegal lenders that have a disproportionate impact on the welfare and economy of local communities. It is recognised that these teams now serve some of the most hard to reach communities and individuals and deliver a proportionate approach to tackling this dreadful crime

My concern for the future is in respect of the consultation and the future of tackling illegal lenders. By repealing the Consumer Credit Act and replacing it with a FSMA compliance regime the illegal lenders may revert to a risk free occupation. I accept that the intention is to simplify and coordinate the modus operandi of the credit industry however, I am unsure as to whether full consideration has been given to the impact of removing certain aspects of the legislation, such as the unlicensed trading offence, would have in respect of tackling illegal lenders. Further, this may be an opportunity to make provision to strengthen the legislative framework for the investigation and institution of proceedings against "Loan sharks".

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I was hoping that we may be able to meet with yourselves and officials to discuss this matter further in order to identify a possible solution and discuss the implications some of the suggested proposals may have on the illegal money lending project.

I am also worried that the illegal money lending team's skillset, operating model and specialist expertise may not be easily replicated within a national regulatory authority.

I know that you have indicated your support for the project and hope that you can find time to consider this matter with us so that we can continue to deliver an effective and efficient project on behalf of the Government.

Yours sincerely

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The voice of banking
& financial services

BBA response to HM Treasury

A new approach to financial regulation: Consultation on reforming the consumer credit regime

1. The BBA welcomes the opportunity to respond to the consultation on the reforming the consumer credit regime. The British Bankers' Association (BBA) is the leading association for the UK banking and financial services sector, speaking for 223 banking members from 60 countries on the full range of UK or international banking issues and engaging with 37 associated professional firms. Collectively providing the full range of services, our member banks make up the world's largest international banking centre, operating some 150 million accounts and contributing £30bn to the economy.

2. Our response addresses each of the consultation questions in light of their relevance to, and our members' experiences of, retail banking. Our focus is therefore on these issues as they relate to current account overdrafts, unsecured loans, credit cards and charge cards. We do though appreciate that the scope of consumer credit stretches far wider and where appropriate we provide comment with regard to the wider credit market.

General remarks

3. The government acknowledges that the UK consumer credit market is one of the largest and most diverse in the world. This demonstrates the benefits of the current regime in terms of competition and ability to enter the market and to innovate for UK and foreign participants. In making the case for reform, the consultation focuses on the perceived limitations of the current regulatory regime, rather than its advantages, such as those which allow a wide and diverse range of consumer credit products to be used by two thirds of all households, where size in terms of resources and number of employees is no barrier to entry into the market.

4. As explored further in our response, it is important that the government gives careful consideration to the potential detriments that could result for the market and for consumers in making fundamental changes to the current regime. The consultation paper makes clear that the government has a preferred option (Option 1), but it is less forthcoming in considering alternatives. Although a second option is outlined it is subject to little analysis and simply maintains the current regime under an as yet unconfirmed regulatory authority.

5. It is noteworthy that the perceived weaknesses of the current regime listed at paragraph 1.17 of the consultation do not include any deficiencies in the standards of consumer protection that customers enjoy at present. Instead, the government, in our view rightly, focuses on the weaknesses in the framework of regulation for financial services. This suggests that consumer credit regulation is not of itself deficient, but that the framework in which it operates could be improved.

6. The BBA believes that instead of the two options included in this consultation, an alternative option is possible which would allow the current and effective credit regulations to continue, but within a unified and rationalised regulatory framework, using elements of each of the options identified by the government. This hybrid model would allow the government to meet its ambitious timetable for change in a structured, logical and cost-effective manner, whilst retaining the successful aspects of the current regime which have allowed the UK to develop a large and diverse market for consumer credit.

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The BBA's preferred approach

7. The BBA believes that a new regulatory regime that meets the government's four key objectives can be created without fundamental changes that might weaken the benefits of the existing regime. Indeed, we think it would be remiss of government to countenance further fundamental changes to consumer credit regulations before the newest credit regulations have fully embedded and their impacts, on consumers and creditors, are known and fully understood.

8. Instead, the BBA supports a change to the current regulatory regime to bring existing credit regulation (rationalised where appropriate) under the auspices of a single retail financial services regulator i.e. the Financial Conduct Authority (FCA).

9. Bearing in mind that the Consumer Credit Act (CCA) and associated regulations transpose the Consumer Credit Directive (CCD), its transposition into a new rule book, as advocated by the government, would prove a difficult and monumental task. We therefore believe there is considerable merit in preserving the existing substantive conduct of business provisions of the CCA (e.g. Parts II, IV, V, VA, VI, VII, VII and X) and its accompanying regulations. An amended FSMA, to create the FCA, could then include new enabling provisions allowing those CCA conduct of business provisions to be 'maintained' by means of Statutory Instruments (SI) that could where necessary (and where permitted by the constraining influence of the CCD) be expanded upon through regulatory guidance. Other relevant parts of the CCA , amended as necessary to fit with the new regime, could then be dealt with in a similar manner or where appropriate as new FSMA provisions.

10. A similar approach was used to implement the EU Payment Services Directive as the Payment Services Regulations 2009 into FSMA via SI, giving the FSA the status of a recognised authority for regulation of the legislation.

11. The advantages of adopting this approach for consumer credit are manifold. For the new regulator it would avoid the difficult task and risks of producing a new rule book that is compliant with the CCD. The stumbling block to successful implementation of the new regulatory regime is likely to be reaching agreement on any new rule book. Moving from the current CCA conduct of business requirements to a completely new rule book could prove additionally contentious if a rule book style of regulation results in narrowing how the CCD should be interpreted. Lenders have built their systems and devised processes to be compliant with the CCA and to be faced with a different approach in order to comply with a new rule book would be challenging and costly and would certainly require considerable implementation to make systems/processes changes.

12. There is not an appetite amongst our members to embark on a further expensive implementation project following three sets of major CCA changes which have taken place since 1985. The cost effectiveness of introducing a completely new rule book should therefore be measured against this background.

13. For the credit industry our preferred approach would allow existing consumer credit (the 'back book') to continue on its current terms and would avoid the massive costs associated with creating a new compliance function for new credit in tandem with the existing regulatory framework for the back book.

14. For consumers, our proposed approach would address all of the perceived weaknesses and resulting confusions, identified in the consultation paper, whilst maintaining the consistency of current standards and protections within a more proactive and intrusive regulator, the FCA.

15. The BBA's suggested approach also avoids exposing consumer credit to the potential risks of a 'FSMA-style' rulebook, where Principles-based regulation does not give consumers or providers the certainty they require and creates the risk of retrospective regulation through hindsight, which is neither fair nor predictive for the industry.

16. Transferring the current legislative approach across to the single regulator, via an SI and regulatory guidance as needed, would allow the government to achieve an orderly transition within its timetable and would allow for a possible two-stage approach, should there be an appetite after 2014 for a more fundamental re-examination of the standards established by the CCA, subject of course to continuing compliance with the maximum harmonisation Directive.
17. As the government acknowledges, a new approach to credit regulation must consider the scope and purpose of credit licence arrangements and the appropriate forms of supervision and enforcement of a new regime. BBA's preferred approach would be to reduce the number of entities and activities requiring a licence (or authorisation) by aligning the new regime's requirements for authorisation with those of the CCD. This would allow the government to take debt management and debt collection firms out of the equation, with regulatory responsibility being passed to a more appropriate debt regulator such as the insolvency service. Other currently licensed activities beyond what is required by the CCD, such as hire, would also need to be authorised elsewhere.
18. In terms of supervision of consumer credit activities, the BBA believes that the regulator should apply its focus and resources to customer risk, rather than to systemic risk – which of itself has little bearing in unsecured consumer lending. This focus would direct resources to those areas of the credit landscape which pose the highest risk to customers e.g. high cost lending and point of sale credit. This will mean that the regulator's focus is more likely to be on smaller, less mainstream providers, but would not of course mean that mainstream lenders are ignored.
19. Regulatory reporting should apply across the industry and business models should also be subject to appropriate rigour. Determining where on the customer risk curve each provider would sit could be achieved by categorising businesses based on the types of credit offered; volumes provided and even customer segmentation. More regulatory activity may require to be directed to the high risk lenders which generally have a different profile than high risk firms under the current FSA regime. Some firms that are categorised as medium to high risk for current FSA regulatory activity e.g. BBA members are likely to be low risk for consumer credit.
20. It is important that regulation of consumer credit is achieved on the basis that the same regime will fit all firms regardless of size and resources available. A change in regulatory regime should not act as a driver for forcing reputable small firms out of the business simply because licensing is too costly and/or compliance becomes unmanageable and/or presents too great a risk. Any change from current supervision model used by OFT to a more proactive and intrusive model will involve greatly increased cost.
21. Estimates of costs of varying levels of increased supervision between the current OFT approach and current FSA approach could be modelled to establish an optimum level of supervision that is both effective and proportionate but also affordable for the smaller firms who play an important role in the provision of consumer credit.
22. The government's Impact Assessment makes ample use of the phrase 'costs unquantifiable at this stage' but it is paramount that no decisions are taken on the future of regulation in this sector without first knowing what the ballpark costs per firm are likely to be.

Chapter 1

1. Do you agree with this assessment of the consumer credit market?

23. The government acknowledges that consumer credit is vital to the UK economy. For the overwhelming majority of people, credit is a convenient and straightforward financial service that can be accessed when needed, in a form that suits its intended purpose and in a way that suits the consumer. Over thirty years of legislative instruction informs the way that credit is bought and sold and a myriad of protections govern the ways in which debts can and cannot be collected should the consumer experience difficulty.
24. As outlined earlier in our response, in assessing the consumer credit market the government focuses attention on the regulatory framework and its perceived weaknesses and does not identify any inherent problems with the rules which govern credit or the products and services

available. We agree with some elements of the government's assessment of the market, but in places we do not recognise the same degree of limitations and problems that the consultation outlines. These are explored further below.

2. Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail financial services?

Accountability for some objectives relating to retail financial services is split -

25. The BBA agrees that no one organisation is ultimately accountable for all aspects of consumer credit regulation against a set of clear statutory objectives. This does create duplication of regulation and of resources for our members. It may have created confusion amongst consumers as to who has responsibility in certain areas, such as current account overdrafts, but advice and information is readily available to consumers and we don't believe that they have suffered any material detriment under the existing regime.

26. We believe that a single accountable regulator with responsibility for financial services would be beneficial for our members in terms of consistency, certainty and costs. All benefits that could ultimately benefit the customer. However, we recognise that our members start from a different position than the majority of current credit licence holders in that they are, for the most part, already regulated by the FSA for most of their UK business.

Lack of coherence in consumer protection and market oversight

27. We recognise the examples given in this section of the paper, but note that they are not fundamental failings, but rather inconveniences of the current regime which demonstrate a less than optimum approach.

28. It is clear however that the different roles and approaches of the FSA, OFT and Lending Code/LSB can have their advantages. The Lending Code is not encumbered by legislative or statutory protocol and can therefore act dynamically to address emerging issues. The OFT uses its licence powers as a useful tool of deterrence amongst a community of around 100,000 active participants, for whom a more intrusive form of supervision would not be possible. The FSA has for secured credit been able to look across the market to see where consumer and systemic risks may occur.

29. It is important therefore when considering a new approach that we do not lose the benefits of the current approach where they exist.

Confusion and duplication

Where the current regimes create an issue, as acknowledged in paragraph 25 of our response, a single regulator might improve the position. However, where there is more than one regulated activity in relation to a product, for instance credit sold with insurance or insurance purchased using credit, it may be that internal division of regulation within the single regulator will continue to perpetuate any issues unless there is sufficient internal oversight to prevent conflicts arising.

Too reactive and insufficiently flexible

30. Although in isolation the CCA can be seen as inflexible and OFT regulation reactive, the government highlights these as perceived weaknesses without acknowledging that OFT regulation is cost effective as available resources are concentrated to regulating high risk activities. That is not to say that regulation cannot be improved but the model we are proposing may be a better way of achieving that aim. Those parts of the CCA dealing with licensing and enforcement could be overhauled within a FSMA structure while preserving the existing conduct of business rules.

Deterrent to effective deregulation

31. The BBA agrees that the current legislative framework can be less responsive to coping with changes but as the main driver for further change is likely to be European legislation it is in

relation to those areas of the current regime that are not in scope of European legislation where difficulties will arise.

3. The Government would welcome further evidence relating to the consumer credit regime, including in particular:

- **the types of risks faced by consumers in consumer credit markets;**
- **key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers;**

32. Unlike deposits or investments, the risks related to the capital element of consumer credit lie with the lender i.e. if the firm or the contract fails the consumer does not lose their money. However, consumers can suffer detriment if they borrow or are lent to irresponsibly, if they purchase an inappropriate credit product or if their circumstances change to their financial detriment during the life of the product.

33. Detailed regulatory provisions exist to prevent irresponsible lending. These include the CCA requirements on credit worthiness and fairness, which are reinforced by the OFT Irresponsible Lending Guidance, and self-regulatory requirements on credit assessment and affordability such as the Lending Code.

34. Two key provisions of UK credit legislation (in their current form derived from the CCD) are designed to address the second risk, an inappropriate product. These are: detailed and prescriptive information and disclosure rules to ensure that the features of all regulated credit products are described accurately and in plain language; an appropriateness provision which requires that the purpose of the product is described, including the uses for which the product will not generally be suitable.

35. The greatest risk that consumers face and the most difficult to mitigate is an unforeseen change to the consumer's personal and/or financial circumstances during the life of the credit product, which could make a previously appropriate product, no longer affordable. If this risk materialises it can be compounded by inappropriate collections activity by the lender and/or a third party debt collections agency. However, whilst the change in the consumer's circumstances cannot normally be foreseen or addressed by regulation, there are a number of protections that consumers should and do have against inappropriate treatment when in financial difficulties. These are required under the CCA, within self-regulation such as the Lending Code, and within numerous legislative and regulatory provisions which govern the treatment of debt and debt collection in the UK. These protections extend from how and when consumers can be contacted to pursue collection, the avenues that must be explored and the processes that must be followed to pursue judicial enforcement of a debt, to the actions of bailiffs and insolvency practitioners in enforcing a judicial resolution. It is not clear how a new regulator could materially make an impact on this particular risk that the existing regulator could not make.

36. In addition to the regulatory protections outlined above, consumers also have access to a number of restorative regulatory solutions if a lender fails to comply with legislative or regulatory requirements. For lenders currently subject to statutory regulation under FSMA and/or CCA this includes the consumer's right to referral to FOS where necessary and for all CCA lending the consumer has a statutory right to challenge a credit agreement via the judicial system if he/she believes there has been non-compliance with the CCA or an unfair relationship arising out of the agreement. Importantly, consumers also have the protections provided by Trading Standards and their ability to investigate and address failures associated with the purchase of goods and services using credit.

37. The government consultation is silent on the subject of debt and debt regulation. It is not clear therefore whether the government envisages the FCA being given responsibility in this area. The BBA believes that consideration of the future regulation of consumer credit and the necessary protections that consumers should enjoy must acknowledge the flip-side of lending and borrowing and the need to ensure that the future regulatory regime for credit has a regard to and appropriate relationship with the future regime for dealing with consumer debt.

- **and the incidence of regulatory duplications or burdens on firms and/or inconsistent regulation of similar types of business.**

38. The government acknowledges the current anomalies in regulation where credit may be an element of, or associated with another financial service, such as insurance purchased using credit and current accounts with an overdraft facility being subject to either FSA or OFT regulation depending on the account balance. At a larger scale this obviously plays out in the fact that most BBA retail banking members need to maintain regulatory and supervisory relationships with both the OFT and FSA and are therefore subject to the reporting and supervisory requirements of both and the fees and levies which result.

39. Additionally, BBA members have to maintain a relationship with the Lending Standards Board and ensure compliance with the Lending Code, which fills the conduct of business gap for overdrafts, credit cards and unsecured loans, and they may also have a similar relationship with the Finance and Leasing Association and its FLA Lending Code for point-of-sale credit products.

40. We do not intend to provide detail on the duplications or burdens experienced by firms outside of BBA membership, but do acknowledge that the burdens of current consumer credit regulation can be manifold for those firms who are not lenders in the traditional sense, but still caught by CCA provisions. An example would be a membership body, such as a sports club, which allows its membership to be paid by direct debit instalment.

4. Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?

41. Each of the government's objectives appears sensible and rational, but it is not clear that they can be achieved in unison, to the extent that the government appears to require. For instance, the government seeks to create a single, simple, proportionate and cost effective regime, whilst also requiring a more intrusive, properly resourced and pre-emptive regulator. These could prove contradictory in practice, particularly if a single regulator is expected to meet these objectives for the entire financial services industry including nearly 100,000 current credit licence holders who stretch from retailers and car showrooms to debt management, payday loans and price comparison sites.

42. The government suggests that a new regime may strengthen consumer protections, without identifying where current protections are deficient. The consultation is also silent on the extent to which the maximum harmonisation CCD will allow new regulations and/or deregulation to take place.

43. The BBA believes that the four objectives outlined at paragraph 1.18 of the consultation are only achievable for consumer credit, as it applies to our members, using our suggested approach of transposing the CCA into a Statutory Instrument, made under the Act that creates the FCA. This would provide the FCA as a single regulator for mainstream retail financial services and retain current consumer protections overseen by a more proactive and intrusive regulator (subject to these activities being affordable). Deregulation would be possible when transposing the existing legislation to the new regime and the new regime would remain proportionate and cost effective by avoiding the need to tear up the rule book or for firms to run different back-book and front-book businesses.

Chapter 2.

5. The Government welcomes views on the impact a unified regulatory regime for retail financial services may have in terms of clarity, coherence and improved market oversight.

