Dear Treasury

the Office of Fair Trading have an excellent record in defending consumer interests and assessing whether companies have behaved in a fair and reasonable manner.

I do not feel that the transfer you suggest will be helpful. "Simplifying" processes often has detrimental results for individuals who may wish to complain. Regulation is usually detailed for good reason.
I am very concerned about the government's proposals under which vulnerable customers may become even more vulnerable to predatory credit providers.

M Macleod

My ref: C:\wpdocs\misc.679 2.3.11.

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

By Emeritus Professor JK Macleod

History. The ground-breaking Consumer Credit Act 1974 (CCA) was largely based on the excellent Crowther Report of 1971 (Cmnd 4596), much of which was the work of Sir Roy Goode (still General Editor of the leading *Encyclopedia*); but the novel CCA draftsmanship of Francis Bennion (still a respected author on statutory interpretation) has not really worked. The CCA envisaged much implementation by Statutory Instrument under the aegis of the DTI: unfortunately, it took ten years to implement under the poor leadership of Derek Hyde. That delay, combined with the unusual draftsmanship of the CCA and the less-than-clear SIs caused such bafflement that it took the legal profession some 30 years to come to grips with the scheme; and litigation on it only became common in the 1990's. It is certainly time for an overhaul.

Box 1A.

- **Rule-making and enforcement.** The current rule-making is in the hands of the DTI/BIS and parliamentary statutory instruments.
  (i) The DTI/BIS has a poor record of drafting in this area: it got off on the wrong foot (see above) and never seems to have recovered. At very least, a new, simpler form of drafting is needed.
  (ii) The Parliamentary scrutiny system currently applied to these draft SIs may work well for road improvements; but what is needed in this field is more scrutiny off the floor of the Commons - a new Select Committee? NB Especially the consumer-facing regulations could be seen as too politically sensitive for transfer to an FSMA-type body.
- **Consumer rights and redress.** The CCA creates a number of consumer rights:
  (i) These rights were drafted to allow much individual enforcement by way of the traditional courts, whereas what is needed this century is more Alternative Dispute Resolution, a more flexible FOS.
  (ii) The OFT has always set its face against supporting individual consumer enforcement and in favour of collective enforcement. Before 2006, its court enforcement might be described as torpid; but since then it has become much more vigorous, though with mixed success.
- **Market oversight.** Unsurprisingly, the CCA system applied by the OFT is rooted in the 1970s, whereas the FSMA system is much more flexible and modern. However, market studies are a valuable modern OFT process.
- **Supervision of firms and business applications.** It seems likely that the FSMA

system will only work properly for large creditors. Even if it takes over the OFT function entirely, it will probably need something like the existing system for the myriad of small businesses.

Box 1B.

Q1. When the CCA 2006 was enacted, I agree that your preference for immediate transfer of all OFT functions to an FSMA-style model was appropriate. But since then:

(i) There is no getting away from the fact that pre-2006 the OFT exhibited much that was worst in the civil service: this seems to have been a combination of poor DTI supervision and poor OFT leadership. However, under the new 2006 leadership (Messrs Collins & Fingleton), the OFT is now a much better organisation.

(ii) The poor regulations introducing Directive 2008/48 to the UK (2010 SIs 2010-4) show just what a mess DTI/BIS-sponsored regulations can produce. Nor do I think they can duck behind the wide prior consultation the above 2006 leadership introduced (in itself welcome): the DTI/BIS is in the lead.

(iii) The present appalling state of UK consumer credit law means that any reforms will have to be carefully introduced if the result is not to be chaos.

Q2. The major substantive issue for UK consumer credit law is how to assimilate EU Directives into UK law.

(i) 20yrs ago, UK law was so far ahead of EU credit law that it was rational to retain the CCA and simply graft the few necessary EU changes onto the CCA structure. But, it made no sense for the DTI/BIS to go ahead with the CCA 2006 when it knew of the major EU changes in the offing (even if they could not know the precise shape).

(ii) Since the 2008 Directive, EU credit law is up to speed and the basic issue is whether to adopt EU law instead of the CCA - this seems a political question that the DTI/BIS has just ducked. **Q3.** The answer to the above political question should shape your approach as follows:

(i) If you retain the CCA 1974-2006, then my advice would be to make the minimum changes to the institutions (FSMA & OFT) whilst gradually simplifying UK substantive consumer credit law over this Parliament.

(ii) If you decide to replace the CCA with Directive law, your proposal to re-configure the relationship between the FSMA and OFT has considerable force. But it may take 10yrs to introduce in a way that is understandable to consumers and small business; and I am not a fan of such great-leaps-forward.

(iii) It seems to me that a more gradual approach might be preferable: whilst simplifying UK substantive consumer credit law over this Parliament (above), you could immediately transfer to an FMSA-type structure those relatively self-contained bits of the OFT empire - the Competition Commission and CCA licensing. The 'OFT' name could be kept for the consumer-facing functions, whether or not oversight transfers to the Treasury.

Box 1C.

Q4. These praiseworthy objectives have to be seen in the light of the impossibly complicated present UK law of consumer credit, which tends to bury principle in a 'system' that is only properly understood by Roy Goode and the Banks' large computers. I do not think your objectives are wholly attainable without sweeping simplification of the substantive law.

Box 2A.

Q5. Bear in mind that the EU looks likely to introduce sweeping mortgage reform in the next 5yrs. Please don't make the same DTI/BIS mistake again: introducing a new UK regime (the CCA 2006) just as the EU is about to spawn compulsory reforms (the 2008 Directive).

Box 2B.

Q6. The Local Authority Trading Standards Depts provide extremely valuable local consumer protection. Whatever changes you make, please make adequate provision for them - say along the lines that the OFT has developed since 2006.

Box 2C.

Q7. We are back with the major political issue identified above in **Q2** - CCA or Directive based law?

Box 2D.

Q8. This is a CCA area outside the Directive. Is the substantive law to be CCA or Directive based law?

Box 2E.

Q9. This seems to raise 2 different questions:

(i) As regards business2business, this is a competition issue: a complicated system favours large lenders having the benefit of elaborate computer programmes and specialist trained staff, so raising a barrier (particularly) to new small entrants.

(ii) As regards business2consumers, regardless of the amount of (mostly ineffective) paper-work which is provided to consumers, the 'system' is beyond the comprehension of most consumers and their advisers.

Box 2F.

Q10. This raises the (political?) question of to what extent consumer protection legislation is to be enforced on behalf of consumers by -

(i) Individual action by the injured consumer; or

(ii) Collective action on behalf of consumers generally.

Box 2G.

Q11. As few consumers or their advisers understand the dichotomy between rules protecting them as regards (a) credit and (b) supply issues, the new system needs to retain a close relationship between (a) and (b), such as is currently found in the OFT regime.

Box 2H.

Q12-5. Your Paper makes the case for the advantages to business of an FSMA-type regime. There is a (political?) danger this might be seen as proposing corresponding disadvantages to consumers.

Box 3A.

Q16. The proposed FSMA-style programme would probably be fine for big-business, but be beyond the comprehension of small business creditors The latter frequently seem unable to cope even with the more rigid OFT system.

Box 3B. (No numbers)

Presumably, credit unions are usually 'staffed' by well-intentioned amateurs anxious to conform to the regime, eg vicars. I should have thought that small business creditors are likely to have exactly the opposite mind-set (think Arthur Daley).

Box 3C.

Q17. Agreed.

Q18. No comment.

Box 3D.

Q19. No comment.

Box 3E.

Q20. The present Group Licensing scheme under the CCA works well and has done from the outset. It should continue under whatever guise.

Box 3F.

Q21. There is some merit in Voluntary Codes, as pursued by the OFT from its inception and encouraged by the CCA 2006. Whether it is cost/effective or will bear the weight of importance attached to it by the OFT is another question. Perhaps the more modern Guidance could fulfil most of its functions.

Box 3G.

Q22. 'Light touch' may be currently difficult to sell. I would need concrete examples of those categories before I could comment.

Box 3H.

Q23. Since 1975, the OFT has had a poor record developing individual licencing. Why not transfer the entire CCA licensing system to the FMSA immediately, regardless of the other issues canvassed in this Paper?

Box 4A.

Q24. Much depends on whether you decide to grasp the nettle to replace the CCA system with an EU-based one. Don't forget that, whilst the typical consumer credit agreement might last a year, some others may last 20yrs.

Boxes 4B & C.

Q25. Go for grandfathering.

Q26. No comment.

Box 4D.

Q27. Keep as much as possible of the detailed changes out of sight of consumers, insofar as their position will not be affected. Then, the vital issues are likely to be -

(i) Balancing the respective positions of large and small creditors.

(ii) Transferring the OFT's competition jurisdiction to an FSMA regime (I do not forget the alleged advantages of administering consumer protection and competition through the same body).

Q.28. No comment.

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From : Midfit Ltd 1 Oak Tree Close Bleasby Notts NG14 7HZ

RESPONSE to

A new approach to financial regulation:

consultation on reforming the consumer credit regime

Financial Regulation Strategy
HM Treasury
1 Horse Guards Parade
London
SW1A 2HQ

16 March 2011

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

Midfit 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 offer finance to the haulage industry and have done so for some 27 years. We have two working directors and no other employees.

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
For Midfit Ltd

J. H. Kelsey - Director

HM TREASURY AND BIS

REFORMING THE

CONSUMER CREDIT REGIME

CONSULTATION PAPER

Response by Money Advice Scotland
March 2011

About Money Advice Scotland

Money Advice Scotland was set up in 1989, and its objectives are to promote the development of free, independent, impartial confidential money (debt) advice. MAS is the umbrella organization in Scotland and a broad church, with members ranging from CABx, local authorities through to credit industry, insolvency practitioners, credit unions etc.

Money Advice Scotland‟s vision is to "champion and support the continuing development of free, independent, impartial confidential money (debt) advice, and financial inclusion"

The organization achieves this through the following:

- *Delivering training and qualifications in money advice*
- *Delivering a high quality annual conference*
- *Providing a consultancy service for advisers*
- *Providing a statutory scheme for the certification of money advisers*
- *Providing a referral point for members of the public who are seeking advice*
- *Providing social policy input to matters relating to consumer credit and debt, particularly new legislation*

How we have drawn up this response

A sub group of Money Advice Scotland's governing body met and discussed the Money Advice Trust response to the consultation, most of which we endorse wholeheartedly. We have submitted a separate response, which includes much of the text of Money Advice trust‟s paper. As you will appreciate there are issues of particular importance to Scotland, given the different legislation in respect of debt enforcement etc, and indeed for Money Advice Scotland‟s members.

Please note that we consent to public disclosure of this response.

Introductory comment

Like the Money Advice Trust (MAT), we welcome the review of the current regulatory regimes for financial services and we value attempts to simplify and unify regulation and consumer protection for financial services.

We are however, concerned that a rules-based regime could be a high-level principles-based framework (in contrast to the detailed regulation-based approach under the Consumer Credit Act), underpinned by non-mandatory guidance, which would not capture the necessary level of detail to be effective.

We are most reluctant to lose the consumer rights contained in the Consumer Credit Act 1974 (CCA) protections without ensuring that there are robust protections in their place. Without being able to see the details of the new proposals it is difficult to comment on the best approach. However we are clear on the need for ensuring that any new system, should avoid anything of significance "falling through the cracks".

In this paper we outline what measures we value under the CCA and our areas of concern.

We support neither option 1 nor 2 which are outlined in the consultation paper. We believe that the best way to protect consumers and to regulate financial services is to take the best of both the FSMA and CCA regimes, and to avoid the failures of both of the current regimes.

In order to achieve this, we would urge Government to ensure that there are sufficient resources to ensure that the new regime can be put into effect to create an effective, coherent and comprehensive regulatory regime. There is a danger that if resources are too limited that the reforms will not work as intended.

In Scotland we have a particular issue with regard to there being adequate funding in place for enforcement by Trading Standards Departments, in respect of the Consumer Credit Act. It is our consideration that any system has to be very proactive and not reactive in terms of avoiding consumer detriment.

Responses to individual questions

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

The assessment of the current market as outlined in sections 1.8 to 1.10 of the paper is reasonable in its aim to

"facilitate the right outcomes for consumers while being proportionate to the risks posed."

We agree with MAT, regarding the assessment of the consumer credit market as outlined in the paper, and we would point out that the growth of the sub-prime credit market is of particular concern to the free-to-client debt advice sector. The increase in very high interest lending such as payday loans and pawn broking adds to the debt burden for those in financial difficulties. Effective regulation and control of this sector is of paramount importance to avoid further consumer detriment. This is of course in addition to effective regulation of mainstream credit as the majority of people in debt will have debts to mainstream credit providers.

In Scotland, many communities suffer the blight of only being able to access payday loans, and as a result never get out of the cycle of debt, if they are unable to pay off their loans. In many instances the borrower "flips" the loan – in other words the first loan isn't paid in full when the person is paid and a further loan is taken out to cover it. The interest and costs to the borrower then escalate, and they become trapped. Payday loans are intended, as a product to be short term loans and in reality, for many they are being used to sustain longer term borrowing, which comes at a cost.

There are insufficient alternative affordable sources of credit in these areas, although work is taking place to try to address the balance.

The consultation paper mentions the rise in people struggling to pay debts. We would draw your attention to the recently published Money Advice Trust and University of Nottingham "Demand, capacity and need for debt advice in the UK" research.[1] This predicts that:

"If unemployment continues to increase as suggested by a number of independent forecasts, by mid-2011 demand for advice will exceed that seen at the peak of the financial crisis in late 2009."

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[1] **http://www.infohub.moneyadvicetrust.org/content_files/files/demand_capacity_and_need_for_debt_advice_in_uk.pdf**

In Scotland, the Accountant in Bankruptcy"s[2] recent news release indicated the numbers of bankruptcies are falling – 11% in the last quarter, however the number of Debt Payment Programmes (where clients pay back 100% of their debt) under the Statutory Debt Arrangement Scheme have risen by 16% compared to the same quarter in 2009-2010.

Question 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 can see that on the face of it, having a single regulator accountable for the performance of retail financial services covered by one regulatory regime would appear attractive. However, we strongly believe that effective consumer protection measures are the best way to ensure that the primary objective of the Financial Conduct Authority (FCA) CPMA, of ensuring confidence in financial services and markets is met.

We, like MAT, have previously raised concerns in relation to the issues raised by an over-reliance on competition. We believe that competition does not make financial services more accessible to people on the lowest incomes or who are vulnerable in some way or protect them from unfair practices. It is our view that if anything it often forces more people out of the system. **We strongly believe that reliance on competition does not clean up the marketplace.**

We agree with MAT, and would welcome a more proactive approach to consumer credit regulation, aimed at preventing the problems caused by unfair products, services and practices from proliferating in the first place. We would draw an analogy with the Food Standards Agency and the speed with which it can act if a dangerous product comes on to the market. We would also make the point that today, as soon as one company is closed down for bad practice; another appears in its place. We need a flexible and innovative regulatory structure with the ability to act timeously and decisively to reduce the proliferation of bad (and sometimes illegal) practices examples of which are provided below.

We acknowledge the current work of the OFT and other licensing bodies and regulators in tackling bad practice, but often this work is not timely enough, nor does is appear that the relevant organisations possess sufficient power to regulate as effectively as we would expect. A significant proportion of investigations rely upon individual consumers being prepared to make formal complaints to regulators that will help to build up a body of evidence. There is little incentive for the consumer to cooperate as for example the OFT is specifically prevented from dealing with individual complaints on a case-by-case basis, and is also unable to

[2] www.aib.gov.uk/news/releases/2011/01/scots-insolvency-numbers-down-again

let the consumer know the outcome of their investigations in any formal way. This is most unsatisfactory where individuals may want redress for their own problem (in which case they must use FOS) but would also like their experience to help others (in which case they must complain to the OFT as well)."

We welcome the declaration in paragraph 1.5 that the CPMA (now FCA)

"will take a tougher, more proactive and more focused approach to regulating conduct in financial services and markets than has the FSA".

We would, like MAT, suggest that the regulator covering consumer credit issues needs to have improved regulatory powers and resources to pro-actively police compliance and conduct enforcement against companies in breach of regulations. The current system is hampered by the difficulties in enforcing breaches of guidance against individual companies. The Consumer Credit Act 2006 led to an improvement in the licensing regime but action is still generally reactive against individual companies where enhanced power to prohibit bad practices and conduct across the board is required.

As an example, Like MAT,we are aware of OFT credit licensing revocation cases that are drawn out for years under appeal, allowing the trader to still operate and cause detriment to individual consumers. There needs to be a robust time-limited appeal system in place. There also needs to be enhanced powers to provide redress for consumers and to do so retrospectively where harm has been identified.

However, the full effects of the enhanced powers given to the OFT under the CCA 2006 are only now bearing fruit. There has been a marked increase in actions taken by the OFT in 2010 in relation to requirements and licence revocations.[3] These are in relation to areas where the free-to-client advice sector have been active in raising concerns such as in relation to the use of charging orders (in England and Wales), debt management company practices, "look-alike" websites (debt management companies that portray themselves as free independent advice agencies), payday loan contracts, debt collection practices of various companies and so on. Any change to the regulator needs to be carefully considered to ensure that such a move is not premature. There is a danger that the benefits of the CCA 2006 changes to the powers and capability of the OFT to take action will be lost. We would highlight the powers that the OFT has available under Section 11 of the Enterprise Act 2002 to refer a market to the Competition Commission. There does not appear to be an equivalent power under FSMA and would suggest this needs addressing. As Citizens Advice say in their response to the BIS Financial Services Regulation consultation paper[4]:

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[3] **http://www.oft.gov.uk/OFTwork/credit/enforcement-action/#named1**

[4] **http://www.citizensadvice.org.uk/index/campaigns/policy_campaign_publications/consultation_responses/cr_consumeranddebt/her_majestys_treasury_financial_services_regulation**

"Citizens Advice believes that the current consumer protection objective in section 5 of FSMA needs to be updated to reflect the role of the CPMA as a strong consumer champion. The duty is vague in its purpose and, in requiring protection to be „appropriate", indeterminate in its force. It also fails to clearly set out the wider public interest objectives that we would expect of a consumer champion."

We note that the Treasury is also consulting on "A new approach to financial regulation: building a stronger system"[5] One of the options in this consultation is for the FCA"s Consumer Panel to have the ability to trigger the super-complaint process. However, it is not clear from the Treasury consultation whether these super-complaints would be as wide as those under s11 i.e. covering any features of a market that appear to be significantly harming the interests of consumers and therefore either competition and/or consumer protection problems. We would strongly support any new powers to cover consumer protection issues where these do not arise from a restriction of competition.

Overall, we accept that the concerns raised in the paper regarding the difficulties of developing coherent policy responses to emerging consumer protection issues over two separate regimes. This is coupled to the lack of accountability by one body for the performance of retail financial services. We accept the current regulatory framework is confusing for consumers and industry but would applaud the way in which regulators have worked round this by way of memorandums of understanding, joint working, and so on.

We have outlined our concerns at the proposed approach throughout our response to this paper.

[5] **http://www.hm-treasury.gov.uk/d/consult_newfinancial_regulation170211.pdf**

Question 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;

Irresponsible lending and borrowing

We would support intervention to protect consumers from the consequences of unaffordable borrowing. Money advisers frequently report speaking to clients who are in a downward spiral of multiple personal debts and using one credit card to pay off another etc. There is increasing evidence of consumers using credit cards to pay priority debts such as their mortgage[6] Many consumers are temporarily insulated from falling into mortgage arrears by record low interest rates, but this does not apply to those with subprime and / or high interest second charges. It is very hard for consumers in financial hardship to make appropriate choices and there must be adequate protection against the sale of inappropriate products. Over the years the free-to-client advice sector has seen many instances of inappropriate consolidation loans taken out to consolidate unsecured debts, or mortgages taken out with no repayment vehicle in place.

High cost credit

We, like MAT have had a longstanding concern over the detriment to consumers caused by the interest rates associated with loans offered via bills of sale, payday lending and in some instances, home-collected credit particularly where loans are rolled over. We are concerned that some products which fall into this high-interest category appear on the face of it to be unfair to the consumer. There is clearly a need for some further work to ensure that vulnerable consumers are treated fairly in how they access credit products.

We would urge that the levels of interest that can be charged by banks in relation to authorised and unauthorised overdrafts are not overlooked. Such credit facilities are not always regarded as falling within common definitions of high-cost credit products. Nonetheless, they can create a heavy burden for consumers who have fallen into debt, albeit this is a product valued by many consumers.

Payday loans

There should be a strategic review of the use of payday loans to establish whether these products are operating to the detriment of consumers. Such a review should pay particular attention to the practice of „rolling up‟ loans, and adding further interest and charges. We question whether payday loans should be allowed to continue to exist in their present form.

[6] http://england.shelter.org.uk/news/january_2011/2m_pay_for_home_on_cards

Debt collection

We have continuing concerns that some debt collection agencies and debt purchase companies are failing to abide by the OFT Debt Collection Guidance, and welcome the OFT"s actions against individual companies.

We acknowledge the work of the trade association the Credit Services Association and their role. However there are debt collectors who are not members of the trade association and not working to the same standards.

We understand that the OFT has imminent plans to revise the guidance which, in our opinion, needs to be strengthened to deal with abuses and to deter non-compliance. The review of the OFT Debt Collection Guidance should highlight the continuing problem of lenders failing to pass on full information about the debt, including information about third parties dealing with the account, financial statements, and details of existing payment arrangements. There is also a role for the Lending Standards Board in terms of their compliance visits.

There are also further unresolved issues regarding harassment of vulnerable people in debt, use of official-looking letters, and inappropriate collection action such as issuing statutory demands, pursuit of statute-barred debt particularly by debt sale companies, extensive issues with mis-tracing, bad management of disputed debts, and so on.

In Scotland there remain issues with cross-border collection of debt, where companies are pursuing debtors in Scotland through the English courts, or sending debtors inappropriate letters threatening action (including imprisonment for non payment of debt) which relates only to England and Wales. This is not acceptable practice

The fee-charging debt management sector

There is a substantial risk faced by consumers in relation to fee-charging debt management companies. This has been clearly demonstrated by the work of the OFT in their Debt Management Compliance Review[7] As a result of the review, there has been further licensing action in January 2011[8] We agree with our colleagaues at MAT that In the absence of a statutory debt management plan for England and Wales, as envisaged under the Tribunals Courts and Enforcement Act 2007 much more needs to be done to protect vulnerable consumers in debt from such firms.

"…As part of the review the OFT found that:

- *there is widespread non-compliance with the Guidance by debt advice and*

[7] **http://www.oft.gov.uk/shared_oft/business_leaflets/credit_licences/OFT1274.pdf**
[8] **http://www.oft.gov.uk/news-and-updates/press/2011/10-11**

debt management licensees, with most debt management firms audited failing to some extent in at least three areas;

- *misleading advertising is the most significant area of non-compliance, in particular misrepresenting debt management services as being free when they are not;*
- *frontline advisers working for debt management companies generally lack sufficient competence and are providing consumers with poor advice based on inadequate information."*

In Scotland we are fortunate as we have a Statutory Debt Arrangement Scheme (under the Debt Arrangement and Attachment Act 2002, and Debt Arrangement Scheme Regs 2011) which is in place. Changes will be made to it – effective from 1 July 2011, which will likely result in more Debt Management Companies delivering Debt Payment Programmes. They will likely be charging the debtor for setting it up, have ongoing charges, and indeed acting as a Payment distributor, thus collecting 8% of the debt passed back to the creditors. It is essential that there is control and compliance in place. There is a burning need for transparency of the service being offered, and to ensure that particularly vulnerable debtors do not suffer consumer detriment. This is a matter for the Accountant in Bankruptcy and the OFT and future regulators.

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

We see the consumer protection work undertaken by the OFT as a crucial key provision in the current regime. We have noted elsewhere in our response that the CCA 2006 provisions have enabled the OFT to take increasingly effective enforcement action against licence holders. The new protections have taken time to bed in, but are now showing increasing effectiveness. We feel that the OFT is hampered by a lack of resources to enable them to take comprehensive enforcement action across sectors. However, where the OFT has been able to take action, they have been effective. There needs to be a balance between proactive and reactive enforcement.

The OFT describes their regulatory principles as follows:

"The Consumer Protection from Unfair Trading Regulations (CPRs) and the Consumer Credit Act 2006 have made significant changes to the body of UK consumer protection law. Together with the Unfair Terms in Consumer Contracts Regulations 1999 and the Enterprise Act 2002, they mark a fundamental move away from prescriptive regulation towards a principle-based consumer protection regime which encourages targeted, risk-based enforcement geared to the efficient operation of the market. At the same time, they also increase the range of enforcement tools available to enforcers, strengthening investigative powers and enabling OFT to take criminal proceedings and to seek financial penalties,

alongside existing civil enforcement and compliance tools."[9]

The OFT and Competition Commission powers under section 11 of the Enterprise Act 2002 are substantial and the OFT refers to it as its "main tool to ensure compliance with the law". Section 11 allows a designated consumer body to complain to the OFT that a feature or combination of features of a market for goods or services is, or appears to be, significantly harming the interests of consumers. This gives the regulator a statutory period of 90 days to publish a response stating what action it will take. There is no equivalent provision under FSMA rules to allow the FSA or CPMA to take such swift and timely consumer protection action. As a result we question whether the preferred option (A) would allow for timely responses to emerging consumer protection issues as set out in the introduction to this consultation.

We have outlined what we consider to be the key provisions of the CCA in providing consumer protection in our response to question 7.

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

We are unable to comment widely on the incidence of regulatory duplications or inconsistent regulation as it affects firms.

It is generally difficult and confusing to work out what will be covered under FSA Banking Conduct of Business Sourcebook (BCOBS) and what is covered by the Lending Standards Board. It has certainly been challenging to deal with particular issues such as the guidance on the right of set off with both the Lending Standards Board in relation to current accounts in overdraft, and the FSA in relation to current accounts in credit. We have had similar problems identifying whether the matter of accessing basic bank accounts when an undischarged bankrupt is covered by BCOBS and the BCOBS Industry Guidance or the Lending Code. There is a danger that such issues get lost between the different regulatory bodies and industry guidance.

In the MAT response to the review of BCOBS Industry guidance[10] they questioned how transparent the interaction is between the FSA BCOBS principles and the industry guidance which is not intended for the public. They understand the FSA "will take [the guidance] into account when exercising its regulatory functions."

[9] **http://www.oft.gov.uk/about-the-oft/legal-powers/enforcement_regulation/enforcement**

[10] **http://www.moneyadvicetrust.org/images/Money%20Advice%20Trust%20response%20to%20the%20review%20of%20industry%20guidance%20under%20FSA%20BCOBS%20regulation%20consumer%20consultation.pdf**

They went on to say as follows:

"There is a risk that the rules and regulations become so obscure as to undermine the protection available for the consumer. This point could also be made in relation to the Lending Code which is not even recognised by the FSA in relation to its regulatory functions."