44. The BBA is supportive of a single unified regulatory authority for retail financial services. However, our support is qualified by the regulatory regime to be employed and the scope of products and services to be included. For retail banking products and services a single regulator would have obvious advantages in overseeing the retail banking market. It should also be able to have a consistent voice and avoid the current risks of duplication or regulatory

arbitrage. Therefore, in isolation, we agree with each of the benefits proposed in paragraph 2.6 of the consultation that a single regulator would bring.

45. The devil is however in the detail of the regime to be employed. As outlined at the outset of this submission, we do not believe that a FSMA-style regime i.e. one with high level rules and guidance under a principles and outcomes based approach is appropriate for consumer credit, where a maximum harmonisation directive already prescribes practices and where over 25 years of detailed legislative framework already establishes minimum business standards.

6. The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.

46. For BBA members, the Lending Standards Board and Lending Code play key roles in providing a dynamic, flexible and transparent regulatory regime for retail banking credit conduct of business. Using the CCA as its framework, the Lending Code is able to provide consumers with minimum standards of best practice to reflect and address new products, channels and practices. Whilst legislation provides the certainty, the Code provides the detail of regulation to address the lender/borrower relationship.

47. The Lending Code is not encumbered by any statutory or legislative processes with regard to addition or amendment. It is therefore able to address new issues and is seen to do so in liaison with key stakeholders such as the government and consumer groups. Independent monitoring and enforcement provides the Code with integrity and the introduction of consumer-facing guides to the Code during 2011 will add to the transparency of the regime and the accountability of subscribers.

48. Trading Standards plays a key role in the current credit regime with regard to the sale of goods and services using credit. It is widely known by consumers and traders and its ability to refer cases to the OFT that may be suitable for licensing intervention acts as an appropriate deterrent to abuse of credit regulation at a local level. The benefits provided by Trading Standards extend beyond simply the credit functions of sellers because the goods and services purchased (and the contracts used to do so) using credit can also be subject to TSO attention. In practice this means that the TSO's responsibilities for credit can be used to ensure that consumers receive appropriate protections with regard to products and services e.g. licensing intervention by the OFT, after referral by the TSO, if the holder is found to be selling goods and services illegally.

7. The Government welcomes views on factors the Government or the CPMA may wish to consider in the event of a transfer of consumer credit regulation relating to how the overall level of consumer protection might best be retained or enhanced.

49. As we have articulated in our opening remarks, the BBA believes that current levels of consumer protection should be retained following any transfer of credit to a single financial services regulator by maintaining the provisions of the CCA within a Statutory Instrument to which the regulator (FCA) is given Recognised Authority.

50. A significant weakness of the government's favoured FSMA-style approach to regulation is that use of high level principles in addition to rules and guidance, results in uncertainty for both consumers and regulated firms. Different interpretations of what is required in order to comply with a high level principle can lead to inconsistency among and within firms and can also result in consumers having expectations above or below what is expected by the regulator. These differences can impact on the integrity of the regulator in the eyes of consumers, firms and commentators and lead to a lack of confidence in the regulated activity.

51. An inevitable consequence of uncertainty as to what is required by the regulator is that interpretations can change over time (by the regulator and by stakeholders) and where clarity is then provided by regulatory action or guidance it can effectively result in retrospective rule making.

52. It is important that the consumer protections currently offered via industry self-regulation are not lost within a new credit regime. As outlined above, self-regulation provides detailed, transparent

and relevant provisions that cover the consumer experience with their lender. Such provisions are not encumbered by EU harmonisation provisions and can normally be enacted without consultative delay. One way this might be achieved under a new regime would be industry guidance – which could where appropriate be given the imprimatur of the regulator (without the risk of super-equivalence).

53. Another important factor that government must consider in the event of a transfer of regulatory responsibility is to ensure that the precedents established through judicial findings, since implementation of the CCA, continue to be regarded as relevant 'case law' for dealing with disputes. It would be unfair and disproportionate if the common law built up over the years is displaced leaving a lack of certainty where previously there had been the certainty provided by judicial precedent.

54. With regard to the wide and disparate nature of services and practices currently captured by consumer credit, the government should consider whether a single financial services regulator is best placed to provide appropriate consumer protection. For instance, Trading Standards is currently focused regionally and has an understanding and appreciation of consumer experience in small, local retailers and lenders. It is not clear that a single London-based regulator will be able to have the same focus and understanding.

8. The Government would welcome further evidence relating to:

- **the use of consumer credit by small and medium sized enterprises (SMEs);**
- **whether the protections currently afforded by the CCA are appropriate and cover the right groups of businesses; and**
- **the costs and benefits of considering extending FSMA-style conduct of business rules to a wider group of SMEs.**

55. The BBA believes that the current scope of regulation for business credit is appropriate and proportionate. We do not believe that any customer detriment exists in the current approach and would support the retention of a £25k limit for the borrowing of small businesses and sole traders.

56. The scope for regulating business lending was debated during the development of the 2006 Act and the transposition of CCD. On neither occasion was it deemed necessary or proportionate to extend regulation to a broader range of borrowing. Indeed, the CCD is not intended to apply to business lending so any transposition of the directive's requirements to business lending within a new regime could amount to gold-plating. This consultation therefore provides the government with an opportunity to consider whether it is appropriate for a future consumer credit regime to apply to any business lending or whether a more appropriate approach might be to create a separate regime to address the risks involved in business lending.

9. The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.

57. The government overlooks an important aspect of the current credit regime in this section of the consultation. The CCD, implemented into UK law in 2010 is a maximum harmonisation directive, meaning that member states cannot fall short of the directive's requirements nor exceed its measures on subjects to which it prescribes. This includes consumer credit advertising; pre-contract information that includes costs; adequate explanation of the features of a product; calculation and presentation of APR and total charges; the requirement to check the creditworthiness of the consumer; rights of withdrawal and terminations and early repayment.

58. The impact and scope of the CCD on a future regulatory regime for consumer credit is an important consideration because it limits the areas in which a new regime, rules-based or not, could have a more flexible approach in setting out what lenders are required to do in key areas of the selling and disclosure process.

59. The inherent flexibility of a FSMA-style regime is both a strength and a weakness. Although it can respond to emerging issues it can also represent a moving feast, where neither firms nor

consumers are certain of the appropriate standards. For firms this uncertainty can manifest in a risk-averse approach and impact on the ability of the business to forward plan with confidence of a stable regulatory landscape. For consumers, this uncertainty may translate into a lack of confidence to participate in financial services where it is perceived that products, practices and processes have changes or are likely to change in the short term.

60. The risk of uncertainty in a FSMA-based regime is exacerbated where the regulator relies on principles and outcomes to measure its expectations. These loose and often subjective measures do not provide firms or customers with certainty or predictability and can result in inconsistent treatment and retrospective judgement.

61. As outlined in the BBA's preferred approach, retention of the CCA's provisions in an S.I. would not restrict the ability of the regulator to work with the industry to improve or create standards to deal with emerging issues. As both the Lending Code and the credit card industry have demonstrated in recent years, there is a real willingness within the financial services industry to make voluntary changes to practices and the protections that consumers enjoy, when evidence, or risk, of detriment emerges.

62. Another important consequence of moving to a new rules-based regime would be the impact this would have on existing credit agreements. There would either have to be a wholesale transfer to new standards or the running of two separate regimes. Both options would be extraordinarily expensive for industry and confusing for customers. Again the BBA approach would avoid this detrimental consequence.

10. The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.

63. The government states that one of the aims of the FCA is to focus on the way in which firms interact with customers and whether customers are treated fairly. As outlined above, the majority of these interactions between firms and customers are dictated, for our members, by the CCD and its impact on the information that must be provided to customers before, during and after a sale. This therefore suggests that for the most part, whether FSMA-style or not, the role of a regulator in these circumstances is to ensure that the prescribed requirements of the CCD are complied with.

64. The BBA believes that FCA supervision of consumer credit should be focused predominantly on consumer risk rather than systemic risk (for which the PRA will have a role). On the basis that supervision will focus on the fairness of the relationship between lender and customer, we believe that supervision within a new regulatory regime should focus on areas of the credit market with high potential for customer risk, such as high cost lending and point of sale credit.

65. However, the size, scope and sheer number of players within the current consumer credit market raises an important question as to whether a FSMA-style regime, which is envisioned to be both intrusive and pre-emptive, can meet the government's aims in an efficient and proportionate manner.

66. Providing effective and appropriate consumer protection through an intrusive supervisory regime is dependent upon the calibre of those carrying out the supervision. Unsecured credit is manifestly different from financial services currently subject to FSMA and it is not readily apparent that the expertise exists within the current regime to apply FSMA-style supervision to a financial service which depends less on the customer/provider relationship than currently regulated services. The sheer range of channels and functions through which personal credit is used and required also presents a formidable challenge to an intrusive FSMA-style regime.

67. The consultation is silent on what role, if any, Trading Standards will have under a new supervisory approach. Trading Standards Officers perform a key function under CCA in policing point of sale credit. The loss of this function under a new regime would be detrimental to consumer protection in the use of credit in these areas.

11. The Government welcomes views on the synergies afforded by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.

68. As the government observes, the FCA can be given the powers to address both the UTCCRs and CPRs for the firms it regulates and its authorisation regime will be able to consider a firm's wider practices where they might impact on its suitability to provide credit. These appear to be sensible ways in which to retain some of the synergies currently available to the OFT.

69. The BBA believes the benefits currently provided by Trading Standards must be retained in some form. Trading Standards Officers provide a useful regional source of intelligence and deterrence and have the expertise to act with regard to the product and the credit offer, which is likely to be missing from the new financial services regulator.

12. Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the Government's objectives (as outlined in paragraph 1.18 of Chapter 1)?

70. The BBA does not believe that the government's objectives could be fully met, or met in an efficient manner, by transferring consumer credit regulation in its totality to a FSMA-style regime. As outlined above, we do not believe that transforming conduct of business regulation for credit from the CCA to a FSMA rule book would allow the government's objectives to be met because of the complexity and costs of such a challenge.

71. However, we do agree that the government's objectives could be achieved in respect of the authorisation, supervision and enforcement of consumer credit through the use of a FSMA-style regime.

72. The government states that a new regime should be proportionate and cost-effective, but it is unable to quantify the costs and benefits of a new regime. Simplification, clarity and coherence are envisioned, but it is clear that, in the short term at least, there would be added complexities and confusion for consumers and lenders in transforming new and existing credit to a new regulatory regime (or in effect running two different regimes).

73. The majority of consumer credit providers do not currently have any of their functions regulated under FSMA, but are able for the most part to provide credit services without detriment to their customers. Applying a more intrusive and proactive regulatory regime to such firms will necessarily increase costs and compliance functions (e.g. regulatory reporting) so one of the challenges for government will be how in these circumstances to meet its objective not to place unnecessary burdens on firms that are not justified by the benefits they bring to consumers.

13. Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?

74. The advantages and disadvantages of transferring consumer credit to a single unified financial services regulator are dependent upon the regime to be applied for consumer credit. As outlined above, a single financial services regulator would be beneficial to our members, if it retained and maintained the existing conduct of business provisions of the CCA, so that the benefits of a single source of regulation are not outweighed by the costs and detriments of replacing the existing regime.

14. Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?

75. We have highlighted a number of key issues that the government should consider in properly assessing its preferred option, the most fundamental of which is that no appropriate cost/benefit analysis has been carried out to demonstrate a justifiable need for action.

76. Further key issues for our members which we have raised and which require further consideration are the likely impacts of a new regime on the UK's interpretation of CCD; the likelihood of the consumer credit market continuing to function in its current form and the

consequences for customers and for the economy if it constricts and the suitability of a more intrusive and proactive regulatory regime to a financial interaction, where the prudential risk is carried by the lender and the potential detriment to the consumer can only normally become apparent in hindsight.

77. The BBA believes that the government should give further detailed analysis to the impact of a regulatory regime change on the 'back book' of lenders. This should not only include the pros and cons for consumers and lenders of transitioning existing agreements across or alternatively running two regimes, but also any potential impacts these approaches might have for the securitisation of loan books within the wholesale market.

15. If you do not agree with the Government's preferred option 1, do you have views on the factors set out in paragraph 2.4 that the Government should consider in determining the most appropriate regulatory authority for the CCA regime under option 2?

78. The BBA believes that each of the factors listed at paragraph 2.4 of the consultation can be considered and resolved using the BBA's preferred approach outlined earlier in our response.

79. The FCA's strategic and operational objectives complement the purpose of the CCA in providing appropriate protection to consumers whilst facilitating an efficient and competitive market. The legislation required to provide the FCA with remit over FSMA could be used to amend the CCA as necessary and the FCA will have responsibility for regulating all other financial services which can include one or more elements of the CCA.

80. With regard to the availability of relevant skills and resources, it is clear that whichever approach the government chooses to take (other than maintaining the status quo), there will need to be sufficient transitional time for a new regulator to recruit and upskill appropriate staff at a national and local level.

Chapter 3.

16. The Government welcomes views on the suitability of the provisions of a FSMA-style regime, such as those referred to in paragraph 3.6, to different categories of consumer credit business.

81. As the government acknowledges, the overwhelming majority of businesses that hold a credit licence are not money lenders. Activities pursued under a license are diverse and many holders are sole traders, likely to have little previous experience of FSMA-style regulation. There are estimated to be over 100,000 licences currently in operation and we do not believe that a FSMA-style regime would be suitable for the majority. This suggests that further consideration needs to be given to the scope of licensable activities, as far as the CCD allows.

82. A FSMA-style regime could significantly increase costs for those firms who are not at present regulated under FSMA (i.e. around 95% of consumer credit licence holders), as a more intrusive regulatory approach to authorisation, supervision and reporting would require additional resources, higher operational costs and could create the risk of license holders leaving the market or seeking to operate without a license.

83. BBA members are familiar with the FSMA regime for their existing regulated activities, so aspects of the regime on authorisation, fee arrangements, threshold conditions and systems and controls would not in theory prove problematic. However, we do not believe that the FSMA rulebook approach to conduct of business would be appropriate.

84. Although the government may choose to draw parallels between the FSMA regulation of mortgages (MCOBS) and a future regime for unsecured consumer credit, it should note that mortgage lending did not previously have legislative-based rules and it was therefore possible to create the current MCOB approach based on the Mortgage Code that preceded it. However, even with a relatively clean slate in which to create MCOBS it has become apparent through the FSA's proposed revisions to the rulebook that the regulator recognises a need for lending to be subject to a prescriptive set of requirements than to a principles-based approach. This

suggests that any transfer of consumer credit to the FCA should retain the provisions of the CCA, rather than the more ambiguous principle/rule/guidance/outcome approach.

85. Moving to an outcomes-based principles regime would generate uncertainties for credit licence holders. At present, firms can be certain that compliance with the prescriptive legislative requirements of the CCA creates a safe harbour and they can therefore plan their business accordingly. This certainty is not clear within a FSMA regime as compliance with the rules may not necessarily be sufficient to meet the subjective outcomes expected by the regulator, which can only ever be evident after the event.

86. As FSA's responsibility for the PSRs has illustrated, it would be possible to place consumer credit under the auspices of the FCA without having to dissemble the CCA and create a new rule book based on an approach which has been discredited by stakeholders and commentators for the uncertainties it creates.

17. Do you agree that statutory processes relating to CPMA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?

87. Proportionality should always form the cornerstone of any legislative and/or regulatory intervention and effective consultation and cost/benefit analysis should be used to achieve these intentions. It is therefore important that appropriate weight and consideration is given to cost/benefit analysis in determining regulatory policy and that qualified (yet persuasive) consumer benefits are not always assumed to outweigh tangible (yet often incomplete) quantification of costs to the industry and wider economy.

88. The BBA supports a risk-based approach to regulation and believes that for consumer credit these risks are more likely to be consumer focused, than risks of a systemic nature. In part this is because if a lender fails the borrower does not lose, but also because strict capital requirements which govern how a bank is able to lend should ensure that unsecured consumer credit provision should not normally, of itself, create a systemic risk.

89. If regulation is to be risk-based and those risks are to be described in terms of consumer detriment, it is important to consider where and how the consumer can face detriment and to focus supervisory efforts in that direction. As explored in response to question 3, we believe that point of sale risks i.e. irresponsible lending or inappropriate products can be addressed via the CCA and regulatory focus should be directed to sub-prime and goods and services credit. For the risks associated with over-indebtedness, we believe the government must give careful consideration as to how and whether debt should be regulated by the FCA.

18. The Government welcomes views on key factors that would need to be assessed in considering fee arrangements for consumer credit firms.

90. We believe that there are two key factors that must be considered in determining an appropriate fee structure for a new regime. The first comes from an acknowledgement that any significant increase in fees, from their current levels, is likely to drive some smaller (and in some cases more specialist) lenders out of the market. For many others, such an increase will have to be passed on to consumers rather than absorbed into business costs.

91. The government states at paragraph 3.20 that a new regime should avoid cross-subsidy, but it is difficult to reconcile this approach if the regulator is expected to focus their efforts on those lenders and types of credit that present the greatest potential customer risk, whilst avoiding its funding regime leading to a constriction in the market. It is likely to be smaller and more specialist lenders with least market share where there is greatest potential for consumers to suffer detriment and where a more intrusive approach is required, but these are the firms least able to shoulder the costs of a non-subsidised fee structure that allocates fees in accordance to the resources that the regulator will need to employ.

92. The BBA therefore believes that some cross-subsidisation is inevitable if resources are to be allocated to where they are needed most, without forcing the market to constrict because of the

added costs of more intrusive regulation. However, due to the economies of scale that should be achievable for those firms already subject to FSA regulation and fees, it will be difficult for the government to justify a level of cross-subsidisation that would be necessary to allow small lenders to continue to operate, whilst transferring the fees regime across from the OFT model (where compliance costs amount to circa £15 million p.a.) to an FSA model (which currently costs financial services up to £850 million p.a.)