With regards to inconsistent regulation there are two main examples that are relevant in relation to claims management companies and cold calling in relation to the mis-selling of Individual Voluntary Arrangements (IVAs). We have outlined our concerns below.

We too have concerns over the current regulation of claims management companies. The provisions of Part 2 of the Compensation Act 2006 do not seem to have „bitten" and the OFT and Ministry of Justice and other stakeholders are well aware of some breathtaking examples of bad practice. These include misleading advertisements, taking money from the public on the basis of totally unsubstantiated claims, cold calling, mis-advising consumers to suspend payments to creditors and so on.

We also note that the Insolvency Service has taken action[11] following concerns about the activities of companies that cold-call consumers and suggest that their IVA has been mis-sold or is faulty in some way. Often, such companies suggest that the consumer should break the IVA by stopping payments, and then charge a fee to "help" them go bankrupt instead. We also note that the OFT has issued requirements against companies who suggest bankruptcy annulment through refinancing.[12] However, whilst we are very pleased that action has been taken, it has taken some time since complaints about such companies first arose, as it was unclear in some circumstances which regulator would be responsible for taking action. This is an example of where a coordinated approach by the OFT and Insolvency Service is necessary to combat these problems and provide redress for consumers.

The free-to-client money advice sector is dealing with an increasing number of enquiries from consumers in relation to cold calling where fee-charging companies offer a debt management service. There are instances where such companies give the impression that they are free advice agencies such as National Debtline. Again this seems to be an area where regulatory powers overlap between the OFT and partner regulatory bodies which can cause delay where new issues arise in

11 **http://nds.coi.gov.uk/clientmicrosite/Content/Detail.aspx?ClientId=95&NewsAreaId=2&ReleaseID=417023&SubjectId=36**

12 **http://www.oft.gov.uk/news-and-updates/press/2010/130-10**

the market and regulators need to coordinate to decide how to investigate and take action. We are very pleased to note that the OFT recently took action against a lead generation firm to deal with illegal cold-calling practices.[13]

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

We would agree that the objectives are mainly laudable, but the detail needs to be right in order to ensure effective consumer protection against unfair practices.

Like MAT, we are concerned that the FSA regime would be a high-level principles-based framework (in contrast to the rules-based approach under the CCA), underpinned by non-mandatory guidance, which would not capture the necessary level of detail or exert the necessary degree of force to be effective.

We believe that the reforms should provide effective mechanisms for the regulator to identify new sources of consumer detriment at an early stage and to take swift action to tackle them. It is vital that there is a proactive and flexible process to enable any new regime to deliver on its consumer protection objectives of consumer protection.

We are concerned that any new regime should not take precipitate action in removing and simplifying regulation without a high degree of research and evidence that the regulations in question are not providing benefits to consumers. The key emphasis should be on retaining and ensuring consumer protections and not easing regulatory burdens on firms. In our experience, there are many firms at the margins who take any opportunity to create a business model out of gaps in consumer protection such as sale and rent back schemes and the current dubious activities by claims management companies. We are concerned that this is likely to happen again unless extreme care is taken.

Question 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.

It would appear that a unified regulatory regime for retail financial services could have a positive impact. We would expect it to be beneficial in terms of clarity for the potential confusion for consumers in relation to regulation of bank accounts to be removed. However, we wonder if the confusion would be mitigated by having a single regulator rather than abolishing the CCA. Much consumer protection is

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[13] **http://www.oft.gov.uk/news-and-updates/press/2010/113-10**

underpinned by different legislation and regulation without this confusing the consumer on a practical level.

A unified regulatory regime would bring greater coherence. However, this should not be overemphasised as it is pointed out in section 2.7, financial services will remain subject to the Consumer Credit Directive and other general consumer legislation.

Improved market oversight will depend upon the resources and enforcement powers given to the CPMA and the relative importance the CPMA gives to taking robust action in relation to the trends and issues identified.

Question 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.

Like MAT, We **strongly support** maintaining the crucial roles of institutions involved in the regulation of consumer credit, including local Trading Standards Services, and the National Fraud Authority. We would urge Government to continue such arrangements under the CPMA. The current FSA model which allows for functions to be performed on its behalf by bodies deemed competent to do so would appear to be a model worthy of replication.

The free-to-client debt advice sector works closely with local trading standards services, the specialist Illegal Money Lending Teams, Scambusters and so on. We consider their work to be vital in tackling consumer detriment against the most vulnerable and marginalized consumers. The new regulator will be regulating many more small firms than the FSA currently regulates – therefore it will be vital for the CPMA to develop links with individual trading standards services, specialist teams and national trading standards bodies (e.g. Trading Standards Institute) and the advice sector.

We do question whether there is sufficient protection afforded to consumers under the current claims management authorisation process.[14] There has been much concern in recent years in relation to the activities of authorised claims management companies in the financial services field. It is particularly important to consider and evaluate whether MOJ have sufficiently robust enforcement powers to monitor firms. We would suggest consideration of incorporating this area within the scope of CPMA activities. In Scotland, there is not a separate agency enforcing claims management companies, and whilst most are already licensed by the Ministry of Justice, there remains a lack of awareness of the different legislative system of Scotland.

[14] **https://www.claimsregulation.gov.uk/index.aspx**

Question 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.

As the paper recognises:

"The current CCA regime provides for a number of important consumer protections that are valued by many stakeholders."

We agree that it is vital that the CPMA builds upon the FSA"s consumer protection strategy, to become proactive in identifying and tackling consumer detriment. However, this is no substitute for the rights and provisions available to individual consumers as a result of the protection afforded by the CCA 1974. The CCA has vital inbuilt rights that must not be diluted by a FSMA style rule book. As the paper states:

"It is unlikely that there would be a direct replication of the existing formulation of all CCA consumer protections in the rule book."

We have reservations as to whether any meaningful, effective consumer protection would be in place if consumer credit were to be regulated in the way in which retail banking services are regulated by the FSA i.e. high-level principles in rules which are not transparent to consumers, plus the provisions of the Consumer Credit Directive that come into force in February 2011.

We have found the detailed guidance produced by the OFT on the meaning and application of the "fitness test" under s25 of the CCA 1974 to different credit businesses and practices very helpful in identifying and challenging bad practice by firms.

Unenforceability of agreements by unlicensed traders

It is vital to deal with the important protections provided by Section 40 of the CCA 1974 which makes agreements entered into by unlicensed traders unenforceable. There is no equivalent to this overriding protection under FSMA rules. This needs to be retained.

Another potential dilution of consumer protection that might arise under a FSMA style regime is that at present, non-compliance with the detailed rules on documenting the credit agreement and on providing information subsequently, renders the agreements unenforceable (except on an order of the court) whereas there is nothing equivalent in FSMA 2000. On the contrary; agreements are explicitly not affected by rule breaches: FSMA, S151 (2) although the Act does give a right of action for loss under s.150.

Prescribed terms in consumer credit agreements

We cannot support a rule book that would allow any variations in style, wording and presentation of credit agreements. This would lead to consumer confusion, make the task of enforcement of compliance harder and make it extremely difficult to take action against lenders for any breach or for consumers to challenge their agreements. There need to be prescribed terms and conditions for all agreements. There are provisions under the Consumer Credit Directive governing the terms of agreements which would have to be retained but we are concerned that these do not go far enough. The CCA includes detailed provisions for the form and content of credit agreements and how copies of documents must be provided. These need to be retained along with sanctions for non-compliance.

Time orders

The right to apply for a time order under section129-136 of the CCA 1974 is a vital tool used by money advisers when assisting a consumer with debts. This allows the court to reschedule the payments under a regulated agreement when a borrower is in financial difficulties. This can result in a reduction in the payments, interest and charges and prevent further enforcement action by lenders. Such provisions are particularly helpful in second charge lending cases, hire purchase and where payments and interest rates on unsecured credit are excessive.

Although in Scotland we have Time to Pay Directions (pre –decree) and Time to Pay Orders (post decree and diligence stopper) these remedies do not permit the court to re-open the credit bargain, which in many instances is entirely desirable, especially in the case of sub prime lending.

We understand that regulation of second charges will be transferred to FSMA and removed from CCA protection. We are extremely concerned that the vital protections of time orders and unfair relationship provisions for second charge borrowers under the CCA are not lost. FSMA rules need to be amended to incorporate both time order provisions and unfair relationships provisions. We also agree with MAT that if time order type provisions were available under MCOB for first charge mortgages, that many of the provisions such as the Homeowner Mortgage Support Scheme would have been unnecessary.

We have long argued for improvements in the law relating to time orders, and indeed it was the situation in Scotland for some time that no form was available for anyone to make a Time Order application. In our view, the process of applying for time orders can be expensive, requires legal advice in certain instances, can be time consuming and obscure, and do not apply to most borrowers. However, for those debtors who could benefit, it could make a real difference to their overall situation. The amendments introduced in October 2008 under the Consumer Credit Act 2006 (CCA 06) will make little difference in practice.

Unless the issues that have arisen relating to the definition of “temporary” financial difficulties are resolved, a time order remains an unreliable remedy for those in debts outstanding on CCA-regulated loans.

However, **we remain strongly supportive** of a revised and more flexible equivalent to the time order provisions. There needs to be a mechanism in place to allow consumers to reschedule payments under an agreement when a borrower has financial difficulties in relation to not just the monthly payments, but the terms and conditions, and consequent interest rate and charges.

The 'unfair credit relationships' test

There is no equivalent in FSMA of the unfair credit relationships test which was introduced by the 2006 Act under section 140A of the CCA 1974. This provides the court with wider powers to release security, rewrite agreements and liabilities. In contrast, consumers only have a right of private action for damages for similar practices under FSMA.

Whilst we believe that actions to challenge unfair credit relationships could be made more accessible to consumers, we remain strongly in support of this part of the Consumer Credit Act.

Voluntary termination

We believe that the provisions within ss99 and 100 are essential to protect the rights of consumers who have entered into hire purchase and conditional sale agreements and who are no longer able to afford the payments. MAT suggested in its coordinated response to the "BIS consumer credit and insolvency call for evidence"[15] that there is a need to issue guidance regarding these provisions in order to make it crystal clear that consumers retain an automatic right to voluntarily terminate their agreement until the point when the agreement has been terminated by the lender. We believe that this protection should remain if regulation of consumer credit is to pass to the CPMA.

Second mortgages/secured loans

We note the announcement by HM Treasury[16] that the Government intends to transfer the regulation of new and existing second charge residential mortgages from the Office of Fair Trading (OFT) to the Financial Services Authority (FSA). We would welcome the announcement that there is to be put in place a single regulatory framework for all secured lending. However, it is unclear what will happen to key elements of the CCA protection such as unfair credit relationships and revised time order provisions. This could extend court powers to allow interest

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15 **http://www.moneyadvicetrust.org/images/MAT%20coordinated%20response%20to%20the%20BIS%20consumer%20credit%20and%20insolvency%20call%20for%20evidence.pdf**

16 **http://www.hm-treasury.gov.uk/fin_sector_mortgages_enhancing_consumer_protection.htm**

and default charges to be frozen and for consumers to stay in their homes whilst paying less than the contractual amount if necessary. In Scotland through the Debt Arrangement Scheme, providing a debtor pays their debt in full over an extended period, then the interest will be frozen and not payable.

The right of complaint to the Financial Ombudsman Service must be retained and the FSA regulatory powers should also be incorporated along with the OFT Irresponsible Lending Guidance and the OFT Second Charge Lending Guidance. We would urge Government to adopt these elements into the new regulatory regime.

Post-contractual obligations

The CCA 2006 introduced important rights in relation to annual statements, arrears and default notices. This includes the statutory requirement to send information sheets to consumers who may be falling into debt. From the advice sector perspective, such a requirement with prescribed wording is vital to preserve to ensure that all lenders abide by the regulations and provide information in a common, plain English format and include the prescribed list of free-to-client advice providers. It is also essential that debtors in Scotland are given choice as to the providers of advice, and that all potential providers (including local authorities which provide significant services) or sign-posters (such as MAS) are included in the information sheet. It is also vital to preserve the sanctions of temporary unenforceability of the agreement against non-compliance by lenders. This concept is unknown under FSMA and could be lost in the regulatory transfer.

Linked credit agreements

The provisions under section 75 and 75A of the CCA provide extremely important protection for consumers in relation to the joint and several liability of card companies for breach of contract by a retailer and other claims against suppliers. These provisions should be retained.

Question 8 The Government would welcome further evidence relating to:

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

Business Debtline provides advice and assistance to small businesses. These may be sole traders, small partnerships or small limited companies. Typically, a small limited company will consist of a managing director and a company secretary or 2 managing directors in total.

In the experience of Business Debtline, the use of consumer credit by SMEs is common in the form of hire purchase, lease agreements and both fixed sum and running-account credit.

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

At present the protections afforded by the CCA do not even extend to small limited companies. Consequently, these types of SMEs are bound by the specific terms and conditions of their contractual agreement. In the experience of Business Debtline, collections and recovery processes for these types of SMEs are more aggressive. Often small limited companies can find it difficult to get information about their contract and creditors can often withdraw or reduce funding without sufficient notice which can result in immediate closure of the business. This is particularly unfortunate where greater forbearance could result in trading out of the difficulties and saving the business.

It is the case in Scotland also that advisers see clients whose business debts are intermingled with personal debts. Many taxi drivers are sole traders or in partnerships and often seek advice.

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

Costs: loans to small limited companies will not benefit from these provisions and they will still remain outside the scope. Although the rules would extend to a wider group of SMEs in relation to the level of debt that would be covered, the protection for small limited companies would not be there.

Benefits: In the opinion of Business Debtline, the majority of SMEs do take credit that is higher than the current £25,000 limit under the CCA. Therefore, extending the rules to a wider group would afford them more protection and could in the long run save businesses.

Question 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.

We, like MAT believe that a rule-based regime could provide a regulatory regime which is inherently more flexible and responsive than a regime set out in legislation. We appreciate that primary legislation is difficult to amend in the light of market developments and that it is more difficult to respond swiftly to emerging practices. For example, if the OFT had had rule making powers, it could have quickly tackled the bad practices by firms providing credit by bills of sale.

However, our main concern with rules-based regulatory regimes is that they can be high level. For example, the rule book will often use terms such as "reasonable" "treating customers fairly" and "dealing fairly". These are clearly open to interpretation by individual companies, consumers and their representatives.

In comparison, the OFT can impose requirements on individual firms to tackle their specific bad practices – a power that the FSA does not have. However, these requirements do not have the same positive force on the whole industry as rules. In our view it is essential that case studies and the like are provided to show what is good practice and what isn‟t acceptable.

We therefore suggest that the Government look at giving the CPMA new rule-making powers which are linked to the requirement regime.

The other problem with a rules making regime is that it is likely to be ineffective in markets which are very diverse. The FSA struggled to tackle the irresponsible lending and harsh arrears practices exhibited by sub-prime lenders as MCOB assumed all lenders would be the same, and the rules regime made the FSA blind to problems arising in different segments of the mortgage market. Consumer credit is a very diverse market, with many different types of products, including payday loans, bills of sale, hire purchase and buy as you view, and not just credit cards and personal loans. The CPMA will need to undertake swift and surgical micro-interventions to tackle consumer detriment.

Question 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 believe that the FSA‟s supervisory regime could ensure effective and appropriate consumer protection. The FSA should avoid intervening only when there is overwhelming evidence of consumer detriment as can happen under current regulatory regimes. However, it is vital the CPMA draws on the experience and expertise of current regulators such as OFT staff when they take over regulation of consumer credit. The OFT know which companies are causing detriment. It is essential that the CPMA forge better links with the advice sector in a similar way to that of the OFT. By working closer together, and identifying possible detriment can result in a quicker positive response.

We understand that the new CPMA model will be given new tools and powers. It is also the intention for it to be keener to intervene and to intervene earlier than under the FSA regulatory regime. Without firm details of the proposed new powers, it is difficult to comment on the impact this will have on ensuring effective and appropriate consumer protection.

We agree with our colleagues at MAT and we have major concerns that a high level rules-based approach will be insufficient in preventing detriment to consumers. We have found that attempting to interpret broad-brush rules such as the concept of “treating customers fairly” is difficult to do. Where firms are able to put their own interpretation on concepts such as “reasonableness” it is more difficult for consumers and their advisers to challenge an individual company.

As an example, under the MCOB rules 13.3[17] it is required that mortgage lenders:

"Allow a reasonable time over which the payment shortfall or ***sale shortfall*** *should be repaid, having particular regard to the need to establish, where feasible, a payment plan which is practical in terms of the circumstances of the* ***customer****."*

A "reasonable time" has been interpreted very differently over the years by both lenders and ultimately the courts. Advisers find that lenders typically suggest a very short repayment period of 1 to 2 years as being a reasonable time period[18] The Administration of Justice Act 1970[19] sets out the court‟s powers in relation to possession for mortgage arrears, and it states that it can only exercise its powers to delay possession if the borrower can demonstrate that they can pay their contractual mortgage instalment (CMI) and clear the arrears „within a reasonable period.‟ Case law suggests the period could be as long as the remaining term of the loan.[20]

As a result, we would suggest that MCOB 13.3 is not sufficiently prescriptive and is too open to interpretation.

This example illustrates why we would therefore generally favour a greater level of prescription with rules that are less open to individual lender interpretation.

It is worth pointing out that in Scotland the new legislation – Home Owner and Debtor Protection (Scotland) Act 2010, prescribes the "pre- action requirements" which a lender must adhere to before repossessing property.

Question 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 agree that the current regime where the OFT has responsibility for both consumer credit and general consumer protection, means that there is a coherent view of all aspects of a business providing the sale of goods and services on credit. It is vital that these protections are preserved. As it is possible that the OFT will be abolished at around the same time, it is vital that the FCA can enforce

[17] **http://fsahandbook.info/FSA/html/handbook/MCOB/13/3**

[18]

http://www.citizensadvice.org.uk/index/campaigns/policy_campaign_publications/evidence_reports/er_consumerandebt/turning_the_tide_
http://www.citizensadvice.org.uk/index/campaigns/policy_campaign_publications/evidence_reports/er_consumerandebt/set_up_to_fail-2

[19] Section 36, as amended by section 8 of the Administration of Justice Act 1973
[20] (*Cheltenham & Gloucester BS v Norgan* (1995) 1 All ER 449)

breaches of the CPRs and Unfair Contract Terms legislation. This will mean close working with Trading Standards Services.

As the paper points out under paragraph 2.10, the aim is that the FCA:

"..will continue to have concurrent consumer protection powers where another body is the lead enforcer of a general piece of consumer protection legislation."

We suggest that the relationship with the OFT continues with regards consumer protection. The CCA licensing fitness test has only recently bedded in following the Consumer Credit Act 2006 changes. The benefits of the new process are now beginning to be realised as the OFT has stepped up its enforcement work in relation to fitness requirements in the latter part of 2010. This work should not be lost in a transfer to the FCA.

Question 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)?

We can appreciate that the transfer of consumer credit regulation to a FSMA-style regime would appear to support the Government‟s objectives in some areas.

Whilst simplification and deregulation are important principles, our major consideration is consumer protection rather than removing the regulatory burden on firms.

However, our main concern relates to the objective of achieving "effective and appropriate consumer protection." A FSMA style regime will not be able to maintain or strengthen protection for consumers unless a wide range of the consumer protection provisions that exist under the CCA are maintained or enhanced. We have given examples of our concerns in response to question 7.

We are also concerned that the powers under the Enterprise Act 2002 will also be lost in relation to consumer credit. We have outlined our concerns in response to question 3. As we have said, there is no equivalent provision to section 11 of the Enterprise Act 2002 under FSMA rules to allow the FSA or CPMA to take such swift and effective consumer protection action.

Question 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?

We have outlined our main concerns throughout the response to this paper.

We feel that the right to order redress for individual consumers is an extremely important power held by the FSA which could be available to all consumers with financial services problems.

However, we note the work of the OFT in developing a civil sanctions pilot which will run from April 2011. This will allow;

"the provision of voluntary restoration to consumers who suffer detriment as a result of unsafe products or unfair or misleading business practices".[21]

There will be criminal sanctions for non-compliance.

As we identified in our response to question 7, there are a number of crucial elements of the CCA 1974 that would need to be replicated within a FSMA rules based regime. Without these vital protections for consumers we would find it difficult to support the transfer.

As identified earlier, we are concerned as to how the work of Trading Standards will be incorporated into the regime, given the already stretched services.

Question 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 have concerns over the costs that will be incurred for the free-to-client debt advice sector. There is an enormous body of both online and paper based training materials and training courses that would need to be redeveloped by organisations such as Money Advice Trust under Wiseradviser,[22] Citizens Advice for their training and information systems, the Institute of Money Advisers training programme[23] , and Money Advice Scotland who work very closely with their members, who range from money advisers, through to Insolvency Practitioners.

There are then the related expenses of implementing the training across the free-to-client money advice sector. Specialists would need to develop their own expertise whilst discarding a wealth of knowledge of consumer credit law and case law to rewrite and republish handbooks and information systems with the related costs of doing so and with limited resources. Also, organizations will indeed have purchased various law books, which come at a price.

[21] **http://www.oft.gov.uk/shared_oft/consultations/OFT1296.pdf**
http://www.oft.gov.uk/news-and-updates/press/2010/147-10
[22] **http://www.moneyadvicetrust.org/content.asp?ssid=3**
[23] **http://www.i-m-a.org.uk/training.html**

We are interested to find out what the legal status would be of the vast existing body of caselaw relating to the CCA if the changes were to be implemented.

Like MAT we have worked closely with the OFT in the development and review a range of statutory guidance which represent invaluable tools in providing practical support when assisting debt advice clients and dealing with lenders and creditors who must have regard to the guidance. These include the following in particular:

- *The OFT Debt Management Guidance (currently under review)*
- *The OFT Debt Collection Guidance currently under review)*
- *The OFT Irresponsible Lending Guidance*
- *The OFT Second Charge Lending Guidance*
- *The OFT Mental Capacity Guidance (subject to consultation)*[24]
- *The OFT Consumer Guidance on Section 77-79 CCA*

We do not see FSMA style rules as an adequate substitute for the detailed guidance provided by the OFT. If the Government decides to go ahead with option 1 we would wholehearted support MAT in their view that we would want to see the equivalent of the OFT guidance incorporated into any new rule book.

We also greatly value the approach the OFT has taken to working with consumer groups, including the free-to-client money advice sector. The OFT has taken a very interactive and consultative approach which we feel has been very productive. We believe that this approach should be replicated in any new regime.

We have greatly benefited from the OFT having an office based in Scotland with the Representative in Scotland acting as a conduit to our colleagues in London. As an organization we had urged the OFT for many years to site an office in Scotland. We would expect to see the same presence from any new regime, and working in the same constructive way with the advice sector, as in the case of the OFT.

Question 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?

We recognise that the CCA 1974 has developed in range and complexity over the years. We also recognise that there would be advantages in a regime that would enable speedier amendment than through the current legislative route. However,

[24] **http://www.oft.gov.uk/about-the-oft/legal-powers/legal/cca/mental-capacity-guidance/**

we are not convinced that a move to a FSMA rule based regime and the repealing of the CCA would be a proportionate response on grounds of complexity, cost and related transitional confusion for both lenders and consumers. We would seek substantial reassurances that the protections afforded by the CCA would not be lost. There appears to be little guarantee that key protections would be preserved. As an example we would reiterate the points MAT made in relation to the HM Treasury Mortgage Market Review paper on second mortgage regulation.[25]

"Whilst we welcome the proposal that the same regulatory regime should apply to all mortgages and secured loans, we do not agree that a simple migration of responsibility from the OFT to the FSA would be enough to achieve the Government‟s objective. Instead, we would like to see an equalisation of the two markets, based on taking the best consumer protection measures from both the Consumer Credit Act (CCA) regime and that of the Financial Services and Markets Act (FSMA). We suggest that a market that is „fair, stable and efficient‟ is a market with consistent and meaningful consumer protection. Such protection must cover pre and post-contractual matters including selling, lending, arrears management and individual consumer redress when things go wrong. We are concerned that it would be a missed opportunity if there was an extension of the scope of FSA mortgage regulation to include second-charges, without incorporating such provision."

We do not have any developed views as yet on the factors the Government should take into account in determining the most appropriate regulatory authority. We are mainly concerned that the OFT‟s powers, expertise and experience and their body of guidance work are not lost.

Question 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.

Overall, we believe that the provisions of a FSMA-style regime could lead to a tougher regulatory regime for consumer credit businesses:

The authorisation and threshold conditions will be considerably tougher under the FSMA regime, compared to the current OFT regime. However, we would caution the CPMA to be wary of exempting small firms from these – in our experience small credit firms come up with new products, often aimed at marginalized groups of people, which cause a great deal of consumer detriment. **It would be completely inappropriate** to exempt small firms from these procedures.

25 **http://www.moneyadvicetrust.org/images/MAT%20coordinated%20response%20HM%20Treasury%20consultation%20mortgage%20regulation%20FINAL.pdf**

Fee arrangements – this could be based on a percentage of turnover of the firm. We believe that the CCA regime has not charged large multi-national firms enough in fees.

Systems and control requirements – we believe that the FSA has a better handle on these

Conduct of Business rules – as we have argued strongly throughout this response, these will need to be effective, detailed and preserve current consumer rights, if they are to be effective in preventing detriment.

Prudential requirements – we believe that these could be vital even for small consumer credit businesses to ensure that they lend responsibly.

Reporting requirements – there are no reporting requirements currently in the CCA regime. These could be onerous for small firms, so the CPMA could consider exempting small firms from some of these requirements. However, we would warn against exempting small firms from all the requirements – as small firms often cause considerable consumer detriment, and they are operating in the customers area and know the customers circumstances, almost as well as the debtor themselves.

Enforcement provisions – with the exception of the requirements regime, the FSA have much better enforcement powers compared to the OFT. They can impose unlimited fines (OFT can only charge £50,000 maximum) and can order firms to compensate affected consumers.

The free-to-client debt advice sector are mainly covered by the OFT group licensing scheme. This provides “light-touch” regulation but requires compliance with the relevant provisions of the OFT Debt Management Guidance (where it relates to the free debt advice sector). We would suggest an equivalent to the Guidance would need to be in place to cover the activities of both free debt advice services and the fee-charging debt management company sector.
As evidenced by the OFT Debt Management Guidance Review, the fee-charging **debt management company sector is categorised as a high risk area** and should continue to be treated as such.