19. The Government welcomes:

- **evidence relating to experiences of the current appointed representatives regime;**
- **views on how an appointed representatives model might be applied to different categories of consumer credit activities, including how current business models and networks might lend themselves to such an approach; and**
- **evidence relating to the implications an appointed representatives regime might have for firms and consumers.**

93. The BBA believes that many lenders would not be prepared to assume the liabilities that result from allowing others to sell their products and services under an Appointed Representative (AR) regime.

94. The government uses the current AR regime under FSMA to illustrate how it might be employed for credit, but there are fundamental differences between the activities of ARs for investment, pension and mortgage products than those of firms who currently provide credit on behalf of lenders. ARs under the FSMA regime are appropriately qualified and their principle functions are to sell financial services, whereas credit can be currently sold by any number of different retailers whose main functions will be the sale of non-financial goods and services.

95. Operationally such an approach would be extremely difficult for lenders to police due to the nature of the point of sale environment, where customer/staff interactions are less formulated and less geared toward financial services and where the lender is too far removed from the seller and the sales environment to be confident that they can always ensure that the actions of the seller are compliant.

96. The BBA believes that application of the AR regime to consumer credit would result in a fundamental change to the point of sale credit market, with some providers withdrawing their products and others having to initiate a more drawn out and therefore expensive point of sale process to mitigate the liabilities that the regime would create.

20. The Government welcomes:

- **evidence relating to experiences of the current group licensing regime; and**
- **views on how the professional bodies regime might be adapted for different categories of consumer credit activities.**

97. Although the group licensing regime can provide benefits to firms and to the OFT in allowing organisations to operate at the margins of licensable activity, it is within these activities that some of the most unscrupulous firms currently operate. For example, some claims management companies and debt management firms currently use the permissions of a group license to pursue questionable activities to the detriment of vulnerable customers.

98. We believe that the government must first determine the future scope of activities for which a credit license is required (beyond those dictated by the CCD) before considering what is the most appropriate means by which to license or authorise their operation. For instance, it could be appropriate to remove debt advice and management services from consumer credit regulation and instead provide for them to be regulated under a dedicated regime within the Insolvency Service.

21. The Government welcomes views on the extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises.

99. Self-regulatory codes currently provide the most dynamic and visible means of conduct of business regulation for stakeholders to establish and measure the most appropriate treatment of customers under the CCA. At present, these codes fill a gap that exists because the CCA's requirements prescribe only aspects of the creditor/borrower relationship and the OFT's remit is restricted to that of a reactive regulator (enforcer) with few monitoring and supervision functions.

100. If the government determines that consumer credit should be regulated under a more proactive and intrusive regulator, either via the FSMA regime or, as we recommend, via a recognised authority of the CCA, then careful consideration needs to be given to how self-regulation could fit into such a regime. It is important that statutory regulations and self regulation do not overlap or conflict and that firms and customers know which regulator and what standards apply in any circumstance.

101. Such concerns suggest that it would not be appropriate for the FCA to outsource its day-to-day regulatory activities to a self-regulatory body such as the Lending Standards Board (LSB). Under such a model the industry could not have certainty to any outsourced regulator's decision so long as the statutory regulator has the power to intercede and re-interpret rules and guidance when it saw fit.

102. The BBA does though see merit in the Industry Guidance approach to self-regulation, whereby the industry can seek the agreement of the statutory regulator to a set of minimum standards being sufficient to meet the regulator's expectations. Such an approach should though be established within a clear and consistent statutory process so that it cannot be used by the regulator as a tool by which to circumvent the consultative process and introduce new standards.

103. We believe that self-regulation via Industry Guidance could be an efficient and effective tool to apply a new regulatory regime across the wide and varied segments of the consumer credit market. It would allow the continuation of existing standards, where appropriate, without risking super-equivalency to the CCD by the new regulator.

22. Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.

104. As outlined above, the BBA believes that some activities currently requiring a credit license, but not subject to the maximum harmonisation directive e.g. debt management and debt advice could be moved out of the regime. We do not believe these should be deregulated, but that they would be better suited to a regulatory regime, dedicated to debt and insolvency. A similar approach should also be considered for hire and hire purchase.

105. As outlined in the BBA's submission to the BIS review of credit and personal insolvency, we believe that a number of CCA requirements (not prescribed by the CCD) are not fit for purpose and could be removed without causing consumer detriment. These include rationalising the requirements around the signing of agreements; removing the requirement to send notices of arrears to "gone aways"; rationalising and in some parts removing the unenforceability sanctions of the CCA where these are disproportionate and open to abuse by claims management firms; repeal of requirements concerning modified agreements.

23. Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approach?

106. The BBA refers the reader to our preferred approach, outlined at the outset of this submission, which we believe provides a proportionate, effective and low-risk approach that would be achievable within the government's committed timetable.

Chapter 4.

24. The Government welcomes views on how the treatment of agreements already in existence could be approached.

107. The BBA strongly believes that it would neither be appropriate or justifiable in terms of costs and complexity to create two conduct of business regimes (a front book and a back book) to achieve the government's aims of creating a new regulatory regime. To do so would entail massive costs and systems changes for the industry; would risk widespread confusion amongst customers and would create a number of complex challenges, such as how to deal with running account credit or the rearrangement of existing credit lines.

108. Likewise, the BBA would not support the retrospective application of new conduct of business requirements to existing credit business. Again this would require massive systems changes and associated costs and could result in widespread confusion and misunderstanding for customers.

109. The BBA believes that a retrospective change would also have consequences for existing securitisations of loan books. Depending on the terms of the transactions, it may put lenders in breach of contract. By way of example, to the extent that any new rules have an impact on existing loan enforcement procedures and practices of lenders, considerations arise as to whether compliance may result in a breach of asset servicing arrangements contemplated by securitisation transaction documents.

25. The Government welcomes views on:

- **how existing licensees could be dealt with; and**
- **factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms.**

110. The BBA would support the use of "grandfathering" to bring existing licenses into a new regime, for those firms already authorised by the FSA. This would allow the new regulator to adopt a risk-based approach and focus on creditors who are not currently subject to the FSA's comprehensive authorisation process.

111. The BBA notes that it is common practice for special purpose vehicles (SPVs) used in securitisations to obtain a CCA license. As acknowledged by the government in the 2009 consultation on mortgage regulation, if SPVs were to be subject to regulation under a FSMA-style regime it could hamper the operation of securitisation markets and secondary markets of consumer credit portfolios.

112. Therefore a carve out for both existing SPV licensees and new SPVs will need to be incorporated within any new FSMA-style authorisation regime.

26. The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.

113. The BBA agrees that any future regime requiring a transition of fee structures should be subject to an appropriate 'soft launch' to mitigate the risks of widespread withdrawal from the market of credit providers. Discounted and/or graduated authorisation fees might be appropriate as would the continuation of existing licenses, where these are for a defined period.

114. An extended period of collection will also be required for the new fees due to the volume of firms likely to have to contribute to a new levy. A new regulator would also need to consider appropriate safeguards in transitioning to a new structure to mitigate that unscrupulous lenders might seek to unfairly reposition themselves more favourably within the new structure.

27. Are there other factors the Government should take account of in considering transitional arrangements?

115. If the government determines that a new regulatory structure is appropriate it must ensure that all authorities which interact with consumer credit are either fit for purpose or are developed in

tandem with the new credit regulator. Examples include each of the statutory authorities with responsibility for debt issues and those that will assume responsibility for regulating the Consumer Protection Regulations (CPRs) and Unfair Terms in Consumer Contracts Regulations (UTCCR) where they might relate to goods and services purchased with credit.

28. The Government would welcome evidence on the experience of firms, consumers and their representatives in relation to similar previous transitions, for example the extension of FSA jurisdiction to new markets since 2000.

116. The BBA encourages the government to liaise with the ABI and the CML to consider the impact of the extension of FSA jurisdiction to the insurance and mortgage markets respectively and in particular, with respect to the consequences for the back-books of firms within both markets.

HM Treasury/ BIS Department for Business Innovation & Skills

A new approach to financial regulation: consultation on reforming the consumer credit regime

RESPONSE OF THE BRITISH CHEQUE & CREDIT ASSOCIATION (BCCA)

22 March 2011

Introduction

The British Cheque & Credit Association (BCCA) is a trade association which was formed in 1994. It represents the interests of businesses which offer encashment facilities for third party cheques and/or certain other forms of very short term, unsecured consumer loans repayable within six months or less. This includes what is now generically called “payday lending”.

The BCCA has around 850 members, the vast majority of which are small businesses which operate from high street premises. The BCCA also represents several lenders which operate solely via the internet. Whilst most members offer third party cheque encashment facilities, only some offer “payday loans”. However, these include all of the BCCA‟s corporate and internet based members.

The BCCA is in daily contact with its members and therefore understands fully their commercial needs and concerns.

There are no confidentiality issues contained in this response.

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RESPONSE OF THE BRITISH CHEQUE & CREDIT ASSOCIATION

The BCCA welcomes the opportunity to respond to this consultation. It is our policy to co-operate fully with legislators and regulators on all matters.

Note: For the purposes of this response, we refer to the 'CPMA' rather than the 'FCA' given that the change in name occurred after this consultation was published.

General Comments & Observations

- The BCCA‟s preferred option is OPTION 2. We are strongly opposed to Option 1 due to the likely impact this would have on the consumer credit industry. Our key reasons for favouring Option 2 are listed below:

    - **Market Exit** – Given that the regulatory burden will significantly increase, SME‟s in particular are likely to leave the market - the very sector of the economy that could produce growth in the future. We are concerned that an FSMA-style would bring with it a **'one size fits all approach'** to regulation. For a significant number of credit businesses this would result in a disproportionate level of regulation in relation to the product(s) they offer.

      The result of SME‟s exiting the market is less competition. This will have a detrimental impact on consumers in terms of the charges they pay and their ability to access credit.

    - **CCA regime** – We believe that the CCA regime is fit for purpose. It is well established and has witnessed significant change in the last 36 years, primarily since the Consumer Credit Act 2006. More recently there have been changes as a result of the European Consumer Credit Directive. This has increased consumer protection measures within the existing regime. Further regulatory change of the magnitude described in the consultation would result in yet another period of uncertainty and overwhelming change for consumer credit businesses. In the current economic climate this is undesirable.

    - **Expertise and experience of the CCA regime** – This has been developed over a period of time at the Office of Fair Trading (OFT) and Trading Standards.

      We do not believe that the OFT has failed in its duty to licence and enforce under the CCA regime. Given the changes to the licensing regime as a result of the Consumer Credit Act 2006 the OFT is able to scrutinise applicants who apply for a licence, particularly those under „high-risk" categories. To achieve this, applicants may be asked to complete credit risk profiles (CRP) or credit competence plans (CCP). In addition, they may also be subject to an on-site visit from their Local Authority Trading Standards Service (LATSS).

The OFT can, at any time, impose requirements on licensed businesses as well as having the power to refuse, vary or revoke a licence. The OFT has proven that they are willing to exercise these powers. In recent months alone, there have been a number of cases where, for example, requirements have been imposed on small and large credit businesses. Breach of any requirement can result in a fine of up to £50,000 which we believe is a deterrent to potential future non-compliance.

- Given the market failures in terms of mis-selling that have occurred under the FSMA regime, for example, with pensions, PPI and endowment mortgages we are surprised that this model of regulation is being held up as being better than the CCA regime.

- Should Government be intent on a single regulator for retail financial services, then we would suggest that the CCA regime is retained with the OFT continuing to licence and enforce consumer credit businesses sitting within the CPMA.

- It is unclear what the Government"s vision of consumer credit is for the future. For a healthy, competitive market without unnecessary regulatory burdens then we believe that Option 2 should be the preferred option. Option 1 is likely to result in a small number of larger credit businesses which will result in less consumer choice in terms of price and supply and ultimately reduced access to credit.

- We do not believe that there are enough sound, objectively justified reasons for the magnitude of change proposed. It is our understanding that there has been no research undertaken with businesses or indeed consumers prior to this consultation to assess how those most affected by the proposed changes view the current CCA regime and the OFT.

- Government should not under estimate the magnitude of change that is being proposed in the consultation document under Option 1. For example, it would involve re-educating those businesses that could afford to stay in the market; there would be costs involved in system changes, training staff etc. In addition, consumers and their advisors would have to become familiar with a new regime. This would take time and for Government funded advice agencies, would also result in costs to the taxpayer.

- If Option 1 were adopted and failed, it would have a catastrophic effect on businesses, consumers and the wider economy. Therefore we do not feel that this decision should be rushed. As Andrew Tyrie, Chairman of the Treasury Select Committee commenting on their report published on 3 February 2011, „House of Commons Treasury Select Committee Financial Regulation: a preliminary consideration of the Government‟s proposals‟ (Seventh Report of Session 2010-11) has stated;

  „In light of the banking crisis, the government is rightly proposing radical changes to the way in which financial services are regulated. However, having examined the initial proposals, the Committee's overriding concern is about the proposed speed of implementation.'

  He also commented that *'it is vital to maintain the momentum for reform, but there is no point in flawed change.'*

  (Source Citywire 3.2.11)

- The timescales that were suggested in the consultation document should Option 1 be adopted (mid 2014) seem highly unrealistic for the reasons mentioned above. Government should reflect on recent examples such as the challenges and pressure that businesses faced during the implementation of the European Consumer Credit Directive and the impact this had when very restrictive timescales were imposed.

- The consultation does not appear to work in tandem with the Government‟s announcement in July last year of a review of consumer credit and personal insolvency.

- The consultation seeks views on how, if Option 1 were adopted, consumer credit licences and existing agreements should be treated. We believe that decisions surrounding these matters should only be consulted on once a decision has been made on whether consumer credit responsibility should be transferred.

Chapter 1

1. ***Do you agree with this assessment of the consumer credit market?***

We do not agree with the assessment of the consumer credit market detailed in Chapter 1 of the consultation document. As a result, we have the following comments:

- The consultation document on page 13, paragraph 1.17 under the heading „*Too reactive and insufficiently flexible'* states that, „*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.'*

  We believe that some firms under the FSA‟s supervision in the past have engaged in dubious business practices (an example has been included below). We also believe that the extent and nature of consumer detriment this has created has been far greater than instances of abuse under the CCA regime. We believe that the FSMA-style model of regulation is flawed and are surprised that it is being held up as an example of what future regulation should be modelled on.

  <u>Example</u>

  Despite being supervised by the FSA and being subject to a plethora of controls and requirements to document and complete detailed records of interaction with prospective customers receiving financial advice, two of the worst instances of consumer abuse occurred in connection with **pension products & endowment mortgages**.

  The mis-selling of these products was widespread and well known. The documentation required by the FSA merely confused the customer. This was particularly so in the hands of unscrupulous salesmen who were merely „ticking the right boxes‟

  There is no evidence that the FSMA-style of regulation had any effect on consumer protection. A significant amount of money has been paid out to consumers in compensation after the market abuse came to light. These events illustrate the widespread nature of consumer detriment that occurred under this model of supervision.

- We have concerns regarding the comments made in the same paragraph when its states that,

  '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.'

There is an inherent danger in *'outlawing emerging unfair practices across the board'* in that it could inadvertently result in legitimate practices being banned when it is simply the abuse of such practices that should be dealt with. Therefore we believe it is appropriate that action is only taken against those credit businesses where instances of abuse have been identified and proven.

We also believe that this style of approach could create further uncertainty for businesses if, for example, new policies/ guidance etc were continuously being imposed as a regulator reacts to instances of unfair practice.

It is also worth noting, that the OFT, through their guidance, indicate to licensed credit businesses what they believe to be unsatisfactory businesses practices. This is evidenced, for example, in the current Debt collection guidance Final guidance on unfair business practices July 2003 (updated December 2006) OFT 664 and the Irresponsible lending – OFT guidance for creditors March 2010 (updated February 2011) OFT 1107.

- The consultation document makes numerous references to the fact that it can be difficult to make changes to primary legislation because of the Parliamentary process that is involved. Where possible, new avenues could be explored to deal more quickly and efficiently with small imperfections identified/ changes required in primary legislation.

- We do not believe that the lack of deregulation that has occurred is solely as a result of the general requirement for primary legislation to amend the CCA. We believe that this is partly because previous Governments have been focused on increasing rather than reducing the regulatory burden and there has not been a concerted effort to deregulate. We believe this is the reason why a number of deregulatory measures in relation to the CCA remain outstanding.

2. Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail financial services?

We do not believe that it is a fair assessment of the problems caused by the way in which consumer credit is regulated for the reasons detailed in our answer to Question 1.

We would also like to make the following points:

- The CCA regime is well established with business, consumers, advice agencies and the courts. Familiarity with a regulatory regime is important in ensuring compliance and creates an environment where consumers are aware of and are confident in exercising their rights. We believe that to take that regime away would have a detrimental impact, creating an uncertain and unnecessarily challenging future.

- We do not support the view that there remains a *'fundamental weakness caused by the split in responsibility'* between the FSA and the CCA regime. Indeed there seems to be no evidence base for this. Remarkably the Impact Assessment is unable to identify any real consumer benefit that would result from transferring consumer credit responsibility.

- However, as referred to in our „*General comments and observations'* if the Government is intent on a single regulator for retail financial services, then we would suggest that the CCA regime is <u>retained</u> with the OFT continuing to licence and enforce consumer credit businesses sitting within the CPMA.

- We would also like to point out that removing the split in responsibility for retail financial services might create problems which under the existing regime do not exist. Recent examples in history prove that there can be unintended consequences.

3. The Government would welcome further evidence relating to the consumer credit regime, including in particular:

- ***the types of risks faced by consumers in consumer credit markets;***

The most significant risk to consumers in consumer credit markets is reduced access to credit. Were this to occur, the risk is that it would force some consumers to approach illegal money lenders. This risk would increase if a significant number of SME"s exit the market and access to credit is reduced. The Impact Assessment also identifies this risk.