Question 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?**

With regard to the risk-based approach this appears to match the approach taken by the OFT who have identified the following credit activities as being high risk licence categories.[26]

D - debt adjusting
E - debt counselling
F - debt collection
H1 - credit information services (including credit repair)

These categories of business are then subject to a higher level of scrutiny and be required to demonstrate credit competence. With the OFT"s enhanced powers following the Consumer Credit Act 2006, we are beginning to see the results of this approach. The OFT are starting to take increasing numbers of actions by way or requirements and revocations against companies who contravene the licensing principles. It is vital that the increasing effectiveness of this work is not lost going forward.

However, for groups that have been identified as lower risk, the intention outlined in section 3.17 of the paper to rely upon "regulatory returns and complaints-led intelligence" leads us to reiterate concerns that MAT have previously expressed in responses to previous consultation papers that poor practice may continue to fall through the gaps in regulation. In the MAT response to the BERR Consumer White Paper[27] they said:

"We applaud the current work of the OFT and other licensing bodies and regulators in tackling bad practice, but often this work is not timely enough, nor does is appear that the relevant organisations possess sufficient power to regulate as effectively as we might hope. A significant proportion of investigations rely upon individual consumers being prepared to make formal complaints to regulators that will help to build up a body of evidence. There is little incentive for the consumer to cooperate as for example the OFT is specifically prevented from dealing with individual complaints on a case-by-case basis, and is also unable to let the consumer know the outcome of their investigations in any formal way."

(This is due to restrictions under Part 9 of the Enterprise Act 2002 which prevents the OFT from identifying businesses that are subject to requirements or warnings or under investigation.)

We are therefore not confident that without reform of the problems with complaint mechanisms under CPMA, that a risk-based approach can rely upon the ability of consumers to make complaints with no possibility of redress or recognition. Also, it is self-evident that in order to complain, the consumer must be able to identify the issue as causing them detriment. In many cases, this will not happen as the

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[26] **http://www.oft.gov.uk/OFTwork/credit-licensing/credit-licence/riskcategories**
[27] **http://www.moneyadvicetrust.org/images/MAT_response_to_BERR_Consumer_White_Paper_Issues_Paper_May_2009_%20FINAL.pdf**

consumer is unaware they have been sold a toxic product.

We welcome the concept of proportionality in relation to fees and the recognition that exceptions to the general approach are permitted such as for credit unions. We would argue that those eligible currently for the group consumer credit licence for free-to-client debt counselling advice agencies should continue to be licensed free of charge.

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

We would suggest that it would be vital to take into account the OFT review of consumer credit licensing fees.[28] Fees should be allocated fairly between different types of licensed firms. It is clearly not proportionate that a small limited company would pay the same fee as a large bank. Any revised system should be able accurately to reflect the different costs of regulating different types of business under the regime.

"The CAB disagreed with the simplistic approach suggested within the consultation paper. They responded that the OFT should devise a system for charging fees that weighs the level of risk presented by an application against the size of the business, into a matrix. The CAB also requested that OFT should consider whether the use of an on-line fees calculator, such as that used by FSA, would negate the drawbacks of a more complex system which were highlighted in the consultation paper."[29]

In setting fee levels the FSA or CPMA would need to take into account the appropriate level of fee relating to the regulatory scrutiny required by different types of consumer credit activity. We would urge any fee setting to fully take into account the OFT"s experience of dealing with the increased risk associated with certain types of licence activity such as fee-charging debt management companies and so on.

Question 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

[28] **http://www.oft.gov.uk/OFTwork/consultations/closed/2010/cclf**

[29] 2.42 **http://www.oft.gov.uk/OFTwork/consultations/closed/2010/cclf**

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

We do not have any relevant evidence to provide relating to the current appointed representatives regime.

Question 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.

As free-to-client money advice providers who are part of the current group licensing regime, we would suggest that the current scheme has worked very well. We believe that it is important for our sector to be regulated.

We believe that the FSMA professional body regime could be adapted to meet the needs of the group licensing regime for charitable free-to-client debt advice providers.

However, we question whether the evidence relating to the fee-charging debt management companies" trade associations ability to self-regulate would justify extending this regime to either debt management companies or insolvency practitioners. (See our answer to question 21). Alternatively the Government could consider using the provisions in the Financial Promotions Order to devise carve-outs for charitable free-to-client debt advice providers.

Question 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 value the extremely important work of the Lending Standards Board in developing and monitoring the Lending Code as a voluntary code of good practice. This is an example of self-regulation working relatively well. However, this is due to the major trade bodies co-sponsoring the code and a commitment by major lenders to subscribe to the provisions of the Lending Code. Subscription remains on a voluntary basis and there can be difficulties in ensuring all subscribers comply with the Code. . The Code is subject to an external independent review but subscribers cannot be forced to accept any proposed revisions. This reduces the effectiveness of the Code as it can be affected by subscribers" own interests.

Other trade bodies have much less effective self-regulatory codes. Often, the content of voluntary codes can be subject to interpretation. This makes it difficult to take a consistent approach and it can be hard for advisers and consumers to work out what phrases such as "positively and sympathetically" mean in practice. This makes it harder for consumers to call companies to account in relation to a particular code.

However, we have had previous experience where self-regulatory codes are prevented from being effective because membership is voluntary. Where there is no membership requirement then despite good work on developing a code of practice, the trade body will have no ability to force non-member companies to comply. Lack of regulation and enforcement powers against members are also a major concern. We would also question the independence of the role of a trade body in policing its own members. There are also likely to be issues of the body having sufficient resources to carry out an effective monitoring and enforcement strategy that will have the ability to identify and discipline members where necessary.

As an example, within the debt management industry, there are two trade bodies[30] who each cover only a very small number of debt management companies. They have differing codes of practice and membership requirements. Recent merger talks have reportedly foundered.[31] Many companies operate without being members of either trade body.

The recent OFT Debt Management Compliance Review[32] found widespread non-compliance with the OFT Guidance and many instances of bad practice.

The proposals in the paper to formally incorporate the provisions set out in existing voluntary codes may be a way forward. We would advocate regulatory control rather than devolving such powers to self-regulation and guidance. If self-regulation was to continue, compulsory membership would be required at the very least.

Question 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 unable to identify any categories of consumer credit activity that would be suitable for deregulation at present. There is a danger of such deregulation resulting in unintended consequences for consumers and an erosion of the current protections. If there were any such areas identified, we would suggest careful research and analysis of the particular activity would be required to explore the

[30] DEMSA **www.demsa.co.uk/**
Debt Resolution Forum **www.debtresolutionforum.org.uk/**

[31] **http://www.debtresolutionforum.org.uk/news/**
[32] **http://www.oft.gov.uk/shared_oft/business_leaflets/credit_licences/OFT1274.pdf**

possible consumer detriment that could result. An equally robust substitute scheme would need to be in place to ensure effective protection for those consumers affected.

We would caution against any temptation to water down protections by way of a code of practice or similar. Many trade bodies have codes of practice in place but if there is no requirement for membership of the trade body and where the body does not possess the resources to provide effective and rigorous investigation of their members, this cannot be a substitute for regulation.

We note that the paper makes the suggestion that in some cases control via other parallel regulation or professional standards would be sufficient. The example given relates to whether:

"Charities Commission rules provide adequate safeguards for the clients of free debt advice provided by charitable organisations."

We are not confident that the Charity Commission rules (or the Office of the Scottish Charity Regulator in Scotland) provide sufficient safeguards for clients of free debt advice. Such deregulation would be no substitute for the protection afforded by the OFT group licensing scheme and the requirement to adhere to the provisions of the OFT Debt Management Guidance. Achieving charitable status gives no indication of the professionalism and quality of the service being provided in such a specialist area where clients of such services are likely to be especially vulnerable and subject to extreme detriment if the service is inadequate or negligent.

Question 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 are unable to put forward any further suggestions at this stage.

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

It is extremely important that the transitional provisions are clear, straightforward and treat consumers with existing agreements fairly.

From a consumer perspective much depends upon the extent to which existing rights under the CCA have been transferred into the new regime. We cannot see it as fair that from a certain date, contractual rights that existed when the agreement was entered into become invalid and unenforceable by the consumer. If for example, no equivalent to the time order provisions is established under the new rules, then vital existing protections for consumers with current consumer credit agreements would be lost. As the paper states at point 4.14:

"However, if the CCA gives significant additional rights and protections, consideration would need to be given to maintaining them unless a CPMA rule can be put in place for existing agreements that offers at least as much overall protection for the consumer. In addition, transitional arrangements would be needed to address processes underway at the date of repeal of the CCA, including, for instance, prosecutions, other legal actions and periods of right of withdrawal."

Under previous changes in the protection afforded to consumers with existing agreements such as the CCA 2006, existing agreements retained their additional protections (such as those relating to the automatic enforceability of agreements). New provisions only applied to new agreements entered into on or after a certain date. However, we appreciate that some new rights and protections can be granted from a set date to all existing agreements where that right is deemed advantageous and does not diminish existing rights. An example of this again relates to the CCA 2006 where the right to complain to the Financial Ombudsman was granted to consumers with existing credit agreements from a set date (although only for disputes that arose from that date onwards).

This example was in the context of the CCA 2006 being an amending Act and not replacing the entire CCA 1974 and rewriting the rules under a new regulator. However, the time, legal complexity of implementation and the costs to the credit sector, advice sector and Government were substantial.

Question 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 would expect existing consumer credit licence holders to have to demonstrate that they meet the different and enhanced requirements for FCA regulated firms on application. Whilst we appreciate there would need to be a lead in period, it does not appear proportionate to grant automatic authorisation as a regulated firm under the FCA where the firm has not demonstrated it is able to meet the higher requirements. Such an approach could have a detrimental effect on consumer protection.

The Government should therefore consider using the approach the FSA used to take on regulation of sale and rent back firms – a transitional period where the full regulatory regime does not apply, but which allows them time to adapt to the full regime. If they have not met the full requirements of the new regime by the end of the transitional period, they must cease to trade.

Alternatively applications could be staggered, perhaps enabling dual licensing under the CCA and FSMA rules for a set period with a cut-off date.

Question 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 firms could simply pay the difference between the OFT fee regime and the fees required by the new FCA regime. Clearly any transitional fee structure needs to be fair to those subject to the transfer from the current fee structure. There would need to be appropriate notice provided with a lead-in time to ensure this works.

We would urge the retention of an equivalent to the group licensing regime for free-to-client debt advice providers and other bodies within the regime. This should continue to be free of charge to those organisations that come under the scheme as these are not-for profit charitable bodies.

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

Yes. We believe that the Government should not let the planned reform of the regulatory system mean that vital reforms to consumer credit are deferred. We would suggest that a delay until 2014 for any further changes to take place would cause consumer detriment and would not be acceptable.

Question 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.

This is outside our area of expertise as we have no particular experience of similar previous transitions.

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Money
Advice
Trust

HM TREASURY & BIS REFORMING THE CONSUMER CREDIT REGIME CONSULTATION PAPER

Response by the Money Advice Trust (March 2011)

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Introduction

INTRODUCTION

About the Money Advice Trust

The Money Advice Trust (MAT) is a charity formed in 1991 to increase the quality and availability of money advice in the UK. We work with the UK's leading money advice agencies, government and the private sector to increase the availability of money advice, improve its quality, and enhance the efficiency and effectiveness of its delivery.

MAT's vision is to help people across the UK to tackle their debts and manage their money wisely. MAT aims to support individuals and micro-businesses in the UK through their debts and into financial health, and to improve the capability, quality and efficient delivery of free independent money advice by:

- *Delivering advice to the public via National Debtline, Business Debtline and My Money Steps;*
- *Supporting advisers;*
- *Making the case for free money advice;*
- *Co-ordinating initiatives to improve money advice;*
- *Sharing research and information to shape and influence policy.*

How we have drawn up this response

In preparing this response, we have consulted our partner agencies in the free-to-client money advice sector in order to achieve a consensus view. These partners include:

- *Advice NI*
- *Advice UK*
- *Citizens Advice*
- *Citizens Advice Northern Ireland*
- *Citizens Advice Scotland*
- *Institute of Money Advisers*
- *Money Advice Scotland*
- *National Debtline and Business Debtline (where relevant)*
- *Payplan.*

Some of these partner agencies will also submit their own separate responses to this consultation paper. These submissions may include issues not covered below.

Please note, our partner agencies may not have provided views on this response where this consultation paper does not cover their specific jurisdiction.

Please note that we consent to public disclosure of this response.

Introductory comment

We welcome the review of the current regulatory regimes for financial services and we value attempts to simplify and unify regulation and consumer protection for financial services.

We are concerned that a rules-based regime could be a high-level principles-based framework (in contrast to the detailed regulation-based approach under the Consumer Credit Act), underpinned by non-mandatory guidance, which would not capture the necessary level of detail to be effective.

We are reluctant to lose the consumer rights contained in the Consumer Credit Act 1974 (CCA) protections without ensuring that there are robust protections in their place. Without being able to see the details of the new proposals it is difficult to comment on the best approach. In this paper we outline what measures we value under the CCA and our areas of concern.

We support neither option 1 nor 2 which are outlined in the consultation paper. We believe that the best way to protect consumers and to regulate financial services is to take the best of both the FSMA and CCA regimes, and to avoid the failures of both of the current regimes.

In order to achieve this, we would urge Government to ensure that there are sufficient resources to ensure that the new regime can be put into effect to create an effective, coherent and comprehensive regulatory regime. There is a danger that if resources are too limited that the reforms will not work as intended.

Responses to individual questions

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

The assessment of the current market as outlined in sections 1.8 to 1.10 of the paper is reasonable in its aim to

"facilitate the right outcomes for consumers while being proportionate to the risks posed."

Regarding the assessment of the consumer credit market as outlined in the paper, we would point out that the growth of the sub-prime credit market is of particular concern to the free-to-client debt advice sector. The increase in very high interest lending such as payday loans and pawn broking adds to the debt burden for those in financial difficulties. Effective regulation and control of this sector is of paramount importance to avoid further consumer detriment. This is of course in addition to effective regulation of mainstream credit as the majority of people in debt will have debts to mainstream credit providers.

The consultation paper mentions the rise in people struggling to pay debts. We would draw your attention to the recently published Money Advice Trust and University of Nottingham "Demand, capacity and need for debt advice in the UK" research.[1] This predicts that:

"If unemployment continues to increase as suggested by a number of independent forecasts, by mid-2011 demand for advice will exceed that seen at the peak of the financial crisis in late 2009."

Question 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 can see that on the face of it, having a single regulator accountable for the performance of retail financial services covered by one regulatory regime would appear attractive. However, we strongly believe that effective consumer protection measures are the best way to ensure that the primary objective of the Financial Conduct Authority (FCA) CPMA, of ensuring confidence in financial services and markets is met.

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1 **http://www.infohub.moneyadvicetrust.org/content_files/files/demand_capacity_and_need_for_debt_advice_in_uk.pdf**

We have previously raised concerns in relation to the issues raised by an over-reliance on competition. We believe that competition does not make financial services more accessible to people on the lowest incomes or who are vulnerable in some way or protect them from unfair practices.

As an example this is what we said in our response to the OFT Financial Services Strategy consultation in 2009.[2]

"Potential competition does not guarantee fairness, and in some circumstances a tension arises between the two principles. For example, on a macro-economic level, the widespread acquisition of toxic debt that triggered the current crisis, was an example of competing entities seeking to gain a 'profit' edge in a 'free' and loosely-regulated environment.. As a general principle, then, a balance has to be struck between protecting consumers, via regulation, from externally-generated risks created by an unstable market on the one hand, and allowing for sufficient competition to enable a reasonable level of consumer choice on the other.

As there is no magic formula that will guarantee a perfect balance between these elements, and in cases where there is apparent conflict between competition and fairness, we would argue in favour of safety over choice, since the overall negative impact of consumer exposure to risk is likely to last longer and be more damaging than the effect of a reduction in the availability of credit products."

We also wish to highlight concerns we have raised regarding regulation in the past. In the Money Advice Trust response to the BERR Consumer White Paper, we stated as follows:

"Government departments and regulators engaged in licensing and regulation often find themselves in the situation of shutting the stable door after the horse has bolted. This means that consumers may well have been victim to rogue companies, bad practice, or toxic products for years, before effective action can be taken to address the problem.

We would welcome a more proactive approach to consumer credit regulation, aimed at preventing the problems caused by unfair products, services and practices from proliferating in the first place. We would draw an analogy with the Food Standards Agency and the speed with which it can act if a dangerous product comes on to the market. We would also make the point that today, as soon as one company is closed down for bad practice; another appears in its place. We need a flexible and innovative regulatory structure with the ability to act timeously and decisively to reduce the proliferation of bad (and sometimes illegal) practices examples of which are provided below.

[2] **http://www.moneyadvicetrust.org/images/MAT_response_to_OFT_Financial_Services_Strategy_consultation_paper_(2).pdf**

We applaud the current work of the OFT and other licensing bodies and regulators in tackling bad practice, but often this work is not timely enough, nor does is appear that the relevant organisations possess sufficient power to regulate as effectively as we might hope. A significant proportion of investigations rely upon individual consumers being prepared to make formal complaints to regulators that will help to build up a body of evidence. There is little incentive for the consumer to cooperate as for example the OFT is specifically prevented from dealing with individual complaints on a case-by-case basis, and is also unable to let the consumer know the outcome of their investigations in any formal way. This is most unsatisfactory where individuals may want redress for their own problem (in which case they must use FOS) but would also like their experience to help others (in which case they must complain to the OFT as well)."

We welcome the declaration in paragraph 1.5 that the CPMA (now FCA)

"will take a tougher, more proactive and more focused approach to regulating conduct in financial services and markets than has the FSA".

We would suggest that the regulator covering consumer credit issues needs to have improved regulatory powers and resources to pro-actively police compliance and conduct enforcement against companies in breach of regulations. The current system is hampered by the difficulties in enforcing breaches of guidance against individual companies. The Consumer Credit Act 2006 led to an improvement in the licensing regime but action is still generally reactive against individual companies where enhanced power to prohibit bad practices and conduct across the board is required.

As an example, we are aware of OFT credit licensing revocation cases that are drawn out for years under appeal, allowing the trader to still operate and cause detriment to individual consumers. There needs to be a robust time-limited appeal system in place. There also needs to be enhanced powers to provide redress for consumers and to do so retrospectively where harm has been identified.

However, the full effects of the enhanced powers given to the OFT under the CCA 2006 are only now bearing fruit. There has been a marked increase in actions taken by the OFT in 2010 in relation to requirements and licence revocations.[3] These are in relation to areas where the free-to-client advice sector have been active in raising concerns such as in relation to the use of charging orders, debt management company practices, "look-alike" websites (debt management companies that portray themselves as free independent advice agencies), payday loan contracts, debt collection practices of various companies and so on. Any change to the regulator needs to be carefully considered to ensure that such a move is not premature. There is a danger that the benefits of the CCA 2006

[3] **http://www.oft.gov.uk/OFTwork/credit/enforcement-action/#named1**

changes to the powers and capability of the OFT to take action will be lost.
We would highlight the powers that the OFT has available under Section 11 of the Enterprise Act 2002 to refer a market to the Competition Commission. There does not appear to be an equivalent power under FSMA and would suggest this needs addressing. As Citizens Advice say in their response to the BIS Financial Services Regulation consultation paper[4]:

"Citizens Advice believes that the current consumer protection objective in section 5 of FSMA needs to be updated to reflect the role of the CPMA as a strong consumer champion. The duty is vague in its purpose and, in requiring protection to be 'appropriate', indeterminate in its force. It also fails to clearly set out the wider public interest objectives that we would expect of a consumer champion."

We note that the Treasury is also consulting on "A new approach to financial regulation: building a stronger system"[5] One of the options in this consultation is for the FCA's Consumer Panel to have the ability to trigger the super-complaint process. However, it is not clear from the Treasury consultation whether these super-complaints would be as wide as those under s11 i.e. covering any features of a market that appear to be significantly harming the interests of consumers and therefore either competition and/or consumer protection problems. We would strongly support any new powers to cover consumer protection issues where these do not arise from a restriction of competition.

Overall, we accept that the concerns raised in the paper regarding the difficulties of developing coherent policy responses to emerging consumer protection issues over two separate regimes. This is coupled to the lack of accountability by one body for the performance of retail financial services. We accept the current regulatory framework is confusing for consumers and industry but would applaud the way in which regulators have worked round this by way of memorandums of understanding, joint working, and so on.

We have outlined our concerns at the proposed approach throughout our response to this paper.

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[4] **http://www.citizensadvice.org.uk/index/campaigns/policy_campaign_publications/consultation_responses/cr_consumeranddebt/her_majestys_treasury_financial_services_regulation**

[5] **http://www.hm-treasury.gov.uk/d/consult_newfinancial_regulation170211.pdf**

Question 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;

Irresponsible lending and borrowing

We would support intervention to protect consumers from the consequences of unaffordable borrowing. Money advisers frequently report speaking to clients who are in a downward spiral of multiple personal debts and using one credit card to pay off another etc. There is increasing evidence of consumers using credit cards to pay priority debts such as their mortgage[6] Many consumers are temporarily insulated from falling into mortgage arrears by record low interest rates, but this does not apply to those with subprime and / or high interest second charges. It is very hard for consumers in financial hardship to make appropriate choices and there must be adequate protection against the sale of inappropriate products. Over the years the free-to-client advice sector has seen many instances of inappropriate consolidation loans taken out to consolidate unsecured debts, or mortgages taken out with no repayment vehicle in place.

High cost credit

We have had a longstanding concern over the detriment to consumers caused by the interest rates associated with loans offered via bills of sale, payday lending and in some instances, home-collected credit particularly where loans are rolled over. We are concerned that some products which fall into this high-interest category appear on the face of it to be unfair to the consumer. There is clearly a need for some further work to ensure that vulnerable consumers are treated fairly in how they access credit products.

We would urge that the levels of interest that can be charged by banks in relation to authorised and unauthorised overdrafts are not overlooked. Such credit facilities are not always regarded as falling within common definitions of high-cost credit products. Nonetheless, they can create a heavy burden for consumers who have fallen into debt, albeit this is a product valued by many consumers.

Payday loans

There should be a strategic review of the use of payday loans to establish whether these products are operating to the detriment of consumers. Such a review should pay particular attention to the practice of 'rolling up' loans, and adding further interest and charges. We question whether payday loans should be allowed to continue to exist in their present form.

[6] **http://england.shelter.org.uk/news/january_2011/2m_pay_for_home_on_cards**

Debt collection

We have continuing concerns that debt collection agencies and debt purchase companies are failing to abide by the OFT Debt Collection Guidance, and welcome the OFT's actions against individual companies. We understand that the OFT has imminent plans to revise the guidance which, in our opinion, needs to be strengthened to deal with abuses and to deter non-compliance. The review of the OFT Debt Collection Guidance should highlight the continuing problem of lenders failing to pass on full information about the debt, including information about third parties dealing with the account, financial statements, and details of existing payment arrangements.

There are also further unresolved issues regarding harassment of vulnerable people in debt, use of official-looking letters, and inappropriate collection action such as issuing statutory demands, pursuit of statute-barred debt particularly by debt sale companies, extensive issues with mis-tracing, bad management of disputed debts, and so on.

The fee-charging debt management sector

There is a substantial risk faced by consumers in relation to fee-charging debt management companies. This has been clearly demonstrated by the work of the OFT in their Debt Management Compliance Review[7] As a result of the review, there has been further licensing action in January 2011[8] In the absence of a statutory debt management plan as envisaged under the Tribunals Courts and Enforcement Act 2007 much more needs to be done to protect vulnerable consumers in debt from such firms.

"…As part of the review the OFT found that:

- *there is widespread non-compliance with the Guidance by debt advice and debt management licensees, with most debt management firms audited failing to some extent in at least three areas;*
- *misleading advertising is the most significant area of non-compliance, in particular misrepresenting debt management services as being free when they are not;*
- *frontline advisers working for debt management companies generally lack sufficient competence and are providing consumers with poor advice based on inadequate information."*

[7] **http://www.oft.gov.uk/shared_oft/business_leaflets/credit_licences/OFT1274.pdf**
[8] **http://www.oft.gov.uk/news-and-updates/press/2011/10-11**

Insolvency Practitioners

There are a variety of what are loosely termed insolvency advice activities that are licensed either through the Insolvency Service as insolvency practitioners or escape licensing at present. This includes companies giving advice about insolvency options or arranging for related insolvency applications. These need to be regulated either through the OFT licensing scheme or through an FSMA style scheme. The regulation of the insolvency practitioner market to-date, has not dealt sufficiently with instances of bad practice as there is an over-reliance on self-regulation in what constitutes a high-risk market.

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

We see the consumer protection work undertaken by the OFT as a crucial key provision in the current regime. We have noted elsewhere in our response that the CCA 2006 provisions have enabled the OFT to take increasingly effective enforcement action against licence holders. The new protections have taken time to bed in, but are now showing increasing effectiveness. We feel that the OFT is hampered by a lack of resources to enable them to take comprehensive enforcement action across sectors. However, where the OFT has been able to take action, they have been effective. There needs to be a balance between proactive and reactive enforcement.

The OFT describes their regulatory principles as follows:

"The Consumer Protection from Unfair Trading Regulations (CPRs) and the Consumer Credit Act 2006 have made significant changes to the body of UK consumer protection law. Together with the Unfair Terms in Consumer Contracts Regulations 1999 and the Enterprise Act 2002, they mark a fundamental move away from prescriptive regulation towards a principle-based consumer protection regime which encourages targeted, risk-based enforcement geared to the efficient operation of the market. At the same time, they also increase the range of enforcement tools available to enforcers, strengthening investigative powers and enabling OFT to take criminal proceedings and to seek financial penalties, alongside existing civil enforcement and compliance tools."[9]

[9] **http://www.oft.gov.uk/about-the-oft/legal-powers/enforcement_regulation/enforcement**

The OFT and Competition Commission powers under section 11 of the Enterprise Act 2002 are substantial and the OFT refers to it as its “main tool to ensure compliance with the law”. Section 11 allows a designated consumer body to complain to the OFT that a feature or combination of features of a market for goods or services is, or appears to be, significantly harming the interests of consumers. This gives the regulator a statutory period of 90 days to publish a response stating what action it will take. There is no equivalent provision under FSMA rules to allow the FSA or CPMA to take such swift and timely consumer protection action. As a result we question whether the preferred option (A) would allow for timely responses to emerging consumer protection issues as set out in the introduction to this consultation.

We have outlined what we consider to be the key provisions of the CCA in providing consumer protection in our response to question 7.

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

We are unable to comment widely on the incidence of regulatory duplications or inconsistent regulation as it affects firms.