- ***key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers; and***

We believe the key provisions for consumer protection under the current regime that are effective are as follows:

  - Local Authority Trading Standards Services through their partnership with Consumer Direct are able to provide advice and support to consumers who complain about goods and/ or services they receive. Trading Standards are able to gather intelligence regarding businesses that are operating within their boundaries and have powers under the <u>Enterprise Act 2002</u> to take appropriate action against businesses where this is necessary. They are also able to support and advise businesses to ensure compliance and secure appropriate outcomes for consumers. Intelligence is shared between Trading Standards and the OFT to ensure that consumers are protected against businesses that are non-compliant.

- There is very little reference in the consultation document to the role that the Financial Ombudsman Service (FOS) plays in the consumer credit market and the fact that FSMA regulated businesses are bound by the same rules. As a result of the Consumer Credit Act 2006 FOS jurisdiction was extended to cover consumer credit complaints. It means that consumers do not have to rely on the court system and can attempt to resolve their dissatisfaction through a system that is free and easily accessible to them. It would appear that in credit related cases consumers are increasingly taking note of their right to refer a case to FOS.

- Under the CCA regime, every aspect of the lending process is regulated so that there are adequate consumer protection provisions in place.

- ***the incidence of regulatory duplications or burdens on firms and/or inconsistent regulation of similar types of business.***

- Generally, BCCA members are only regulated by the OFT and it is unlikely that businesses operating in the short term, unsecured lending market would fall into the 16,000 businesses which are dually regulated by OFT and FSA.

4. Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?

We do not necessarily disagree with the headline objectives. However, we are concerned with some of the detail contained within those objectives in the consultation paper.

We have the following comments in relation to the appropriateness of the objectives:

- *Clarity, coherence and improved market oversight* (page 14, paragraph 1.18) – we are concerned with some of the comments within this objective, for example, *'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.'* This could result in a „one size fits all" approach to regulation being adopted.

  This would be entirely inappropriate given the varying nature of products that this would extend across. We believe that proportionality is the key to effective regulation. For example, it would not seem unreasonable that the requirements relating to the granting of a £100 short term, unsecured loan for 30 days are less onerous than those imposed for a £25,000 secured loan over 10 years.

- *Effective and appropriate consumer protection, including through a responsive and flexible framework* – we are concerned with some of the comments within this objective, for example, *'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'* (page 14, paragraph 1.18).

  Flexibility can be a double-edged sword and can have unintended consequences for business. Flexibility can create uncertainty and further regulatory burdens if requirements are constantly being changed or introduced. We believe that, given the significant amount of changes that the credit industry has been through, that the pace of change is slowed down.

- There has always been an emphasis on consumer protection and this is evidenced in the nature of the changes that have occurred in recent times. However, we believe that there is an opportunity for Government, rather than driving Option 1, to use these objectives to encourage simplification, deregulation, proportionality and cost effectiveness through the existing regulatory framework.

Chapter 2

5. The Government welcomes views on the impact a unified regulatory regime for retail financial services may have in terms of clarity, coherence and improved market oversight.

We are not convinced that there is the level of confusion amongst consumers regarding the roles of both the FSMA-style regime and the CCA regime.

As we have mentioned in our introduction under *'General comments and observations*‟, should Government be intent on a single regulator for retail financial services, then we would suggest that the CCA regime is <u>retained</u> with the OFT continuing to licence and enforce consumer credit businesses sitting within the CPMA. We believe that this would help to achieve the Government‟s objective of increased market oversight with all retail financial services undertaking the same objectives.

6. The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.

As we have mentioned in our response to question 3, we believe that Consumer Direct, Trading Standards and FOS play a fundamental role within the current consumer credit regime and that these institutions should be preserved. There is a real risk that a failure to retain institutions that consumers recognise could increase the likelihood of consumer detriment.

- Local Authority Trading Standards Services through their relationship with Consumer Direct are able to provide advice and support to consumers who complain about goods and/ or services they receive. Trading Standards are able to gather intelligence regarding businesses that are operating within their boundaries and have powers under the Enterprise Act 2002 to take appropriate action against businesses where this is necessary. They are also able to support and advise businesses to ensure compliance and secure appropriate outcomes for consumers. Intelligence is shared between Trading Standards and the OFT to ensure that consumers are protected against businesses that are non-compliant.

  It is also worth noting the vital role that Trading Standards play in establishing relationships with local businesses through the Home Authority/ Primary Authority principle. This can help to ensure consistency of advice and indeed co-ordinated enforcement action under the Primary Authority principle.

- There is very little reference in the consultation document to the role that the Financial Ombudsman Service (FOS) plays in the consumer credit market and the fact that FSMA regulated businesses are bound by the same rules. As a result of the Consumer Credit Act 2006 FOS jurisdiction was extended to allow consumers to refer consumer credit complaints to them. It means that consumers do not have to rely on the court system and can attempt to resolve their dissatisfaction through a system that is free and easily accessible to them. It would appear that in credit related cases consumers are increasingly taking note of their right to refer a case to FOS.

7. The Government welcomes views on factors the Government or the CPMA may wish to consider in the event of a transfer of consumer credit regulation relating to how the overall level of consumer protection might best be retained or enhanced.

We would like to make the following comments:

- We believe that the current CCA regime is robust and provides a significant level of consumer protection. We believe that enhancing the level of consumer protection further would create an imbalance between the rights of consumers and the rights of creditors.

- If Government decided on Option 2, we believe it could be an opportunity to focus on and address any anomalies within the CCA regime.

8. The Government would welcome further evidence relating to:

- ***the use of consumer credit by small and medium sized enterprises (SMEs);***
- ***whether the protections currently afforded by the CCA are appropriate and cover the right groups of businesses; and***
- ***the costs and benefits of considering extending FSMA-style conduct of business rules to a wider group of SMEs.***

There is some evidence that consumer credit is accessed by very small start up enterprises where mainstream credit is denied. We believe that the protections afforded by the CCA regime are ordinarily perfectly adequate in their current form. We do not believe that there is a strong enough case for extending the rules any further. There is a danger that this type of change might stifle small scale entrepreneurs.

9. The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.

As we have mentioned previously, what businesses want, particularly after a period of regulatory change and in light of the difficult economic environment, is certainty.

There would be a real risk of constant change on a much more frequent basis than is experienced under the CCA regime. As we have mentioned, increased regulatory burdens could result in SME‟s exiting the market and could seek to stifle the Government‟s objective of simplification and deregulation.

10. The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.

As we have mentioned previously, we have concerns regarding the way in which the current FSMA-style regulation is being held up as a model regulatory regime when, through numerous examples in the past it has proven to have resulted in SME‟s exiting the market and the failure to identify inappropriate business practices.

Therefore we strongly disagree with the contention on page 20, paragraph 2.18 of the consultation document that „.... *the focus on regular reporting, firm governance, culture and systems and controls under a FSMA-style regime – complemented by thematic work across sectors or issues where appropriate – should deliver better outcomes for consumers.'*

Following the FSA taking control of the supervision of the **insurance** and **pensions** industry in 1988, their style of approach was to demand high levels of documentation to justify sales of insurance and investment products being sold to consumers.

As we have previously mentioned when referring to the mis-selling of pension products and endowment mortgages, this style of approach did not improve consumer protection. Instead it had unintended consequences of reducing choice in the market.

Along with demands for large amounts of documentation there was a “one size fits all” approach regardless of whether the product being sold was a £5 per month savings policy with the “man from the Pru” or a £200,000 investment of a widows life savings.

The increased cost and complications of complying with these requirements led the majority of insurance companies in the industrial branch insurance sector exiting the market altogether. These companies (such as Prudential, Refuge Assurance, Pearl Assurance etc, once household names) provided insurance and investment products with premiums home collected on a weekly/monthly basis to lower income families.

It is interesting to note that the home collected credit industry, operating under the CCA regime and serving almost exactly the same customers, has remained.

The resultant reduction in the level of insurance and savings providers in this sector will almost certainly have resulted in increased costs to the taxpayer due to providing funerals where no money is available.

We believe that the CCA regime has actually delivered better outcomes for consumers than the FSMA-style model when the above examples are taken into consideration.

11. The Government welcomes views on the synergies afforded by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.

We would support retaining synergies that already exist, for example Trading Standards Services. Please see our response to questions 3 and 6.

If Government chose Option 2, synergies that work well under the current system could be retained.

12. Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the Governments objectives (as outlined in paragraph 1.18 of Chapter 1)?

We do not agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the Government‟s headline objectives.

We believe that the following objectives could not be adequately achieved; *simplification* and *deregulation*, *proportionality* and *cost effectiveness* for the following reasons:

- **Simplification and deregulation** - The ability to move from a CCA regime to an FSMA-style consumer credit rulebook is significantly understated. We believe it is important for Government to recognise the challenge that would present itself if the entire Consumer Credit Act 1974 (CCA) and its subordinate legislation had to be re-written.

- We do not believe that it would result in simplification or deregulation – in fact, we believe it would have the opposite effect. This is touched on at page 21 in paragraph 2.24 in the consultation document when it states *'a transfer of consumer credit to the CPMA may therefore result in new obligations for firms in some areas.'*

  We would also make the point, as acknowledged in the consultation document, that Government would be unable to completely re-write the CCA given the constraints of maximum harmonisation EU law.

- We believe that deregulation could be achieved through the existing regime by Government making a concerted effort to assess those areas of the consumer credit market where this would be appropriate.

- **Proportionality and cost-effectiveness** – We are concerned that this objective would be undermined under the CPMA. We believe that there is an inherent danger that „a one size fits all approach‟ to regulation will be adopted and that this will result in SME‟s exiting the market. This will have a detrimental impact on consumers. There will be reduced competition and access to credit as well as the cost increasing.

- As acknowledged within the consultation document and within the Impact Assessment, it is clear that if the Government progresses Option 1 it would result in a significant increase in costs for business. For example, on page 15, paragraph 70 of the Impact Assessment, it states, *'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).'* Again we believe that this will result in SME‟s exiting the market, but we also believe that it could result in some businesses operating outside of the regulatory regime. This is a real risk to Option 1 being adopted.

13. Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?

In our introduction under „*General comments and observations'* we set out the key disadvantages to Option 1 being adopted. These are, in summary:

- Market exit
- Potential for „one sits fits all" regulation
- Uncertainty for business
- Loss of expertise and experience
- FSMA-style model has not been able to prevent significant market failures and consumer abuse in the past
- Potential loss of other organisations/ bodies

Advantage

- One regulator for retail financial services, as it would provide a single point of contact for consumers. This, coupled with the familiarity of the existing CCA regime run by the OFT could add benefit (Option 2).

14. Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?

We believe that all of the specific issues that have been identified in our introduction under *'General comments and observations'* and which have been reiterated in our response to question 13 should be considered by Government.

We believe that before any decision is made Government should consult specifically on these issues and the effect that they would have on consumers and business. Given the seriousness of the issues raised and potential consequences, making a decision on which option should be taken should not be hurried by Government.

15. If you do not agree with the Governments preferred option 1, do you have views on the factors set out in paragraph 2.4 that the Government should consider in determining the most appropriate regulatory authority for the CCA regime under option 2?

We believe that all of the factors set out in paragraph 2.4 should be given in-depth consideration when determining the most appropriate regulatory authority for the CCA regime under Option 2.

In particular we believe that *'The availability of relevant skills and resources within the relevant regulatory authority* should be a key consideration. For example, the OFT has developed significant expertise and experience in the consumer credit market and in their dealings with industry over a prolonged period of time.

We would support the suggestion of a further consultation on the regulatory authority with responsibility for the CCA regime

Chapter 3

16. The Government welcomes views on the suitability of the provisions of a FSMA-style regime, such as those referred to in paragraph 3.6, to different categories of consumer credit business.

We believe that the provisions listed in paragraph 3.6 would be entirely unsuitable for credit businesses per se, for the following reasons:

- It would not support the Government‟s objectives for the CPMA with respect to; simplification, deregulation, proportionality and cost effectiveness.

- It would create disproportionate regulatory burdens that would be a key driver for market exit (for example as has occurred in the past regarding industrial branch life insurance – see answer to question 10);

- This style of regulation has not prevented significant market failures or consumer abuse in the past (see example relating to pension product and endowment mortgage mis-selling – see answer to question 1);

- All the evidence tends to suggest that this type of intrusive supervision is not effective and does not prevent consumers being exposed to considerable detriment.

17. Do you agree that statutory processes relating to CPMA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?

We believe that if the Government progresses Option 1 that a separate consultation is carried out to ensure that the most proportionate approach to consumer credit regulation is adopted.

Given the varying nature of businesses that are currently regulated under the CCA regime, proportionality is of key importance. Disproportionate regulation/ supervision results in market exit and increased compliance costs which are ultimately passed on to consumers.

We support risk-based regulation. For example, we would expect the regulation of a £100 short term, unsecured loan repayable in 30 days to be different from a £25,000 secured loan repayable over 10 years. In the former case, you would expect a lighter-touch approach than for the latter.

18. The Government welcomes views on key factors that would need to be assessed in considering fee arrangements for consumer credit firms.

We would like to make the following comments:

- We believe that any fee charging system should balance simplicity with fairness and proportionality. Transparency is also a key factor.

- Due consideration should be given to the fees that are currently applied under the CCA regime in terms of the amounts and their frequency. This is extremely important given that any significant divergence could result in market exit.

  As acknowledged in the consultation document on page 29, paragraph 3.22 *'the Government recognises that there is a significant discrepancy between the typical fees paid under the current FSA and OFT regimes, and the period over which they apply, and that a transfer would be likely to result in increased fees for many firms'*

  Paragraph 3.22 also goes on to say that *'the FSA charges a one-off application fee and an annual periodic fee, both of which currently have minimum levels higher than OFT licence fees'*

- Other factors that should also be given due consideration in any assessment of a fee charging structure include:

  - Size of the business (for example a sole trader or small limited company with one or two branches in a specific area compared with a bank that has hundreds of branches across the UK).

  - Type and amount of credit (for example, a creditor who only offers small term, unsecured loans compared with a creditor who offers higher value loans on a secured or unsecured basis).

19. The Government welcomes:

- ***evidence relating to experiences of the current appointed representatives regime;***

- ***views on how an appointed representatives model might be applied to different categories of consumer credit activities, including how current business models and networks might lend themselves to such an approach; and***

- ***evidence relating to the implications an appointed representatives regime might have for firms and consumers.***

The BCCA has no comment.

20. The Government welcomes:

- ***evidence relating to experiences of the current group licensing regime; and***

- ***views on how the professional bodies regime might be adapted for different categories of consumer credit activities.***

The BCCA has no comment.

21. The Government welcomes views on the extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises.

We believe that self-regulation has a place in any regulatory regime for the following reasons:

- A trade association"s Code of Practice is of fundamental importance both to its members and to consumers. This is because Codes of Practice tend to reaffirm key consumer protection principles whilst in certain cases, extending that level of protection.

- Often, voluntary Codes of Practice include sanctions where subscribers fail to comply.

- We fundamentally disagree with comments made in the Impact Assessment on page 13, paragraph 59 that *'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.'*

  We believe that a robust Code of Practice supports the regulatory regime.

- We believe that the provisions set out in voluntary Codes of Practice should remain the subject of self-regulation rather than being incorporated into, for example, a consumer credit rulebook, for the reasons mentioned above.

22. Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.

We believe that deregulation could be achieved regardless of whether Option 1 or 2 was adopted. We have always supported deregulation where there is an opportunity to do so.

23. Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approach?

We believe that the only way to preserve a proportionate and effective approach is through the retention of the CCA regime, preferably with licensing and enforcement of it by the OFT for the reasons mentioned throughout the course of this response.

Chapter 4

24. The Government welcomes views on how the treatment of agreements already in existence could be approached.

We believe that this type of detail should have been reserved for discussion, if relevant, once a decision had been made by Government. However, we would like to make the following comments:

- The suggestion on page 36, paragraph 4.11 of the consultation document that consumer credit agreements already in existence would be transferred to the CPMA is highly likely to have a detrimental impact on both consumers and businesses.

- From a business perspective it would increase the cost of transition from the CCA regime to the CPMA (as acknowledged in paragraph 4.12, page 37 of the consultation paper) and would also add another dimension of complexity. We believe that it would stifle the Government‟s objective of simplification.

- From a consumer perspective, for those with existing consumer credit agreements, it would be exceptionally confusing to understand what rights and protections apply to the agreement once the transfer to the CPMA had been made. It could result in consumers not exercising their rights and therefore having a detrimental impact.

25. The Government welcomes views on:

- ***how existing licensees could be dealt with; and***

- ***factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms.***

We believe that this type of detail should have been reserved for discussion, if relevant, once a decision had been made by Government. However, we have the following comments:

- The CCA licensing regime is robust. This is particularly so since the changes to the licensing regime as a result of the Consumer Credit Act 2006. The OFT is able to scrutinise applicants who apply for or who look to renew their licence, particularly those under „high-risk" categories. To achieve this credit risk profiles (CRP) or credit competence plans (CCP) are used.

  In addition, the OFT can, at any time, impose requirements on licensed businesses as well as having the power to refuse, vary or revoke a licence. The OFT has proven that they are willing to exercise these powers. In recent months alone, there have been a number of cases where, for example, requirements have been imposed on small and large credit businesses. Breach of any requirement can result in a fine of up to £50,000 which we believe is a deterrent to potential future non-compliance.

- Should Government decide to progress Option 1 we would strongly recommend the „grandfathering" of existing consumer credit licences into the new regulatory regime. The suggestion that there would not be an automatic transfer would seem to undermine a licensing system that has proven to be effective. We are surprised that the FSMA-style model is favoured in this regard given that it has failed to prevent instances of substantial market failure and consumer abuse in the past.

26. The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.

We believe that this type of detail should have been reserved for discussion, if relevant, once a decision had been made by Government. However, we would like to make the following comments:

- As stated in our response to question 18 it is our view that any fee charging system should balance simplicity with fairness and proportionality. Transparency is also a key factor.