It is generally difficult and confusing to work out what will be covered under FSA Banking Conduct of Business Sourcebook (BCOBS) and what is covered by the Lending Standards Board. It has certainly been challenging to deal with particular issues such as the guidance on the right of set off with both the Lending Standards Board in relation to current accounts in overdraft, and the FSA in relation to current accounts in credit. We have had similar problems identifying whether the matter of accessing basic bank accounts when an undischarged bankrupt is covered by BCOBS and the BCOBS Industry Guidance or the Lending Code. There is a danger that such issues get lost between the different regulatory bodies and industry guidance.

In the MAT response to the review of BCOBS Industry guidance[10] we questioned how transparent the interaction is between the FSA BCOBS principles and the industry guidance which is not intended for the public. We understand the FSA “will take [the guidance] into account when exercising its regulatory functions.”

[10] **http://www.moneyadvicetrust.org/images/Money%20Advice%20Trust%20response%20to%20the%20review%20of%20industry%20guidance%20under%20FSA%20BCOBS%20regulation%20consumer%20consultation.pdf**

We went on to say as follows:

"There is a risk that the rules and regulations become so obscure as to undermine the protection available for the consumer. This point could also be made in relation to the Lending Code which is not even recognised by the FSA in relation to its regulatory functions."

With regards to inconsistent regulation there are two main examples that are relevant in relation to claims management companies and cold calling in relation to the mis-selling of Individual Voluntary Arrangements (IVAs). We have outlined our concerns below.

We have concerns over the current regulation of claims management companies. The provisions of Part 2 of the Compensation Act 2006 do not seem to have 'bitten' and the OFT and Ministry of Justice and other stakeholders are well aware of some breathtaking examples of bad practice. These include misleading advertisements, taking money from the public on the basis of totally unsubstantiated claims, cold calling, mis-advising consumers to suspend payments to creditors and so on.

We note that the Insolvency Service has taken action[11] following concerns about the activities of companies that cold-call consumers and suggest that their IVA has been mis-sold or is faulty in some way. Often, such companies suggest that the consumer should break the IVA by stopping payments, and then charge a fee to "help" them go bankrupt instead. We also note that the OFT has issued requirements against companies who suggest bankruptcy annulment through refinancing.[12] However, whilst we are very pleased that action has been taken, it has taken some time since complaints about such companies first arose, as it was unclear in some circumstances which regulator would be responsible for taking action. This is an example of where a coordinated approach by the OFT and Insolvency Service is necessary to combat these problems and provide redress for consumers.

[11] **http://nds.coi.gov.uk/clientmicrosite/Content/Detail.aspx?ClientId=95&NewsAreaId=2&ReleaseID=417023&SubjectId=36**

[12] **http://www.oft.gov.uk/news-and-updates/press/2010/130-10**

The free-to-client money advice sector is dealing with an increasing number of enquiries from consumers in relation to cold calling where fee-charging companies offer a debt management service. There are instances where such companies give the impression that they are free advice agencies such as National Debtline. Again this seems to be an area where regulatory powers overlap between the OFT and partner regulatory bodies which can cause delay where new issues arise in the market and regulators need to coordinate to decide how to investigate and take action. We are very pleased to note that the OFT recently took action against a lead generation firm to deal with illegal cold-calling practices.[13]

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

We would agree that the objectives are mainly laudable, but the detail needs to be right in order to ensure effective consumer protection against unfair practices.

We are concerned that the FSA regime would be a high-level principles-based framework (in contrast to the rules-based approach under the CCA), underpinned by non-mandatory guidance, which would not capture the necessary level of detail or exert the necessary degree of force to be effective.

We believe that the reforms should provide effective mechanisms for the regulator to identify new sources of consumer detriment at an early stage and to take swift action to tackle them. It is vital that there is a proactive and flexible process to enable any new regime to deliver on its consumer protection objectives of consumer protection.

We are concerned that any new regime should not take precipitate action in removing and simplifying regulation without a high degree of research and evidence that the regulations in question are not providing benefits to consumers. The key emphasis should be on retaining and ensuring consumer protections and not easing regulatory burdens on firms. In our experience, there are many firms at the margins who take any opportunity to create a business model out of gaps in consumer protection such as sale and rent back schemes and the current dubious activities by claims management companies. We are concerned that this is likely to happen again unless extreme care is taken.

[13] **http://www.oft.gov.uk/news-and-updates/press/2010/113-10**

Question 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.

It would appear that a unified regulatory regime for retail financial services could have a positive impact. We would expect it to be beneficial in terms of clarity for the potential confusion for consumers in relation to regulation of bank accounts to be removed. However, we wonder if the confusion would be mitigated by having a single regulator rather than abolishing the CCA. Much consumer protection is underpinned by different legislation and regulation without this confusing the consumer on a practical level.

A unified regulatory regime would bring greater coherence. However, this should not be overemphasised as it is pointed out in section 2.7, financial services will remain subject to the Consumer Credit Directive and other general consumer legislation.

Improved market oversight will depend upon the resources and enforcement powers given to the CPMA and the relative importance the CPMA gives to taking robust action in relation to the trends and issues identified.

Question 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.

We strongly support maintaining the crucial roles of institutions involved in the regulation of consumer credit, including local Trading Standards Services, and the National Fraud Authority. We would urge Government to continue such arrangements under the CPMA. The current FSA model which allows for functions to be performed on its behalf by bodies deemed competent to do so would appear to be a model worthy of replication.

The free-to-client debt advice sector works closely with local trading standards services, the specialist Illegal Money Lending Teams, Scambusters and so on. We consider their work to be vital in tackling consumer detriment against the most vulnerable and marginalized consumers. The new regulator will be regulating many more small firms than the FSA currently regulates – therefore it will be vital for the CPMA to develop links with individual trading standards services, specialist teams and national trading standards bodies (e.g. Trading Standards Institute).

We do question whether there is sufficient protection afforded to consumers under the current claims management authorisation process.[14] There has been much concern in recent years in relation to the activities of authorised claims management companies in the financial services field. It is particularly important to consider and evaluate whether MOJ have sufficiently robust enforcement powers to monitor firms. We would suggest consideration of incorporating this area within the scope of CPMA activities.

Question 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.

As the paper recognises:

"The current CCA regime provides for a number of important consumer protections that are valued by many stakeholders."

We agree that it is vital that the CPMA builds upon the FSA's consumer protection strategy, to become proactive in identifying and tackling consumer detriment. However, this is no substitute for the rights and provisions available to individual consumers as a result of the protection afforded by the CCA 1974. The CCA has vital inbuilt rights that must not be diluted by a FSMA style rule book. As the paper states:

"It is unlikely that there would be a direct replication of the existing formulation of all CCA consumer protections in the rule book."

We have reservations as to whether any meaningful, effective consumer protection would be in place if consumer credit were to be regulated in the way in which retail banking services are regulated by the FSA i.e. high-level principles in rules which are not transparent to consumers, plus the provisions of the Consumer Credit Directive that come into force in February 2011.

We have found the detailed guidance produced by the OFT on the meaning and application of the "fitness test" under s25 of the CCA 1974 to different credit businesses and practices very helpful in identifying and challenging bad practice by firms.

[14] **https://www.claimsregulation.gov.uk/index.aspx**

Unenforceability of agreements by unlicensed traders

It is vital to deal with the important protections provided by Section 40 of the CCA 1974 which makes agreements entered into by unlicensed traders unenforceable. There is no equivalent to this overriding protection under FSMA rules. This needs to be retained.

Another potential dilution of consumer protection that might arise under a FSMA style regime is that at present, non-compliance with the detailed rules on documenting the credit agreement and on providing information subsequently, renders the agreements unenforceable (except on an order of the court) whereas there is nothing equivalent in FSMA 2000. On the contrary; agreements are explicitly not affected by rule breaches: FSMA, S151 (2) although the Act does give a right of action for loss under s.150.

Prescribed terms in consumer credit agreements

We cannot support a rule book that would allow any variations in style, wording and presentation of credit agreements. This would lead to consumer confusion, make the task of enforcement of compliance harder and make it extremely difficult to take action against lenders for any breach or for consumers to challenge their agreements. There need to be prescribed terms and conditions for all agreements. There are provisions under the Consumer Credit Directive governing the terms of agreements which would have to be retained but we are concerned that these do not go far enough. The CCA includes detailed provisions for the form and content of credit agreements and how copies of documents must be provided. These need to be retained along with sanctions for non-compliance.

Time orders

The right to apply for a time order under section129-136 of the CCA 1974 is a vital tool used by money advisers when assisting a consumer with debts. This allows the court to reschedule the payments under a regulated agreement when a borrower is in financial difficulties. This can result in a reduction in the payments, interest and charges and prevent further enforcement action by lenders. Such provisions are particularly helpful in second charge lending cases, hire purchase and where payments and interest rates on unsecured credit are excessive.

We understand that regulation of second charges will be transferred to FSMA and removed from CCA protection. We are extremely concerned that the vital protections of time orders and unfair relationship provisions for second charge borrowers under the CCA are not lost. FSMA rules need to be amended to incorporate both time order provisions and unfair relationships provisions. We have further argued that if time order type provisions were available under MCOB for first charge mortgages, that many of the provisions such as the Homeowner Mortgage Support Scheme would have been unnecessary.

We have long argued for improvements in the law relating to time orders. In our view, the process of applying for time orders is expensive, time consuming and obscure, and do not apply to most borrowers. The amendments introduced in October 2008 under the Consumer Credit Act 2006 (CCA 06) will make little difference in practice.

Unless the issues that have arisen relating to the definition of "temporary" financial difficulties are resolved, a time order remains an unreliable remedy for those in debts outstanding on CCA-regulated loans.

However, despite our reservations, we are strongly supportive of a revised and more flexible equivalent to the time order provisions. There needs to be a mechanism in place to allow consumers to reschedule payments under an agreement when a borrower has financial difficulties in relation to not just the monthly payments, but the terms and conditions, and consequent interest rate and charges.

The 'unfair credit relationships' test

There is no equivalent in FSMA of the unfair credit relationships test which was introduced by the 2006 Act under section 140A of the CCA 1974. This provides the court with wider powers to release security, rewrite agreements and liabilities. In contrast, consumers only have a right of private action for damages for similar practices under FSMA.

Whilst we believe that actions to challenge unfair credit relationships could be made more accessible to consumers, we remain strongly in support of this part of the Consumer Credit Act.

Voluntary termination

We believe that the provisions within ss99 and 100 are essential to protect the rights of consumers who have entered into hire purchase and conditional sale agreements and who are no longer able to afford the payments. We suggested in the MAT coordinated response to the "BIS consumer credit and insolvency call for evidence"[15] that there is a need to issue guidance regarding these provisions in order to make it crystal clear that consumers retain an automatic right to voluntarily terminate their agreement until the point when the agreement has been terminated by the lender. We believe that this protection should remain if regulation of consumer credit is to pass to the CPMA.

15 http://www.moneyadvicetrust.org/images/MAT%20coordinated%20response%20to%20the%20BIS%20consumer%20credit%20and%20insolvency%20call%20for%20evidence.pdf

Second mortgages/secured loans

We note the announcement by HM Treasury[16] that the Government intends to transfer the regulation of new and existing second charge residential mortgages from the Office of Fair Trading (OFT) to the Financial Services Authority (FSA). We would welcome the announcement that there is to be put in place a single regulatory framework for all secured lending. However, it is unclear what will happen to key elements of the CCA protection such as unfair credit relationships and revised time order provisions. This could extend court powers to allow interest and default charges to be frozen and for consumers to stay in their homes whilst paying less than the contractual amount if necessary. The right of complaint to the Financial Ombudsman Service should be retained and the FSA regulatory powers should also be incorporated along with the OFT Irresponsible Lending Guidance and the OFT Second Charge Lending Guidance. We would urge Government to adopt these elements into the new regulatory regime.

Post-contractual obligations

The CCA 2006 introduced important rights in relation to annual statements, arrears and default notices. This includes the statutory requirement to send information sheets to consumers who may be falling into debt. From the advice sector perspective, such a requirement with prescribed wording is vital to preserve to ensure that all lenders abide by the regulations and provide information in a common, plain English format and include the prescribed list of free-to-client advice providers. It is also vital to preserve the sanctions of temporary unenforceability of the agreement against non-compliance by lenders. This concept is unknown under FSMA and could be lost in the regulatory transfer.

Linked credit agreements

The provisions under section 75 and 75A of the CCA provide extremely important protection for consumers in relation to the joint and several liability of card companies for breach of contract by a retailer and other claims against suppliers. These provisions should be retained.

Question 8 The Government would welcome further evidence relating to:

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

Business Debtline provides advice and assistance to small businesses. These may be sole traders, small partnerships or small limited companies. Typically, a small limited company will consist of a managing director and a company secretary or 2 managing directors in total.

[16] http://www.hm-treasury.gov.uk/fin_sector_mortgages_enhancing_consumer_protection.htm

In the experience of Business Debtline, the use of consumer credit by SMEs is common in the form of hire purchase, lease agreements and both fixed sum and running-account credit.

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

At present the protections afforded by the CCA do not even extend to small limited companies. Consequently, these types of SMEs are bound by the specific terms and conditions of their contractual agreement. In the experience of Business Debtline, collections and recovery processes for these types of SMEs are more aggressive. Often small limited companies can find it difficult to get information about their contract and creditors can often withdraw or reduce funding without sufficient notice which can result in immediate closure of the business. This is particularly unfortunate where greater forbearance could result in trading out of the difficulties and saving the business.

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

Costs: loans to small limited companies will not benefit from these provisions and they will still remain outside the scope. Although the rules would extend to a wider group of SMEs in relation to the level of debt that would be covered, the protection for small limited companies would not be there.