- There is a real risk that businesses will exit the market if there is an immediate hike in costs which are disproportionate to the product(s) that they offer. Ultimately any fee charging structure would have to take account of fees charged under the CCA regime.

27. Are there other factors the Government should take account of in considering transitional arrangements?

If the decision is made by Government to pursue Option 1 then it would seem an appropriate time for a further consultation on the transition process and what risks it poses.

28. The Government would welcome evidence on the experience of firms, consumers and their representatives in relation to similar previous transitions, for example the extension of FSA jurisdiction to new markets since 2000.

The FSA extended its regulation to the mortgage industry in 2005 even though it was seen to be well regulated by the Mortgage Code Compliance Board. This new regulation covered both mortgage suppliers and mortgage brokers. For the suppliers this resulted in increased costs, staffing and some seemingly unnecessary procedures.

However regulation appeared to miss the important larger issues and did not prevent these suppliers from over extending their capital resources, adopting very dubious lending criteria and moving into the sub-prime market in a large way. The resulting chaos, financial loss and damage to the housing market are well known and documented. It also resulted in additional burdens for small mortgage brokers who had added costs and the addition of tedious paperwork and processes. Many also joined “networks” in order to cope with regulation and thus lost their independence and added extra costs.

The regulation of general insurance in 2005 was as a result of a European Directive. As above the implementation of complex and often minor requirements on businesses which were already regulated by the General insurance Council. For insurers, the additional costs appeared to be substantial as firms created new compliance departments to cope with the requirements of the FSA.

Insurance brokers also incurred costs of the new processes and the cost of obtaining advice from the compliance consultancies formed to assist them. The costs of regulation was particularly high for smaller firms hence the increase in small firms combining with larger ones and also moving into Networks. This was often out of necessity rather than desire, particularly for the privately owned broker firms.

ENDS

BRITISH RETAIL CONSORTIUM
for successful and responsible retailing

British Retail Consortium submission to HM Treasury and BIS consultation "A new approach to financial regulation"

The British Retail Consortium (BRC) represents the whole range of retailers including large multiples, department stores and independent shops, selling a wide selection of products through centre of town, out of town, and rural stores, and distance retailers operating both online and via mail order..

At the end of December 2009 the retail sector employed some 2.9 million people (11% of the workforce). The BRC Retail Employment Monitor shows that the sector continues to create new jobs, up 0.6% in Q4 2010. In 2010 retail sales were £293 billion. The retail sector consists of 286,680 outlets, contributing an estimated 8% to Gross Domestic Product.

Summary

The BRC welcomes the opportunity to contribute to the debate over the future of consumer credit regulation in the UK. Unsecured consumer credit is a key feature of retailing and the debate has major implications for retailing and the retail economy.

The BRC fully recognises that, following the announcement on the future of the OFT, the Government's preference is for Option 1 as described in the consultation paper – i.e. the transfer of responsibility to the CPMA, now renamed the Financial Conduct Authority (FCA), and replacement of the Consumer Credit Act (CCA) framework with a FSMA rule book style of regulation.

However, the BRC believes that a number of aspects in the proposals included in Option 1 raise issues of major importance to the retail and retail credit industries, and will have consequences for the retail and consumer economies as a whole. Given the scale of these issues and their potential consequences, BRC members urge the government to address a number of key questions. These include:

- **The lack of an evidence base**. There is limited evidence to support the view that the FCA working on similar principles to the FSA would be a more effective regulator than the OFT has been, either from a market stability or consumer protection point of view. On the contrary, where the consultation paper suggests this will be the case, appears at odds with market experience of the last 10 years.

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- **The lack of accountability.** The proposals do not give adequate accountability of the FCA to Government or Parliament, nor reflect the extent to which its policy and approach will impact the retail economy and retail consumers.

- **The lack of any substantive cost/benefit analysis.** The costs for both Government and business in adopting Option 1 will be very substantial, and all will ultimately have to be passed on to consumers. At a time of fragile economic conditions, when the retail sector in particular is under huge pressure, it is essential that the extent of the consumer detriment (in the shape of increased cost) necessary to introduce these changes is fully understood at the outset. HM Treasury should complete a more comprehensive analysis than the existing impact assessment, that takes into account existing retail investment in to recent regulatory change.

- **Lack of a clear picture of the intended market consequences.** There is no attempt in the paper to paint a picture of the intended economic and market results of the proposals, whether in terms of competition, market participants, availability of credit, financial exclusion or international competitiveness. Given the scale of the changes and their significance for retail as a whole, it is critical that the government sets out its vision of the market characteristics it wishes to create through these proposals, not least so that through the consultation industry can help to avoid unintended consequences.

- **Acceptance of an increase in costs as inevitable.** The fact that, despite the lack of cost/benefit analysis at this stage, it appears to be acknowledged and regarded as acceptable that costs for firms operating in the consumer credit sector will be substantially higher than is currently the case, both as a one off for transition, and under a more intrusive regulator charged with improved market oversight.

- **Change upon change.** The consumer credit sector has seen constant regulatory change since 2004, with the latest major changes under the Consumer Credit Directive (CCD) only effective from the 1st February 2011. The consultation paper envisages at least another three and a half years of further uncertainty, change and additional costs, plus deployment of capital and resource in regulatory driven projects at the expense of business development ones.

- **No stability for business planning**. Given the scale, breadth and complexity of consumer credit regulation, and the need to accommodate maximum harmonization requirements of the CCD, a complete rewrite of consumer credit regulation within the timescales envisaged appears ambitious. For those BRC members currently considering investment decisions in relation to new systems and products it also introduces a huge element of uncertainty, and makes scoping future requirements a matter of guesswork.

- **Better Regulation**. Clearer demonstration is required that the proposals meet the objectives of the better regulation agenda. The proposals should not limit the scope for future self–regulation and industry codes – which have proved valuable tools for the consumer credit market.

- **Consumer champion remit.** As recognised by the Treasury Select Committee report, the FCA will struggle to act as an effective business regulator if it is intended to be a 'robust consumer champion'.

- **Proportionality and one size fits all.** Unsecured consumer credit is a very different market with very different risk dynamics than the other markets currently regulated by the FSA. The FSA regime under FSMA was designed to regulate an investment and deposit taking market, in which investor assets are potentially at risk, not a credit market in which consumers are borrowers, not investors. Whilst subsequently extended to insurance and secured lending sectors, these are again very different markets from unsecured credit, and particularly retail credit, which typically is low value. Disproportionate regulation will simply impose unnecessary cost, strangle business development and prevent growth, all at a time when the exact opposite is required for the UK economy as a whole.

These concerns are discussed in more detail below.

Unsecured credit regulation: Who and How?

BRC members urge the government to proceed with care. In particular, the government should not feel impelled by its announcement with regard to the future of the OFT to rush into a course of action simply to avoid a potential vacuum. There are 2 separate questions to address. Firstly, *who* will be responsible for regulation of unsecured credit? Secondly, *how* will they regulate unsecured credit?

BRC members strongly believe that the 2 questions can be separated, and that of these 2 questions, the second is by far the most important.

With regard to the question of *who* regulates, the critical qualities for the regulator are:

1. market understanding/experience; and
2. effective accountability to government.

Utilisation of existing experienced staff and knowledge base from the OFT and Trading Standards will be important with regard to the first of these. We comment on the accountability issue below.

With regard to the question of *how* the regulator will regulate, BRC members would urge that, prior to embarking on the major undertaking of a potential rewrite of the whole consumer credit regime, the new regulator takes the time to understand the market.

Asking a new regulator (even if it does transition core staff from the OFT) to rewrite the regulatory framework for a market as complex and diverse as unsecured credit, before it has had chance to fully understand all aspects to the market is a hugely high risk strategy, fraught with the risk of unintended consequences – not least consumer detriment as a result of restricted credit. For this reason, it is critical that there is, sufficient government control over the process via effective accountability, and it is not simply left to a regulator new to its market to formulate the legislative framework.

BRC members would therefore suggest that the Government consider the option of creating an unsecured consumer credit division within the FCA, which would initially work within the existing CCA framework, substituting for the OFT.

This division would rely on the core experience and knowledge base of OFT staff and Trading Standards. Once it has transitioned regulatory responsibility and got to grips with the market it is regulating it may then develop detailed proposals, supported by a firm evidence base and impact/cost-benefit analyses, as to the type of framework best suited to consumer credit. This may extend the timescale for the review process beyond 2014, but would greatly increase the prospects for a successful outcome.

BRC members believe that this option would avoid the risk of a regulatory vacuum; provide increased stability for businesses in the short term; allow for fully informed and costed decision making; reduce the risks of unintended consequences; and substantially increase the chances of improving the regulatory regime in the medium to long term. As an additional factor which should not be underestimated it will also provide greater stability for OFT/FSA staff who will be key to a successful transition.

The remainder of this response is structured as a summary of the significance of credit for the retail sector and the key overarching points for BRC members, followed by detailed responses to those specific questions of most concern or relevance to BRC members.

Key Concerns

1. Significance of credit for BRC members

To put the views in this response into proper context it may be helpful to briefly explain the different ways in which BRC members are impacted by consumer credit in their business models. These include:

- Lenders – retailers who themselves or through separate companies in their group provide credit to their own customers.
- Credit intermediaries – retailers who have arrangements with a bank or finance house which provides their customers with point of sale retail credit, either through fixed sum loans or running account credit.
- Acceptance of credit cards issued by third parties.

There are a number of variants on the second of these models, including storecards, branded credit cards and instalment credit, offered through a variety of affinity and joint venture relationships between banks/finance houses and retailers.

Some BRC members are currently authorised and regulated by the FSA as insurance intermediaries, as well as being licensed by the OFT. Others are not regulated by the FSA.

The availability of accessible and convenient sources of credit is critical to the retail sector. Its importance lies primarily in the retail demand generated via access to credit, and goes far beyond the income or profit generated by the credit products themselves. Any action which restricts access to or convenience of credit will also impact retail demand, and slow consumer spending. There are therefore direct implications for UK economic growth.

Additionally, widespread availability of convenient and secure payment mechanisms is absolutely critical to the continued development of the e-commerce marketplace, particularly for online and mobile transacting. Credit cards and retail credit accounts provide precisely this mechanism, not least for the inherent benefit of connected lender liability that is provided under sections 75 and 75A of the CCA.

By way of illustration of the importance of consumer credit to the retail sector:

- Credit and charge cards were used to make 2 billion purchases in the UK to a value of £139 billion in 2009.
- Amongst retailers with their own lending operations, such as the home shopping companies, it is not untypical for more than 90% of sales to be made using their own credit facilities, with most of the balance using third party credit cards.

2. Accountability for Impact on Retail Economy

Given the significance of credit for the retail sector, any substantive review of the regulation of consumer credit has major implications for the wider retail economy, and, consequently for consumer spending and the UK economy as a whole. Historically the economic and political dimension to credit regulation has been recognised by the clear links between the OFT as regulator and BIS as the accountable government department, with accountable Ministers. Governmental and Parliamentary control was also provided by the fact that all credit regulation was subject to the Parliamentary process, either as primary or secondary legislation.

In the light of the impact that credit regulation may have on the retail economy, it is a major concern that the government's preferred option entails the transfer of responsibility for the formulation, drafting and enforcement of all credit regulation to a regulatory body which has very limited accountability to government. These concerns are even greater when that regulatory body is established with strong consumer protection and consumer champion objectives. BRC members believe that there is a real risk that this will lead to inadequate or no consideration of the economic implications of regulatory measures, with unintended market and economic consequences.

It appears to BRC members that under Option 1 government is delegating responsibility not just for regulatory policy in the field of unsecured consumer credit, but also, because of the integral links between credit and retail spending, responsibility for decisions which will have a major influence on the retail economy. Furthermore, delegation is to a body with no effective accountability, and, as currently proposed, with a strong consumer protection remit.

To illustrate this concern, paragraph 52 of the Impact Assessment cites improved quality of lending and reduced incidences of unsustainable borrowing as desired outputs from improved market oversight. This presumably entails the type of regulation recently seen with the Mortgage Market Review. However, there is no recognition of the economic implications of such regulation. Reduced write offs in retail credit can most easily be achieved by reduced lending to riskier credit sets. But such restriction will exclude customers in those riskier credit sets from one of the few sources of credit available to them. The steps to address these consequences will require political action. Some affected customers may be able to access alternative but more expensive forms of credit from other specialist areas of the regulated sector. Others may feel they have no option other than to deal with the unregulated "loan sharks". Others will try to manage cash flow by juggling outgoings such as utility bills and rent. But some form of governmental action will be required to fill the void left by the removal of credit from riskier, lower demographic groups - for example, will social fund lending schemes be expanded; credit unions expected to plug the gap, or welfare benefits increased?

A key concern with Option 1 as proposed is therefore the lack of government control over and accountability for the economic impacts of consumer credit regulation on the retail economy.

3. Need for clear vision of intended consumer credit landscape and economic impacts

Whilst the 4 primary objectives of the government as set out in the consultation are supported by BRC members, it must be acknowledged that they are very high level. They can be (and no doubt will be) interpreted to mean different things to different people. Drawing on the points made above at 2, BRC members believe that it is critical that if a wholesale review of unsecured consumer credit regulation is to be undertaken, clear policy objectives are formulated at a more granular and economic level, to set out the government's vision of the overall landscape of the UK unsecured credit market, including the retail credit market. Handing responsibility for the formulation of the consumer credit regulatory framework to the FCA without a clearly defined mandate for the desired economic operation of the market would risk creating a market in which conduct of business rules are predicated primarily on consumer protection principles, with insufficient consideration of wider economic outcomes.

There is also a concern that the FCA will take as a starting point its experiences in other markets where it has seen evidence of real consumer detriment and market failure (such as some investment products). Any assumption that principles derived from regulation of those markets would be equally applicable, to the unsecured consumer credit market, (in which the risks for consumers and businesses are very different), would be fundamentally flawed.

For instance, BRC members believe that the government should have an intended position in relation to each of the following issues prior to embarking on any wholesale review:

- Is there a desired outcome in terms of availability or constraint of consumer credit, and therefore consumer spending?
- If consumer lending is restricted, so that some consumers are unable to access credit currently available to them, what alternative provision will be made to assist those consumers?
- Is there an ambition to improve competitiveness of UK lenders and retailers operating cross border into the EU, or is this not a priority?
- Does the government wish to see an increase in competition, with a greater diversity of firms providing credit in the UK, or does it envisage a smaller number of bigger players best able to produce economies of scale and absorb increased regulatory costs?
- Does the government wish to facilitate continued expansion of online and mobile transacting, with a framework designed to maximize the particular characteristics of those channels?

- Is the government prepared to see an increase in the cost of credit being passed on to consumers as the price to be paid for supposedly enhanced consumer protection measures?

4. Need for comprehensive and realistic cost/benefit analysis

Another key concern for BRC members is the cost of the government's preferred Option 1, both in isolation and in relation to the tangible benefits. The impact assessment acknowledges that information on both costs and benefits is very limited, but given the scale of the change and the likely costs, both one off for transition and on an ongoing basis, it is critical that an accurate and realistic analysis is undertaken. For BRC members, increased regulatory or compliance costs will have to be passed on to consumers, and the likely impact in terms of higher credit costs or tightening of lending criteria must be taken into account.

BRC members would ask the government to take into account the fact that for the last 7 years they have been running consumer credit change projects, on a more or less permanent basis, covering: -

- Substantial changes to advertising, pre contract information, agreements and early settlement, from 2004/05;
- Introduction of new post contract information requirements, statements, arrears notices and complaint handling rules, etc, under CCA 2006 – from 06 to 08;
- CCD implementation, from 2008 to 2011 (overlapping parts of CCA 2006 implementation);
- Irresponsible Lending Guidance and Storecard/credit card changes during 2010

These changes have primarily been focused on one of the Government's four objectives, namely consumer protection,

The costs of such projects are substantial. For example, costs reported for the CCA 2006 projects by BRC members range from £900,000 to £1.8m, and for the CCD from £450,000 to £1.7m, depending on factors such as size of business, range and complexity of credit products, etc. These costs do not include the lost opportunity cost of prioritising resource away from business development projects.

Any further major change programmes, with their inevitable costs and diversion of resource, will not be welcome unless they also produce for BRC members real and tangible benefits, which substantially exceed the costs incurred. As yet, there is no firm indication of the proposed cost to business of the new regulatory framework, or what ongoing costs may be required.

5. A substantial increase in regulatory costs, both one off for transition and ongoing

It appears inevitable that direct regulatory and compliance costs will increase substantially for BRC members. For firms which are currently only licensed by the OFT, the costs of regulation are currently relatively low. Whilst the more rigorous licence approval process introduced in April 2007 has increased the work which may be entailed in obtaining or renewing a consumer credit licence as a one off, the 5 yearly licence renewal fee is, as is noted in the consultation, low. Furthermore, under the new indefinite duration regime, once granted or renewed, there is no further work involved in applying for a licence.

BRC members do incur costs in responding to consultations and market studies conducted by the OFT and in handling occasional queries or requests from the OFT. However, as is noted, there is no requirement for routine, ongoing supply of data or market information, as is currently the case with the FSA.

By contrast, for FSA regulated firms, in additional to the annual FSA fee and FSCS levy, there are regular routine reporting requirements.

For BRC members who are regulated by the OFT for credit and also regulated by the FSA as insurance intermediaries, the costs of FSA regulation, including fees, the FSCS levy and regular reporting requirements, are many times the cost of OFT regulation, notwithstanding that their core product offering is credit, and insurance is a much smaller element of their business.

BRC members do not believe that there will be any financial benefits to or cost savings from dealing with a single regulator. On the contrary, they believe there will be a substantial increase in costs. The BRC notes that this view may differ from those of the BBA and FLA as referred to in the consultation paper, but can nevertheless only envisage substantially increased costs for its own members for the following reasons:

- As indicated above, members who are currently regulated by both the OFT and the FSA incur substantially greater costs in respect of their FSA regulated activities, even though in all cases insurance mediation is very much an ancillary activity rather than the core activities of retail and lending. It is difficult to see how extending the high cost FSA style regime (with an even more intrusive approach) to the core credit activities can do anything but entail substantially higher costs.
- Members who are not currently FSA regulated currently only deal with one, relatively low cost regulator. Exchanging this for a higher cost regulator can only lead to increased costs.
- Whilst there may only be one regulator, and the FCA has yet to consider how to organise itself internally, given the need for specialist market understanding and the lack of experience in the FSA of unsecured consumer credit, there must be at least a real possibility that supervision of credit

activities within the FCA will be handled by different teams than for other products. If this is the case, there is a likelihood that any avoidance of duplication is more theoretical than real, and that actual duplication will be seen between internal areas of the FCA rather than between different regulators.

- BRC members do not expect that, with a regime intended to be more intrusive, based on flexible rule making and increased market oversight, there will be any reduction in the amount of consultations and market studies relevant to the credit sector. In fact, given the required governance procedures around rule making and the intention that credit regulation will be updated more regularly and fluidly than has previously been the case, the level of input into consultations and responses is likely to raise sharply. Rather than avoid duplication, BRC members expect that the result of Option 1 will simply be that the costs and obligations will rise and intensify under the FCA - it will just be a different regulator imposing them.
- The proposal that existing CCA licence holders will not be grandfathered and will have to apply for new licences or permissions (even if already holding Part IV permissions for other activities) seems to be wholly inconsistent with the theory of cost savings via avoidance of duplication. This entails not only duplication of FSA/FCA authorisation processes, but also adding a third requirement to the existing FSA/OFT authorisation process. The costs and implications for businesses should their authorisation process not be seamless, would be catastrophic.

6. Will the retail credit sector be forced to contribute to the FSCS levy?

Another major concern on costs is the possibility that BRC members, under FCA regulation, will be forced to contribute to the FSCS levy. Those members who are FSA regulated as insurance intermediaries have already seen very substantial increases in the cost of the levy over the last 3 years, it would not be fair or appropriate to require a contribution from firms who engage only in credit activities, or to base a levy on the scale of their credit activities. This would entail forcing low risk credit providers to subsidise costs of failure of high risk deposit takers and investment firms. The consultation paper is silent on this point, and does not consider this as part of the impact assessment, but this question is a key one for BRC members and for the vast majority of smaller firms, many of whom could be forced out of the market by the FSCS levy.

7. Approach to Certainty and Flexibility

It is the view of BRC members that since the CCA came into force in 1985, an overall assessment is that the consumer credit market has been relatively stable, and that there is little, if any, evidence of systemic or widespread consumer detriment. Generally the markets have worked well. As an example of evidence to support this view in the context of particular sectors we would refer to the conclusions of the recent OFT High Cost Credit Review. By contrast, it is generally accepted that the FSA regime established by FSMA has experienced a number of substantial market failures and of instances of alleged misselling and widespread consumer detriment.

Whilst recognising that the government's preferred option is to adopt the FSMA style approach to regulation of credit markets, BRC members would nevertheless wish to query the evidential basis that suggests this is a more effective approach. This conclusion would seem somewhat at odds past experience and evidence.

Further doubt is cast on this by the recent comments from the FSA regard to the validity and effectiveness of its principles based approach, and canvassing the possibility of a return to a more rules based approach. A lack of clarity as to which approach the regulator believes is appropriate, and as to which it will adopt under the guise of the FCA, does not assist firms in planning for the future.

Whilst BRC members agree that the inflexibility inherent in primary and secondary legislation can on occasions be a drawback to the existing CCA mechanism, overall they would prefer the certainty that this brings to the uncertainty and scope for "regulation by hindsight" entailed in the FSA's current approach to regulation.

BRC members believe that the approaches adopted by the OFT in drawing up the Irresponsible Lending Guidance via a constructive consultation process with consumer and industry bodies, and in introducing the storecard and credit card package via self regulatory agreement, are both good examples of how an effective balance can be struck between certainty and flexibility within the context of a legislative framework, as opposed to a rule book based regime.

8. Regulation must be proportionate and designed to reflect the whole Market

BRC members have a concern that too much of the FCA debate is underpinned, either consciously or unconsciously, by considerations and assumptions which may be applicable to banks, but which do not adequately reflect the breadth of different types of lenders and ancillary businesses in the consumer credit market. This raises major issues of proportionality. Measures which may regarded as being appropriate for a loan of £25,000 will not necessarily be proportionate for a retail loan of £250 or a retail account with a credit limit of £250. At low levels of credit, any increase in costs which have to be passed on have a disproportionate affect on the cost of credit, and therefore on the borrower. Any new regime must be designed to be proportionate to each aspect of the market it regulates, which in the case of retail credit means typically low value, convenient sources of credit, a significant proportion of which is provided to consumers in lower demographic groups, who do not necessarily have easy access to other forms of credit.

BRC members concerns as to proportionality are increased by the extent to which the proposals emphasise the need for enhanced consumer protection, and the role of the FCA as an intrusive, powerful regulator with a consumer champion remit. However, the paper provides no evidence to suggest that enhanced consumer protection is needed, or will provide benefits. What is the widespread consumer detriment that will be addressed by the new framework, ultimately at greater cost to the consumer?

BRC Response to Specific Consultation Questions

Chapter 1

1. **Assessment of the consumer credit market; and**
2. **Assessment of problems caused by way in which credit is regulated, and split in responsibility for regulation of retail financial services**

BRC members believe that the analysis of the consumer credit market overstates the supposed difficulties caused by the division of regulatory responsibility between 2 regulators. BRC members agree that, were we starting from scratch on a cost neutral position, the more logical approach would be to have a single regulator and a single regulatory approach. However, we are not in such a position – all OFT regulated firms have invested heavily in systems, controls, products, staff training and processes designed specifically to comply with a detailed framework for regulation of credit that has applied since 1985. A significant part of this cost has been incurred in the last 7 years complying with major changes to legislation entailed in the changes to advertising, agreements, pre contract information and early settlement in 2004/05; the extensive informational requirements and other changes in the CCA 2006, and then the CCD.

BRC members believe that the difficulties stated to be created by the split in regulators are more theoretical than real, and believe there is very limited evidence of them causing actual consumer detriment or market instability. For instance, whilst there are several references to the anomaly of a current account fluctuating between regimes as it moves between debt and credit, and to flexible mortgages, is there any evidence that this has caused significant issues or concerns in practice? In any event, bank current accounts have always been treated as an exceptional case with their own set of partial exemptions under the CCA, and this approach has also been adopted by the CCD. It would not seem appropriate to take a product which is already treated as being in a partially exempt category, and therefore in a different way to mainstream consumer credit products, as a key justification for such a complete review of the consumer credit framework. Similarly, the example quoted of a lump sum

PPI premium financed by credit is now redundant since the FSA took action to effectively prohibit the selling of single premium PPI.

BRC members agree that overall market oversight can be improved, but believe that this should be equally achievable through effective coordination and working between regulators as through a single regulator, which will inevitably have to coordinate its own internal departments to achieve this in any event.

As noted above, BRC members believe that the benefits of avoiding duplication of regulation are overstated, and that in practice the regulatory burden will increase if a FSMA style authorisation regime and approach to supervision is extended to their credit activities. (See Key Concerns point 5).

BRC members also agree that the different accountabilities of the FSA and the OFT, with the Financial Ombudsman Service also in the mix, is not ideal. However, for the reasons noted above, BRC members do not believe it is appropriate to address this by moving all responsibility to the FCA, with no direct or effective accountability into government.

BRC members also agree that the primary and secondary legislative framework of the CCA regime does not lend itself to easy amendment. However, on the other hand, it does create a degree of certainty and stability, with all changes requiring a proper consultative process, and allowing time for firms to prepare for implementation. The FSMA style process, by contrast, lends itself to easy amendment, but at the cost of certainty. Its informality can also lead to a lack of appropriate consultation. For instance, the FSA attempted to limit the consultation period on CP09/23 on assessment and redress of PPI complaints to a 4 week period instead of the usual 12, until forced to review its position by the strength of industry response. Additionally, the FSA has adopted an approach of regulation via open letters, and even, on occasions, by speeches. The FSA regularly refers to speeches by its senior officials, and expects all firms to be aware of them and take their content into account. There is no consultation process for informal approaches to regulation such as open letters and speeches.

BRC members would generally prefer certainty and stability to uncertainty and regular change, not least because change always has a cost. Whoever the regulator, BRC members would wish to see clarity, stability and certainty as cornerstones of the framework, with full consultation processes for all changes, adequate timelines for implementation of changes, and no retrospectivity or regulation by hindsight, as can be the risk with a broad principles based approach based on the current FSMA framework.

As cited above, BRC members believe that the ILG and the storecard/credit card package are examples of effective mechanisms for introducing flexibility into the CCA framework, without sacrificing certainty or stability.

BRC members would also wish to see a governmental accountability process built into the rule making mechanism of the FCA. It is in no-ones' interest for the only effective check to be a judicial review process, given the time, cost and uncertainty entailed in that process – however, this has been the only route available to the BBA in connection with the FSA's new rules on PPI complaint handling.

3. Types of risks faced by consumers in credit markets; key consumer protection provisions; incidence of regulatory burdens or duplications and inconsistent regulation of different types of business

Overall, BRC members believe that the OFT has correctly identified the high risk areas in consumer credit markets as being debt collection, debt adjustment, debt counselling and credit information services, as reflected in its approach to credit competence assessment on licence applications. In particular, BRC members fully support the view of the OFT that the activities of claims management companies (CMCs) and debt management companies are high risk. Their potential for consumer detriment is significant, and BRC members ask that the position of those firms in the new regime is given particular consideration.

On specific consumer protection measures, BRC members believe they are those contained in the CCD, s75 CCA, Consumer Protection from Unfair Trading Regulations, Unfair Contract Terms Regulations and the OFT Irresponsible Lending Guidance. As mentioned above, some form of connected lender liability, whilst perhaps not popular with all industry sectors, is viewed by BRC members as key element in ensuring high levels of consumer confidence when transacting with retailers, especially by distance means such as online or mobile transactions.

However, BRC members believe that it is time to review the specific issue of unenforceability of agreements as a sanction for technical breaches. As noted by the OFT, the last 4 years have seen a huge growth in CMCs abusing this sanction so as to earn fees by encouraging consumers to evade genuine debts. In many cases, to the concern of the OFT, this has involved CMCs in misleading consumers as to the extent of their rights and as to the consequences of not paying. The arguments run by the CMCs have often been creative and tenuous, and lenders have been forced to spend considerable sums in defending the claims. The availability of FOS and the threat of a £500 non refundable fee for the lender regardless of outcome has also been a factor in the development of this industry. In the light of the various well documented court decisions in favour of the credit industry arguments on issues of enforceability BRC members consider that, if a review is carried out as per Option 1, the question of whether unenforceability is an appropriate sanction should be within its scope.

BRC members would also observe that, for substantial benefits to be seen for them from any major review so as to justify the cost, they are most likely to come from the abolition of the sanction of unenforceability (both prospectively and on existing agreements), and from a review of the FOS system and fee structure. With typical balances of circa £400, BRC members feel particularly vulnerable to the tactic of threats of a FOS referral – for the majority of their accounts it is more cost effective to settle the claim, regardless of merit, than to successfully defend the claim and pay the FOS fee. This is fundamentally unjust Furthermore, the FOS practice of charging the £500 fee even on cases which fall outside their jurisdiction, is another grossly unfair practice.

BRC members would therefore regard abolition of unenforceability of agreements, and reform of the FOS fee structure and charging process as potentially involving the quantum of benefits which may justify the costs of further changes to consumer credit regulation.

The position of BRC members on duplication is described at Key Concerns point 5 above.

4. Are the 4 stated objectives for reform of consumer credit appropriate and attainable?

As indicated at Key Concerns point 3 above, BRC members support the 4 key policy objectives, but are concerned that they have been formulated at a very high level, with no granularity as to what they mean for the desired dynamics of the consumer credit market and, (of concern to BRC members) for the retail credit market and retail economy. BRC members believe that this policy formulation should come from government, not the FCA. In particular, whilst the consultation paper provides some discussion on the objectives of clarity, coherence and market oversight and on effective consumer protection, it is very light on discussion on simplification and deregulation, and on proportionality and cost effectiveness.

BRC members have particular doubts as to the attainability of the 3rd and 4th objectives under a FSMA style regime, particularly if operated by a regulator with a strong consumer champion remit.

Whilst the current consumer credit regime is undoubtedly complex, with a number of unnecessary and disproportionate aspects which various sectors would prefer to see removed, a number of the bigger concerns have been removed by a combination of the CCD and the recent chain of authoritative court decisions in claims brought by CMCs. BRC members would not wish to see these avenues reopened to CMCs.

Unless a radical approach is taken, such as repealing all UK consumer credit legislation and replacing it with a simple implementation of the CCD, with no gold-plating, BRC members are doubtful as to how much deregulation will be achieved by a consumer champion regulator. Experience suggests that deregulation and simplification is invariably perceived as a weakening of consumer protection, particularly in the financial services sector. Given the commitment in the consultation paper that there will be no lessening of overall standards of consumer protection (and indeed it is likely to increase), BRC members believe it is unlikely that any significant (or any at all) deregulation will be achieved under the FCA.

Additionally, the FSA Handbook is widely regarded as being highly complex, technical, circular and generally immensely user-unfriendly. Anyone familiar with it could be forgiven for doubting whether the introduction of a similar approach for credit will simplify or deregulate the current regime.

BRC members would therefore wish to scrutinize closely any cost reductions claimed for simplification and deregulation in the cost benefit analysis.

BRC members concerns as to the substantial increase in costs entailed in extending a FSMA style regime to their core credit activities are documented above in Key Concerns, including the particular concern over extending the FSCS levy to consumer credit firms. As it seems to be accepted that costs of compliance will increase, the concern is that they will inevitably be less proportionate than they are under the current regime. For lenders amongst BRC members, customers typically have relatively low balances (an average balance of <£400 would be typical), and are in the C to E demographics. Proportionately an increase in costs passed on to them will therefore potentially have a bigger impact and be more difficult to absorb than for some other customer groups in other sectors**.**

Any increase in costs, particularly in the current fragile economic climate, with both consumers and businesses feeling economic pressures and lacking confidence, must inevitably carry a risk of market exit for some businesses, and therefore of reduced competition, reduced availability of credit and potentially increased financial exclusion.

Chapter 2

5. Impact of a unified regime for clarity, coherence and improved market oversight

See response to Questions 1 and 2.

6. The role of institutions other than the OFT in current consumer credit regime

BRC members believe that Trading Standards and the specialist Illegal Money Lending Unit can and do play a valuable role in consumer credit regulation.

The Illegal Money Lending Unit provides a particularly valuable service, as it targets the area where there is the most consumer harm. However, its resources and coverage are limited. BRC members would welcome increased resource and focus on this area, and the question of how the FCA would tackle this area is a key one for Option 1. Taking practical and effective action against unauthorised loan sharks requires very specialist skill sets and experience.

Trading Standards Departments can provide a valuable source of advice and guidance, particularly for smaller firms with limited access to compliance or legal resource. They can also provide a highly cost effective mechanism for addressing issues at a local level, on a relationship basis. Differing levels of resource, expertise, and competing priorities will inevitably mean that there are degrees of inconsistency between different local authorities, but overall BRC members believe there is real value in a relationship at local level with a primary or home authority.

Given the lack of clarity as to the overall future regulatory landscape it is difficult to comment at this stage on questions such as: how the FCA would interact with Trading Standards under Option 1; how this would relate to any possible central coordinating body for Trading Standards or wider consumer protection issues; and how firms can continue to operate with a relationship with local Trading Standards. However, these must all be considered as the various dependencies progress.

7. How may the overall level of consumer protection best be retained or enhanced?

BRC members concerns as to the extent to which this aim may create obstacles for the overriding objective of simplification and deregulation are set out in the response to Question 4 above.

BRC members believe that if this aim is to be reconciled with the overriding objective of deregulation, an evidence based approach to the targeting of specific consumer protection measures is essential. The consultation paper refers in numerous places to the need to strengthen consumer protection in consumer credit markets, and for the FCA to be more intrusive and a stronger consumer champion than the FSA. However, whilst this may provide strong political sound-bites, it is not a basis for an effective regulatory regime unless there is evidence of the actual consumer detriment to be addressed. Whilst in any market there will be individual instances of bad practice, abuse and consumer detriment, individual or relatively isolated instances do not form a sound basis for good regulation. The BRC would be interested to understand in greater detail the body of evidence of consumer detriment justifying the cost of the suggested change.

BRC members therefore believe that evidence of significant customer detriment or hardship should be identified to support any proposals to enhance consumer protection measures. This is consistent with the recommendations of the OFT

High Cost Credit Review to the effect that further regulation or government action must be based on hard evidence.

BRC members would reiterate the views in response to Question 3 above with regard to the opportunity to review the sanction of unenforceability, and are pleased that this is already in the government's thinking. BRC members would note that removing this sanction will arguably reduce consumer detriment and increase consumer protection by providing a disincentive to the CMCs, many of whom have been heavily criticised by both the OFT and Ministry of Justice for the risk they can pose for consumers.

Given the unfair credit relationship provisions in the CCA, it is also arguable that the unenforceability sanction is no longer necessary, as the courts have virtually unfettered discretion to make whatever order they feel is appropriate. If FOS is to remain as an out of court dispute resolution mechanism, adjudicating cases taking account of the law, the unfair credit transaction provisions (which have now received considerable judicial interpretation) also provide a full remedy.

As is noted in the consultation, the consumer redress schemes under S404 FSMA, for which safeguards already exist, provide a powerful sanction. If this regime is extended to consumer credit, there can be no argument that the overall level of consumer protection has been reduced.

It is critical that the debate on levels of consumer protection focuses on the need for proportionality. In particular, it must reflect the fact that the risks for consumers in the unsecured credit market are very different from those in other markets regulated by the FSA, such as deposit taking, investments, insurance and secured lending. In particular, consumers are not at risk of losing assets in the same way as in those other sectors. Applying consumer protection measures developed for other sectors to the unsecured credit market risks applying a disproportionate and inappropriate level of regulation.

8. SMEs and Business Lending

BRC members do not typically lend to SMEs or businesses, and have no comment.

9. Increased Flexibility of a rules based regime

See comments in Key Concerns point 7 above.

10. Impact of a FSMA style supervisory approach for effective consumer protection

See comments in response to Questions 1 and 2 above.

11. Synergies under current regime in tackling problems associated with the sale of goods and services on credit, and how to retain them in the new regime

Other than under the connected lender liability provisions of sections 75 and 75A CCA, BRC members are not aware of evidence of particular issues or problems associated with the sale of goods or services on credit, and do not regard there as being great synergies under the current regime. Clearly, the OFT currently has wide consumer protection powers to act on non credit related issues, but BRC members are not aware of particular instances when the OFT has taken action against retailers in respect of the retail transaction, and also acted in relation to a related credit agreement. BRC members believe that the position should be reasonably clear and simple, in that if a customer has a remedy against a retailer in a transaction falling within S75 or 75A then the matter will potentially fall within the remit of the FCA, but if it is purely a matter between the customer and the retailer and not covered by S75 or 75A, then the matter will not be within the remit of the FCA, and will fall to be handled by Trading Standards, as it would, for instance, if the purchase was made using a debit card from a current account with a credit balance.

By contrast, hire purchase, conditional sale or credit sale transactions combine both sale of goods and provision of credit in a single agreement, and rental or leasing agreements entail similar structures. Currently the OFT would clearly consider all aspects of such agreements. Attempting to split out components of a single agreement would be highly artificial. BRC members would envisage that agreements of this type would fall wholly within the remit of the FCA under Option 1.

There are many businesses other than retailers for whom credit related activities are not their sole or main activity, and where conduct in other aspects of their business may be relevant. Credit brokers are an obvious example. The extent to which the OFT has been forced to take action against the providers of "ancillary credit services", particularly brokers, debt management companies, debt collection agencies and claims management companies, vividly illustrates the fact that any new regime must cater for a much wider range of businesses than simply lenders

Given that this question is of particular relevance to BRC members, they would welcome the opportunity to discuss any particular issues or evidence of specific problems which the government had in mind in formulating this question.

12. Will transferring credit regulation to the FCA under a FSMA style regulation support the government's 4 key objectives?

See comments above.

13. Other advantages or disadvantages in transferring credit regulation to sit alongside other financial services regulation

See comments in Key Concerns above.

14. Are there specific issues which should be addressed in assessing merits of Option 1, and how can they be addressed?

See comments in Key Concerns above

15. If Option 1 is not preferred, what are the key points in determining the most appropriate regulatory authority?

If Option 1 is discounted the other options for a regulatory authority would appear to be:

- Retain the credit functions of the OFT in a different guise, as a new regulator dedicated to unsecured consumer credit, operating within the existing CCA framework, but with stronger relationships/concordats with the FCA to improve market oversight.
- Devolution of responsibility to Trading Standards, perhaps with a centralised coordination body.
- Transfer consumer credit regulation to a separate department of the FCA, operating within the existing CCA framework, and therefore following a different regulatory approach to other departments of the FCA. Market oversight on all retail financial services should improve provided appropriate internal processes are implemented.

Key factors should be the need for experience and understanding of the market, the cost and benefits for industry and consumers, and the proportionality of the regime.

Of these, BRC members believe that by far the best option would be the third, for the reasons set out in the summary. This would include a remit for the consumer credit division of the FCA to develop a detailed and fully costed proposal for the simplification and improvement of the regulation of credit in the medium term, once the new regulator has gained experience of its market.

<u>Chapter 3</u>

16. The suitability of FSMA style regime to different types of consumer credit business

See comments in Key Concerns point 8 for concerns as to the application of a FSMA style regime to retail credit.

17. Can statutory processes relating to rule making; a risk based approach; and differentiated fee mechanisms provide mechanisms for ensuring a proportionate approach is taken to consumer credit under a FSMA style regime?

See comments at Key Concerns above. BRC members believe that each of these factors can help in assisting with the development of a proportionate approach to consumer credit, but nevertheless have a number of concerns. Specifically:

- Statutory processes relating to rule making are essential, as is accountability to government, and appropriate checks and balances should the FCA not follow the processes. It is in no one's interests (particularly consumers) for the only effective check to be an application to the High Court for judicial review, as has been the case with the BBA's application in respect of the FSA's rule changes on PPI.
- BRC members would agree with the theory of a risk based approach, with lighter touch regulation for low risk areas. In practice, the value of this will depend on the process of risk evaluation – what will be regarded as low risk by the FCA, and to what extent will this be based on hard evidence?
- Whatever the fee mechanisms, it appears inevitable that costs of regulation will increase substantially. Unless there are compensating tangible gains or benefits (for industry and consumer), the cost of the new regime will be less proportionate than the current OFT regime.

18. Views on factors to be assessed in considering fee arrangements for consumer credit firms

The OFT has only recently consulted on fee arrangements for consumer credit licences, and the factors considered in responses to that consultation are equally applicable. Given the small size of many licence holders, and the small amount of the current fees, it is inevitable that any substantial increase will have a major impact on the economic viability of many firms, particularly credit brokers.

19. Evidence on experiences with Appointed Representative Regime; views on how it might be applied to consumer credit; how may different business models and networks adapt to such an approach; implications of an AR regime for businesses and consumers

BRC members regard this as potentially a key issue, which must be fully understood, as, if adopted, it will play a big part in dictating the future shape of the market.

At a high level, if the FCA is to adopt the approach to enforcement and sanctions seen from the FSA in the last 2 years, most regulated firms will be very reluctant to take on responsibility for "policing" appointed representatives. The increasing emphasis of the FSA on personal accountability of approved persons, (with attendant career destroying consequences); the size of penalties being levied; the disproportionate costs and business disruption of S166 "skilled persons" reviews; and the most recent developments in PS 11/3 of publication of proceedings before their outcome is known, are all examples of what has become a disproportionately onerous regime. There are now reports of firms struggling to appoint people into approved persons roles because of the reluctance of staff to take on such a high degree of personal risk.

Against this background, it is unlikely that firms will be willing to accept responsibility for other businesses beyond their direct management control unless it is unavoidable in the context of their business model.

They will also be unwilling to take on such a responsibility unless there are tight controls in place.

It seems inevitable that this will lead to a contraction of the marketplace. Any business for whom credit related activities are not absolutely core, with sophisticated systems and controls to reflect this, representing too great a risk to be acceptable as an appointed representative.

For lenders whose business models depend on introductions from brokers and who therefore are forced to adopt this model, the consequences will be a substantial increase in costs from putting in place compliance monitoring and audit processes in relation to their approved persons. These costs will have to be passed to consumers.

For BRC members who operate as lenders, their key relationships are generally intra group, and therefore generally easily controlled. Some already operate intra group appointed representative arrangements for insurance mediation. These lenders would however be generally be unwilling to accept responsibility for third parties (for the reasons described above), which will limit opportunities to expand product types and new business initiatives.

However, of much bigger concern is the impact on retailers if their joint venture/affiliate lender partners are unwilling to accept regulatory responsibility for the activities of retail staff, who, in the context of major retailers, will be operating from many locations across the UK. Putting in place sufficiently robust controls to be able to **evidence** to the FCA after the event that all customer contacts have been conducted compliantly is an extremely onerous task. Whilst retailers and their associated lenders would undoubtedly try to explore options for controlling the risks to acceptable levels, it seems likely that there will be impacts on point of sale credit, either in terms of availability, customer experience or convenience. This would consequently have an impact on retail sales.

It is not possible at this stage to predict the full consequences with any certainty, but the BRC believes that the adoption of an appointed representative style framework under which lenders would be required to take responsibility for the conduct of retailers whose goods and services they are financing would have major implications for the provision of point of sale credit by retailers, whether on store cards, affinity credit cards, hire purchase and credit sale facilities, or loans. Any impact on credit will also impact retail sales. Given the implications for retailers, BRC members would welcome the opportunity to work with government to develop thinking on the impact of an appointed representative style regime.

Sectors which would be similarly affected are those in which credit is a key part of the purchase decision. The most obvious is the motor vehicle retailing industry, but any area in which instalment finance plays a significant part will be impacted, particularly those in which the broker is introducing customers to credit providers in a very ancillary capacity, such as travel agents or vets introducing payment plans for insurance policies, or private schools or golf clubs offering instalment plans for annual fees.

20. Group Licensing

No comments.

21. Self Regulatory Codes

The BRC does not issue codes of practice for its members. Its members believe that there are advantages and disadvantages of codes of practice. In a principles based regime, in which certainty is not always present, they can provide a useful "safe harbour", if treated by the regulator as being statements of good practice – i.e. compliance with the code will be treated as evidence of compliance with regulation. However, they also carry a risk of regulatory creep, if they are taken as being standards which may apply to firms which are not subscribers to the code, or to sectors other than the one for which they were designed. This is particularly the case if FOS attempt to argue (as has occurred on occasions), that, for instance, provisions of the Lending Code apply to a retail credit provider which is neither a bank nor a credit card issuer, and which has had no involvement in the formulation of the Lending Code, is not a subscriber to the code, and does not apply the code in its business.

22. Is there a case for deregulation of certain categories of consumer credit activity?

In the case of retail credit, BRC members have previously argued for the exemptions under the CCD to apply in the UK. This approach was consistent with the recent government announcement on the change of approach to implementation of EU Directives, avoiding gold plating of EU legislation. BRC members would therefore argue again that the small agreement exemption be increased from £50 to the equivalent of €200, and that credit with no interest or charges be exempt, or at least subject to lighter touch regulation.

23. Are there other ways in which a FSMA style regime might be designed to be proportionate and effective?

No additional comments.

<u>Chapter 4</u>

24. How should existing agreements be treated?

BRC members believe that this question cannot be answered until the extent of the substantive differences between the two regimes is established. If the CCA is rewritten in rule book form, but with little substantive change, there will be much fewer issues from a transitional point of view than if there are wholesale changes to consumer credit law.

Key considerations are certainty, cost and avoidance of adverse retrospective effect. The impact on securitizations and debt sales, for which the financial parameters and prices will have been set, previously needs to be considered. Lessons should be learned from the transfer of second charge lending to the FSA.

25. How should existing licensees be dealt with and what factors need to be considered in deciding whether a modified approach should be adopted for particular categories of firms?

BRC members are concerned that, despite the introduction of an enhanced due diligence process on licence renewal associated with the change to indefinite licence periods, it is now proposed that there will be no grandfathering of existing licence holders, whether or not they also hold existing permissions under Part IV FSMA. BRC members consider that the cost for both firms and the FCA of a wholly new licence application process is disproportionate. Additionally, the sheer logistics for the FCA of processing the number of licence applications that will be required makes this proposal unworkable. Any firm whose application has not been fully processed and approved by "go live" day will be in an invidious position as far as both its customers and its funders go. Lenders whose applications are still outstanding are unlikely to be able to obtain funding for new lending, or to agree sales of debt. This will put huge pressure on the FCA to ensure all licences applications are approved, and given the volumes this just does not appear practicable. Failure by the FCA to process applications in time will potentially have business failure consequences for the firms involved, with the consequent likelihood of litigation ensuing.

BRC members would therefore urge the government to implement a grandfathering process for existing licence holders.

Consideration should also be given as to whether it is really necessary for each separate legal entity in a corporate group to have to apply individually for separate licences, as is currently the case. Where the entities essentially share systems and controls there appears little value in assessing each application on a standalone basis.

26. Factors to consider in transitioning from one fee structure to another

Given the expectation that fees will rise, sufficient time should be allowed for small firms to be able to budget for the increased fees. For small businesses, any significant increase should be staged to lessen the cash flow impact. There is also the question of whether those firms part way through a current OFT 5 year credit licence will receive a pro rata credit

27. Other factors to be taken into account in considering transitional arrangements

BRC members would stress the importance of certainty and clarity. Any firm whose OFT licence is due for renewal over the next 2 or 3 years wishes to know who they will be applying to and what the process and criteria will be. It is absolutely critical that the government avoids creating an environment in which wholesale funders, financial backers and suppliers to credit industry businesses begin to question whether a licence will be granted, as this would undermine confidence, destabilize firms and potentially have a catastrophic effect on the market.

For this reason we would reiterate the point that continuity under a form of grandfathering is essential.

28. Evidence in relation to previous transitions, such as extension of FSMA jurisdiction to mortgage and insurance markets?

The BRC has no direct evidence, but would recommend that data from the FSA on the numbers and sizes of firms offering insurance mediation (especially small firms offering low value products as an

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A New Approach to Financial Regulation:
consultation on reforming the consumer credit regime

HM Treasury and the Department for Business, Innovation & Skills

Response by the Building Societies Association

Introduction

1. The Building Societies Association (BSA) represents mutual lenders and deposit takers in the UK including all 48 UK building societies. Mutual lenders and deposit takers have total assets of over £365 billion and, together with their subsidiaries, hold residential mortgages of almost £235 billion, 19% of the total outstanding in the UK. They hold more than £245 billion of retail deposits, accounting for 22% of all such deposits in the UK. Mutual deposit takers account for about 36% of cash ISA balances. They employ approximately 50,000 full and part-time staff and operate through approximately 2,000 branches.

2. The BSA responded in detail to HM Treasury"s 2010 consultation *A New Approach to Financial Regulation: Judgment, Focus and Stability* www.bsa.org.uk/policy/response/hm_treasury_newapproach_fin_reg.htm; is currently examining the more recent Treasury paper - *Building a Stronger System*; and welcomes the opportunity to comment on the latest consultation concerning regulatory reform - *Reforming the Consumer Credit Regime* (the CP).

Key Points

3. In view of the inefficiencies of, and significant overlap between, the roles of two regulators (as identified in chapter 1 of the CP), the BSA"s long-held position has been that the Government should investigate whether or not the OFT's consumer credit functions should be passed to the FSA; see - www.bsa.org.uk/printerfriendly.htm?art=/policy/response/dberr.htm.

4. This implies no criticism of the OFT, which has primary responsibility for the regulation of consumer credit, but simply recognises the difficulty of having a multiplicity of regulators with overlapping roles. Therefore, we welcome the examination of the problem in the CP and, in principle, favour the proposal to transfer regulatory responsibility for consumer credit from the OFT to the Financial Conduct Authority (FCA). However, there are two significant practical qualifications to this point of principle.

5. First, there are many detailed considerations in relation to the possible migration of the supervision of consumer credit from one regulator to another. The CP, especially chapter 3, helpfully addresses these matters and the BSA sets out its views below. We welcome the recognition, set out in chapter 4, of the scale of the

proposed exercise – which should not be underestimated - and the commitment to further extensive engagement and consultation.

6. Second, until the FCA is fully operational, we cannot know how effective it will be. Therefore, the fundamental question asks whether a regulatory role should migrate from a long-established regulator to one that will not be operational for some time – for obvious reasons, this is by no means an easy question to answer. In this context, the BSA envisages difficulties for the future operation and effectiveness of the FCA if it is established as a "consumer champion" without this characterisation being balanced by a statutory requirement upon the FCA to conduct its business in a fair and impartial manner. The BSA explained its misgivings, which we understand to be shared throughout the financial services industry, in detail in its response to HM Treasury"s 2010 consultation (see above). The House of Commons Treasury Committee described the description as "inappropriate, confusing and potentially dangerous". We agree with the Committee.

7. While the more recent consultation paper, *Building a Stronger System*, provided some reassurance, we believe that it is very important that a statutory duty be placed on the FCA to conduct its business in a fair and impartial manner. Since HM Treasury has confirmed (in *Building a Stronger System*) that "the FCA will be an entirely impartial regulator from whom firms and consumers can expect fair treatment", we cannot envisage reasonable objection to the placing of this principle on a statutory footing.

8. Regarding the options for dealing with the consumer credit legislation under the FCA, the BSA questions how practicable it would be to repeal the legislation, reassemble it, and transfer its provisions to the Regulator"s Handbook of Rules and guidance, at the same time as much wider regulatory regime change. While we understand the arguments favouring the proposal, certain factors militate against it, as follows –

- after the upheaval over 5 or 6 years in consumer credit laws, all concerned would benefit from a period of calm and consolidation, rather than further disruption

- it would expect a great deal of a new regulator, during its initial period of consolidation, to take on such a major, complicated piece of additional work

- the Regulatory Policy Committee has described the analysis of potential costs and benefits of the proposed change as "incomplete"

- there appear to be legal obstacles to taking this route in view of the fact that the Directive is one of maximum harmonisation

- the approach would seem to be inconsistent with the Government's recent pledge against 'gold-plating' EU law.

9. If the final decision is that the UK legislation will be repealed, an alternative to the proposal in the CP would be to copy the EU Consumer Credit Directive into the Handbook, with necessary cosmetic changes to make the text suitable for the new vehicle, but with no substantive amendment. This would be a simpler option and one that would be consistent with the Government"s recent pledge not to „gold-plate" EU law. However, in any examination of this approach, there would have to be a consideration of the balance between the benefits to consumers deriving from the

simpler EU arrangements and the loss of certain protections currently enshrined in UK law.

Questions

Chapter 1: The case for reform of the consumer credit regime

1. Do you agree with this assessment of the consumer credit market?

10. The analysis of the market in paragraphs 1.8-1.9 is fair. The fact that it is a market where almost £131billion was lent in the first nine months of last year sets in context the data regarding market difficulties (set out in paragraph 1.9). That data would appear to owe more to the current recession than to any major disfunctionalities in the market or in its regulation.

11. The BSA agrees in principle with the assessment in paragraph 1.17 of the CP that "for the market as a whole, no one organisation is clearly accountable for performance against a set of clear statutory objectives". In principle, it is inevitably inefficient when responsibility for one business sector is spilt among a number of authorities. As the CP further states, such a split in responsibilities can lead to difficulties in taking a strategic view, confusion, duplication, lack of flexibility and deterrent to regulation. In principle, regulation would be improved if it was the sole responsibility of one regulator.

12. It is worth noting that, as long ago as 2005, the Hampton Review suggested that the consumer credit functions of the OFT might pass to the Financial Services Authority (paragraph 4.50). Indeed, the Hampton Report recommended, among other things "consolidation in national regulators to create a simpler, more consistent structure" www.hm-treasury.gov.uk/media/7/F/bud05hamptonv1.pdf.

13. The proposed new regulatory framework would mean that many financial services firms had two direct regulators - the Prudential Regulatory Authority (PRA) and the FCA. Subject to the qualifications in paragraphs 5 and 6 above, it is important that, by the time the new regime is in place we do not have a situation where certain firms that provide consumer credit products and services are supervised by *three* separate bodies.

2. Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail financial services?

14. The OFT is responsible for regulating and licensing consumer credit in the UK, but firms that are required to apply for authorisation to the FSA, because their activities fall under Financial Services and Markets Act 2000, may also need to apply to the OFT for a consumer credit licence.

15. The OFT and the FSA have arrangements for co-ordination of their respective regulatory activities www.fsa.gov.uk/pubs/other/OFT_FSA_Actionplan.pdf. The joint FSA/OFT publication *Delivering better regulatory outcomes – May 2008 update*, reported joint regulatory work on all of the following topics, some of which relate to consumer credit –

- personal bank account pricing
- credit card interest calculation

- credit advertising
- the retail distribution review
- PPI
- with-profits funds
- communications with consumers
- the Consumer Credit Act 2006
- mortgage arrears
- sale and rent back
- the Unfair Commercial Practices Directive
- anti-money laundering responsibilities
- the Payment Services Directive.

www.oft.gov.uk/shared_oft/about_oft/oft998.pdf.

16. While, on the one hand, this degree of co-ordination is laudable, the need for such a high level of co-ordinated activity gives rise, on the other hand, to questions about the FSA's single financial regulator status. The BSA made this point in 2008, in its response to BERR‟s *Consumer Law Review: Call for Evidence* www.bsa.org.uk/docs/policy/prudentialandfinreg/consumerlawreview_response.pdf.

3. The Government would welcome further evidence relating to the consumer credit regime, including in particular:

- *the types of risks faced by consumers in consumer credit markets;*
- *key provisions for consumer protection under the current regime and their effectiveness in securing appropriate outcomes for consumers; and*
- *the incidence of regulatory duplications or burdens on firms and/or inconsistent regulation of similar types of business.*

17. We note the list of key provisions for consumer protection under the current regime that is set out in paragraph 2.9, but the effectiveness of the ill-defined 'unfair relationship' test, in comparison to its predecessor (the 'extortionate credit bargain' test) has yet to be fully tested, although we recognise that there has been a certain amount of litigation - www.oft.gov.uk/about-the-oft/legal-powers/legal/cca/CCA2006/unfair/unfair-rel-full/.

18. One of the main problems with the UK‟s consumer credit laws is that they have been subject, over several years, to two major reviews – the changes brought about by the 2006 Act (introduced into Parliament notwithstanding the fact that new EU laws were already in the pipeline) and the significant amendments required by the Consumer Credit Directive. These sets of changes, one following so quickly upon the other, have caused upheaval for consumers, firms and regulators alike. As a result, what was never a simple piece of legislation is now very complicated. Whatever happens regarding the *supervision* of consumer credit, all relevant parties now deserve an extended period of time to allow consolidation of the regulations, before any new *substantive legal changes* are proposed (unless they are of a simple, and deregulatory, nature).

19. Whilst we welcome the Government‟s recent commitment not to „gold plate‟ EU laws, we believe that an equally important step would be for the Government to commit not to introduce new domestic laws if developing EU law, covering the same area, is in the pipeline – a practice sometimes called "front-running". More detailed reasoning is provided at
www.bsa.org.uk/docs/policy/prudentialandfinreg/consumerlawreview_response.pdf

4. Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?

20. We are not equipped to comment on whether any UK regulatory regime is "world class" because that would require a comparison with all corresponding regimes abroad, but the BSA believes that it would be enough to have a regulatory regime that is proportionate, effective and provides value for money. Broadly speaking, we believe that the OFT has created such a regime in the context of consumer credit, but that the underlying flaw in the system is the duplication of, or overlap between, regulatory roles, as outlined in the CP (see above).

21. Regarding the specific objectives set out in paragraph 1.18, we comment as follows –

- **Clarity, coherence and improved market oversight** – a single, accountable regulator is more likely, in principle, to achieve this objective than a multiplicity of regulators. Any proportionate steps to reduce compliance and administration burdens in what is a highly regulated industry would be most welcome, as long as it is not at the cost of sensible consumer safeguards.

- **Effective and appropriate consumer protection, including through a responsive and flexible framework** – in principle, we agree with these aspirations.

- **Simplification and deregulation** – again, we agree in principle, but – as noted above - we believe that the authorities need to be sensitive to the long-term upheaval that has taken place over the last 5 or 6 years and propose only changes that would be simple and deregulatory.

- **Proportionality and cost effectiveness** – we agree: this should be an objective of *all* regulatory regimes.

Chapter 2: Options for the future regulation of consumer credit

5. The Government welcomes views on the impact a unified regulatory regime for retail financial services may have in terms of clarity, coherence and improved market oversight.

22. The BSA understands the Government's preference for option 1 (repeal of the Consumer Credit Act - CCA). In principle, we agree with the advantages of option 1, listed in paragraph 2.6. (But we mention in passing that the factors specified related to lack of synergy in the existing regulatory architecture, rather than existing consumer detriment). Nevertheless, a strong argument against the proposal to migrate the CCA into the regulatory handbook is the upheaval that the consumer credit industry, consumer and regulators have already experienced over five years or more (see above)

and the further, very significant disruption that such a radical move would entail. We are also concerned about the three points raised by the Regulatory Policy Committee; namely, that there are incomplete analyses of -

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

www.bis.gov.uk/assets/biscore/consumer-issues/docs/i/10-1376-impact-assessment-reform-regulatory-consumer-credit.pdf

While we note the explanations given in paragraphs 4-7 of the impact assessment, we are surprised that final decisions might nevertheless be made on a matter of such complexity based on such a lack of evidence. On balance, we think that – especially at a time of large-scale, systemic changes elsewhere in the regulatory regime – the proposal to migrate the CCA into the regulatory handbook would be a bridge too far. Indeed, it is difficult to see how the Government could adhere to its pledge against gold-plating if it were to repeal the CCA, only to re-instate it through the Handbook. We think it preferable to install the new PRA/FCA regime and address the possibility of repealing the CCA once the new regime had been given a reasonable opportunity to consolidate. This would also enable a clearer picture to be obtained of costs and benefits.

23. We do not see it as a necessary corollary of a migration of consumer credit regulation from the OFT to the FCA that the CCA has to be repealed – and certainly not within the next two or three years. As paragraph 2.7 of the CP acknowledges, the FSA currently has to accommodate numerous pieces of legislation – eg regarding unfair contract terms, unfair commercial practices etc - that stand apart from the FSA's Handbook of Rules and Guidance, but are, nonetheless, relevant to (and usually binding upon) FSA-regulated firms' business operations. The Payment Services Regulations 2009 provide a recent example.

24. However, *if* the ultimate decision was to implement option 1, an alternative to unpicking the whole of the CCA in its, oft-modified, form and then translate it in full into a Handbook module – would be to copy out the European Consumer Credit Directive into the Handbook. Certain cosmetic textual changes would be required to make it suitable to its new vehicle. This approach would be consistent with the Government's recent pledge against gold-plating, but there would have to be a consideration of the balance between benefits to consumers deriving from the simpler EU arrangements and the loss of certain protections enshrined in UK law.

25. We understand that, because the Directive was grafted onto the existing UK legislation, the CCA (and the Regulations under it) now contains examples of super-equivalence, despite the fact that the Directive is one of maximum harmonisation. We would be interested to know how option 1 could comply with EU law, in the light of the Directive's maximium harmonization status, if it involved repeal of the CCA and its resurrection (in a 'super-equivalent' state) in the regulatory handbook.

26. A further consideration if option 1 were to be pursued on *any* basis flows from the Directive's maximum harmonization status. FSA Handbook modules setting out

business standards do not exist in a vacuum – they are subject, for example, to high level standards such as principles for business. In the light of this, how can the CCA be repealed and incorporated into a business standards module, without breaching the Directive's maximum harmonization requirement?

6. The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.

27. The option referred to in paragraph 2.8 (arrangements to be made for functions to be performed on behalf of the regulator) seems appropriate. Ensuring continuing, constructive relationships with trading standards agencies would be very important.

7. The Government welcomes views on factors the Government or the FCA may wish to consider in the event of a transfer of consumer credit regulation relating to how the overall level of consumer protection might best be retained or enhanced.

28. See comments above.

8. The Government would welcome further evidence relating to:

- *the use of consumer credit by small and medium sized enterprises (SMEs);*
- *whether the protections currently afforded by the CCA are appropriate and cover the right groups of businesses; and*
- *the costs and benefits of considering extending FSMA-style conduct of business rules to a wider group of SMEs.*

29. We have no further comments on these points.

9. The Government welcomes views on how consumer credit firms and consumers may be affected by the increased flexibility that could be provided by a rules-based regime.

30. See comments above.

10. The Government welcomes views on the impact a FSMA-style supervisory approach may have in terms of ensuring effective and appropriate consumer protection.

31. Subject to the points we have made above, this seems to be a sensible approach.

11. The Government welcomes views on the synergies afforded by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.

32. We have nothing particular to add.

12. Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the FCA would support the Government's objectives (as outlined in paragraph 1.18 of Chapter 1)?

33. We are not convinced that "specific characteristics of the unsecured credit market may justify a distinct regulatory approach" (paragraph 2.25) and would need to see clear evidence on this point. But we understand the concerns of smaller providers that changed arrangements might add layers of regulatory complexity and potentially be unhelpful to financial inclusion. We believe that the authorities would need to take this matter into account in respect of any changes that are made. We also recognise that consumer credit is mass market, heavily systematised and needs certainty of rules, but this also applies to certain other financial services sectors eg mortgages and banking.

34. However, as we explain above (see response to question 5), the upheaval that the consumer credit industry, consumers and regulators have already experienced over five years or more, is considerable. In the BSA's opinion, it is this factor that justifies a slower pace of supervisory change in this particular business area.

13. Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?

35. Please see, in particular, our response to question 5.

14. Are there specific issues that you believe the Government should consider in assessing the merits of option 1? How could these be addressed in the design of a new regime as proposed in option 1?

36. We have nothing further to add.

15. If you do not agree with the Government's preferred option 1, do you have views on the factors set out in paragraph 2.4 that the Government should consider in determining the most appropriate regulatory authority for the CCA regime under option 2?

37. Please see our response to question 5.

Chapter 3: Achieving a proportionate and effective regulatory approach

16. The Government welcomes views on the suitability of the provisions of a FSMA-style regime, such as those referred to in paragraph 3.6, to different categories of consumer credit business.

38. We agree with the list of main areas, set out in paragraph 3.6, where there is likely to be a degree of divergence from the current CCA regime. It also needs to be remembered that some of these areas will fall within the scope of the PRA and others within the FCA"s remit, which potentially complicates matters further. But there are certain mitigating factors.

39. First, as the CP notes in paragraph 3.7, some of these FSMA-style requirements have equivalents within the CCA regime.

40. Second, the FSA already regulates a very wide range of business sectors and individual firms, ranging from multi-nationals to small local firms. It has to accommodate firms of greatly varying size and with highly divergent business activities and models. Within our own, BSA membership, there is a wide range of businesses, varying greatly in size and structure. Our members range from those

with one branch and fewer than ten staff to the largest, which has about 800 branches, some 18,000 full and part-time staff and assets of around £200 billion.

41. As recognised later in the CP, an even more pertinent example is the credit union sector, which was not regulated by the Financial Services Authority at its outset. Since coming within the FSA"s regulatory ambit in 2002, credit unions have a specialist sourcebook in the FSA Handbook setting out prudential rules and guidance, they are required to keep a basic level of solvency and to maintain a minimum liquidity ratio, and key staff and volunteers are subject to the FSA"s approved persons standards. Smaller credit unions are mainly supervised using a desk based approach using regulatory returns – the FSA will visit larger credit unions and more attention will be paid to their business planning and operations. Credit unions are also part of the Financial Ombudsman Service and the Financial Services Compensation Scheme.

42. With this kind of background, the regulator should not find it a particularly novel experience having to deal with the diverse range of firms that undertake consumer credit business. Perhaps the more pertinent question is whether or not the FCA could cope with this additional specific workload *at the same time* as establishing itself as the UK"s conduct of business regulator across the entire financial services industry.

17. Do you agree that statutory processes relating to FCA rule-making, a risk-based approach to regulation and differentiated fee-raising arrangements could provide useful mechanisms in ensuring that a proportionate approach is taken to consumer credit regulation under a FSMA-style regime?

43. The BSA supports the approaches outlined in the CP concerning statutory processes, ie –

> "In the event of a transfer of consumer credit responsibility, the [FCA] 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." (paragraph 3.19)

In principle, there is no reason why these approaches – which have worked quite well for other sectors – should not be effective in relation to the regulation of consumer credit.

18. The Government welcomes views on key factors that would need to be assessed in considering fee arrangements for consumer credit firms.

44. The authorities will need to be sensitive to the current economic climate and the impact that raised fee levels could have, especially on smaller firms. We agree with the general approach outlined in the CP, as follows -

> "In setting fee levels for authorised credit activities, the [FCA] would take a proportionate approach and consider the appropriate level for minimum fee requirements for different categories of firm." (paragraph 3.23)

19. The Government welcomes: evidence relating to experiences of the current appointed representatives regime; views on how an appointed representatives model might be applied to different categories of consumer credit activities, including how current business models and networks might lend themselves to such an approach; and *evidence relating to the implications an appointed representatives regime might have for firms and consumers.*

45. We have nothing to add to the points made in the CP.

20. The Government welcomes: evidence relating to experiences of the current group licensing regime; and views on how the professional bodies regime might be adapted for different categories of consumer credit activities.

46. We have no direct experience of this subject but, in principle, can see no reason why group licensing arrangements like those available in respect of consumer credit business, should not be adapted for the FCA.

21. The Government welcomes views on the extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises.

47. Some self-regulatory codes of practice still exist in this, or related areas; for example, the two *Lending Codes* operated, respectively, by the Finance and Leasing Association, and by the British Bankers Association, BSA and UKcards Association.

48. The BSA long supported industry codes of practice and, for example, sponsored the *Banking Code*, which delivered significant consumer benefits for nearly 20 years, until the FSA abolished the Code and replaced it with the BCOBS module in the Handbook. It would be anomalous to scrap a strong, long-standing code of practice in relation to one FSA regulated area (ie banking), while encouraging their development in others. Therefore, our only substantive comment on question 21 is that the authorities need to take a definite position – do they want industry codes of practice on certain matters or do they prefer statutory regulation? It is not in the consumer interest to keep changing on this matter. We simply ask for a consistent position one way or the other.

22. Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.

49. As discussed above (see response to question 5) the simplest deregulatory approach, and one consistent with recently stated Government policy and the maximum harmonisation status of the EU Directive, would be to scrap the CCA in its entirety and move to a copy out of the EU Directive into the regulator"s Handbook of Rules and Guidance. To unpick and reassemble the legislation - yet again - would be counter productive for consumers, for businesses and for the UK economy. As we have explained, the best course of action would probably be to retain the CCA for the time being.

*23. Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approac*h?

50. We have nothing further to add at this stage. However, the BSA has established a Regulatory Reform Working Group made up of practitioners from the BSA membership, BSA associates and members of the BSA Secretariat. Its objective is to help with detailed aspects of the regulatory reform exercise as it progresses, and we would be happy to give practical assistance, through this and other relevant working groups and panels, as the plans on this subject become firmer.

Chapter 4: Implementation and transitional arrangements

24. The Government welcomes views on how the treatment of agreements already in existence could be approached.

51. It is difficult, at this early stage, to provide considered views on detailed matters such as transitional provisions, but we agree in principle with the analysis in chapter 4. Caution would be needed to ensure that existing consumer credit agreements were not affected retrospectively. Presumably the back-book would continue to be regulated under the CCA?

52. If the CCA is to be repealed and re-introduced via the regulator"s Handbook, we believe that the length of the entire exercise would need to be considerably extended beyond current plans. The time taken to incorporate the EU Directive into UK law demonstrates the complexities in such a project. A straight copy-out of the Directive would, as noted above, be a simpler approach, but the simplest approach of all would be to retain the CCA for the time being.

25. The Government welcomes views on:

- *how existing licensees could be dealt with; and*
- *factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms.*

53. We agree in principle with the comments set out in the CP.

26. The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.

54. The possibility of discounted authorisation fees during the transitional period seems to be worth exploring.

27. Are there other factors the Government should take account of in considering transitional arrangements?

55. We have nothing further to add.

28. The Government would welcome evidence on the experience of firms, consumers and their representatives in relation to similar previous transitions, for example the extension of FSA jurisdiction to new markets since 2000.

56. As noted above, and recognised in the CP, the regulation of credit unions was a parallel (but, by no means, identical) extension of jurisdiction.

The Building Societies Association
14 March 2011