Benefits: In the opinion of Business Debtline, the majority of SMEs do take credit that is higher than the current £25,000 limit under the CCA. Therefore, extending the rules to a wider group would afford them more protection and could in the long run save businesses.

Question 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.

We believe that a rule-based regime could provide a regulatory regime which is inherently more flexible and responsive than a regime set out in legislation. We appreciate that primary legislation is difficult to amend in the light of market developments and that it is more difficult to respond swiftly to emerging practices. For example, if the OFT had had rule making powers, it could have quickly tackled the bad practices by firms providing credit by bills of sale.

However, our main concern with rules-based regulatory regimes is that they can be high level. For example, the rule book will often use terms such as "reasonable" "treating customers fairly" and "dealing fairly". These are clearly open to interpretation by individual companies, consumers and their representatives.

In comparison, the OFT can impose requirements on individual firms to tackle their specific bad practices – a power that the FSA does not have. However, these requirements do not have the same positive force on the whole industry as rules.

We therefore suggest that the Government look at giving the CPMA new rule-making powers which are linked to the requirement regime.

The other problem with a rules making regime is that it is likely to be ineffective in markets which are very diverse. The FSA struggled to tackle the irresponsible lending and harsh arrears practices exhibited by sub-prime lenders as MCOB assumed all lenders would be the same, and the rules regime made the FSA blind to problems arising in different segments of the mortgage market. Consumer credit is a very diverse market, with many different types of products, including payday loans, bills of sale, hire purchase and buy as you view, and not just credit cards and personal loans. The CPMA will need to undertake swift and surgical micro-interventions to tackle consumer detriment.

Question 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 believe that the FSA's supervisory regime could ensure effective and appropriate consumer protection. The FSA should avoid intervening only when there is overwhelming evidence of consumer detriment as can happen under current regulatory regimes. However, it is vital the CPMA draws on the experience and expertise of current regulators such as OFT staff when they take over regulation of consumer credit. The OFT know which companies are causing detriment.

We understand that the new CPMA model will be given new tools and powers. It is also the intention for it to be keener to intervene and to intervene earlier than under the FSA regulatory regime. Without firm details of the proposed new powers, it is difficult to comment on the impact this will have on ensuring effective and appropriate consumer protection.

We have major concerns that a high level rules-based approach will be insufficient in preventing detriment to consumers. We have found that attempting to interpret broad-brush rules such as the concept of "treating customers fairly" is difficult to do. Where firms are able to put their own interpretation on concepts such as "reasonableness" it is more difficult for consumers and their advisers to challenge an individual company.

As an example, under the MCOB rules 13.3[17] it is required that mortgage lenders:

*"Allow a reasonable time over which the payment shortfall or **sale shortfall** should be repaid, having particular regard to the need to establish, where feasible, a payment plan which is practical in terms of the circumstances of the **customer**."*

A "reasonable time" has been interpreted very differently over the years by both lenders and ultimately the courts. Advisers find that lenders typically suggest a very short repayment period of 1 to 2 years as being a reasonable time period[18] The Administration of Justice Act 1970[19] sets out the court's powers in relation to possession for mortgage arrears, and it states that it can only exercise its powers to delay possession if the borrower can demonstrate that they can pay their contractual mortgage instalment (CMI) and clear the arrears 'within a reasonable period.' Case law suggests the period could be as long as the remaining term of the loan.[20]

As a result, we would suggest that MCOB 13.3 is not sufficiently prescriptive and is too open to interpretation.

This example illustrates why we would therefore generally favour a greater level of prescription with rules that are less open to individual lender interpretation.

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17 **http://fsahandbook.info/FSA/html/handbook/MCOB/13/3**

18

http://www.citizensadvice.org.uk/index/campaigns/policy_campaign_publications/evidence_reports/er_consumerandebt/turning_the_tide_
http://www.citizensadvice.org.uk/index/campaigns/policy_campaign_publications/evidence_reports/er_consumerandebt/set_up_to_fail-2

19 Section 36, as amended by section 8 of the Administration of Justice Act 1973
20 (*Cheltenham & Gloucester BS v Norgan* (1995) 1 All ER 449)

Question 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 agree that the current regime where the OFT has responsibility for both consumer credit and general consumer protection, means that there is a coherent view of all aspects of a business providing the sale of goods and services on credit. It is vital that these protections are preserved. As it is possible that the OFT will be abolished at around the same time, it is vital that the FCA can enforce breaches of the CPRs and Unfair Contract Terms legislation. This will mean close working with Trading Standards Services.

As the paper points out under paragraph 2.10, the aim is that the FCA:

"..will continue to have concurrent consumer protection powers where another body is the lead enforcer of a general piece of consumer protection legislation."

We suggest that the relationship with the OFT continues with regards consumer protection. The CCA licensing fitness test has only recently bedded in following the Consumer Credit Act 2006 changes. The benefits of the new process are now beginning to be realised as the OFT has stepped up its enforcement work in relation to fitness requirements in the latter part of 2010. This work should not be lost in a transfer to the FCA.

Question 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)?

We can appreciate that the transfer of consumer credit regulation to a FSMA-style regime would appear to support the Government's objectives in some areas.

Whilst simplification and deregulation are important principles, our major consideration is consumer protection rather than removing the regulatory burden on firms.

However, our main concern relates to the objective of achieving "effective and appropriate consumer protection." A FSMA style regime will not be able to maintain or strengthen protection for consumers unless a wide range of the consumer protection provisions that exist under the CCA are maintained or enhanced. We have given examples of our concerns in response to question 7.

We are also concerned that the powers under the Enterprise Act 2002 will also be lost in relation to consumer credit. We have outlined our concerns in response to question 3. As we have said, there is no equivalent provision to section 11 of the Enterprise Act 2002 under FSMA rules to allow the FSA or CPMA to take such swift and effective consumer protection action.

Question 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?

We have outlined our main concerns throughout the response to this paper.

We feel that the right to order redress for individual consumers is an extremely important power held by the FSA which could be available to all consumers with financial services problems.

However, we note the work of the OFT in developing a civil sanctions pilot which will run from April 2011. This will allow;

"the provision of voluntary restoration to consumers who suffer detriment as a result of unsafe products or unfair or misleading business practices".[21]

There will be criminal sanctions for non-compliance.

As we identified in our response to question 7, there are a number of crucial elements of the CCA 1974 that would need to be replicated within a FSMA rules based regime. Without these vital protections for consumers we would find it difficult to support the transfer.

Question 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 have concerns over the costs that will be incurred for the free-to-client debt advice sector. There is an enormous body of both online and paper based training materials and training courses that would need to be redeveloped by organisations such as Money Advice Trust under Wiseradviser,[22] Citizens Advice for their training and information systems, the Institute of Money Advisers training programme[23] and so on.

[21] **http://www.oft.gov.uk/shared_oft/consultations/OFT1296.pdf**
http://www.oft.gov.uk/news-and-updates/press/2010/147-10
[22] **http://www.moneyadvicetrust.org/content.asp?ssid=3**
[23] **http://www.i-m-a.org.uk/training.html**

There are then the related expenses of implementing the training across the free-to-client money advice sector. Specialists would need to develop their own expertise whilst discarding a wealth of knowledge of consumer credit law and case law to rewrite and republish handbooks and information systems with the related costs of doing so and with limited resources.

We are interested to find out what the legal status would be of the vast existing body of caselaw relating to the CCA if the changes were to be implemented.

We have worked closely with the OFT in the development and review a range of statutory guidance which represent invaluable tools in providing practical support when assisting debt advice clients and dealing with lenders and creditors who must have regard to the guidance. These include the following in particular:

- *The OFT Debt Management Guidance (currently under review)*
- *The OFT Debt Collection Guidance currently under review)*
- *The OFT Irresponsible Lending Guidance*
- *The OFT Second Charge Lending Guidance*
- *The OFT Mental Capacity Guidance (subject to consultation)*[24]
- *The OFT Consumer Guidance on Section 77-79 CCA*

We do not see FSMA style rules as an adequate substitute for the detailed guidance provided by the OFT. If the Government decides to go ahead with option 1 we would seek to see the equivalent of the OFT guidance incorporated into any new rule book.

We also greatly value the approach the OFT has taken to working with consumer groups, including the free-to-client money advice sector. The OFT has taken a very interactive and consultative approach which we feel has been very productive. We believe that this approach should be replicated in any new regime.

[24] **http://www.oft.gov.uk/about-the-oft/legal-powers/legal/cca/mental-capacity-guidance/**

Question 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?

We recognise that the CCA 1974 has developed in range and complexity over the years. We also recognise that there would be advantages in a regime that would enable speedier amendment than through the current legislative route. However, we are not convinced that a move to a FSMA rule based regime and the repealing of the CCA would be a proportionate response on grounds of complexity, cost and related transitional confusion for both lenders and consumers. We would seek substantial reassurances that the protections afforded by the CCA would not be lost. There appears to be little guarantee that key protections would be preserved. As an example we would reiterate the points we made in relation to the HM Treasury Mortgage Market Review paper on second mortgage regulation.[25]

"Whilst we welcome the proposal that the same regulatory regime should apply to all mortgages and secured loans, we do not agree that a simple migration of responsibility from the OFT to the FSA would be enough to achieve the Government's objective. Instead, we would like to see an equalisation of the two markets, based on taking the best consumer protection measures from both the Consumer Credit Act (CCA) regime and that of the Financial Services and Markets Act (FSMA). We suggest that a market that is 'fair, stable and efficient' is a market with consistent and meaningful consumer protection. Such protection must cover pre and post-contractual matters including selling, lending, arrears management and individual consumer redress when things go wrong. We are concerned that it would be a missed opportunity if there was an extension of the scope of FSA mortgage regulation to include second-charges, without incorporating such provision."

We do not have any developed views as yet on the factors the Government should take into account in determining the most appropriate regulatory authority. We are mainly concerned that the OFT's powers, expertise and experience and their body of guidance work are not lost.

25 **http://www.moneyadvicetrust.org/images/MAT%20coordinated%20response%20HM%20Treasury%20consultation%20mortgage%20regulation%20FINAL.pdf**

Question 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.

Overall, we believe that the provisions of a FSMA-style regime could lead to a tougher regulatory regime for consumer credit businesses:

The authorisation and threshold conditions will be considerably tougher under the FSMA regime, compared to the current OFT regime. However, we would caution the CPMA to be wary of exempting small firms from these – in our experience small credit firms come up with new products, often aimed at marginalized groups of people, which cause a great deal of consumer detriment. It would be completely inappropriate to exempt small firms from these procedures.

Fee arrangements – this could be based on a percentage of turnover of the firm. We believe that the CCA regime has not charged large multi-national firms enough in fees.

Systems and control requirements – we believe that the FSA has a better handle on these

Conduct of Business rules – as we have argued strongly throughout this response, these will need to be effective, detailed and preserve current consumer rights, if they are to be effective in preventing detriment.

Prudential requirements – we believe that these could be vital even for small consumer credit businesses to ensure that they lend responsibly.

Reporting requirements – there are no reporting requirements currently in the CCA regime. These could be onerous for small firms, so the CPMA could consider exempting small firms from some of these requirements. However, we would warn against exempting small firms from all the requirements – as small firms often cause considerable consumer detriment.

Enforcement provisions – with the exception of the requirements regime, the FSA have much better enforcement powers compared to the OFT. They can impose unlimited fines (OFT can only charge £50,000 maximum) and can order firms to compensate affected consumers.

The free-to-client debt advice sector are mainly covered by the OFT group licensing scheme. This provides “light-touch” regulation but requires compliance with the relevant provisions of the OFT Debt Management Guidance (where it relates to the free debt advice sector). We would suggest an equivalent to the Guidance would need to be in place to cover the activities of both free debt advice services and the fee-charging debt management company sector.

As evidenced by the OFT Debt Management Guidance Review, the fee-charging debt management company sector is categorised as a high risk area and should continue to be treated as such.

Question 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?

With regard to the risk-based approach this appears to match the approach taken by the OFT who have identified the following credit activities as being high risk licence categories.[26]

D - debt adjusting
E - debt counselling
F - debt collection
H1 - credit information services (including credit repair)

These categories of business are then subject to a higher level of scrutiny and be required to demonstrate credit competence. With the OFT's enhanced powers following the Consumer Credit Act 2006, we are beginning to see the results of this approach. The OFT are starting to take increasing numbers of actions by way or requirements and revocations against companies who contravene the licensing principles. It is vital that the increasing effectiveness of this work is not lost going forward.

However, for groups that have been identified as lower risk, the intention outlined in section 3.17 of the paper to rely upon "regulatory returns and complaints-led intelligence" leads us to reiterate concerns we have previously expressed in responses to previous consultation papers that poor practice may continue to fall through the gaps in regulation. In the MAT response to the BERR Consumer White Paper[27] we said:

"We applaud the current work of the OFT and other licensing bodies and regulators in tackling bad practice, but often this work is not timely enough, nor does is appear that the relevant organisations possess sufficient power to regulate as effectively as we might hope. A significant proportion of investigations rely upon individual consumers being prepared to make formal complaints to regulators that

[26] **http://www.oft.gov.uk/OFTwork/credit-licensing/credit-licence/riskcategories**
[27] **http://www.moneyadvicetrust.org/images/MAT_response_to_BERR_Consumer_White_Paper_Issues_Paper_May_2009_%20FINAL.pdf**

will help to build up a body of evidence. There is little incentive for the consumer to cooperate as for example the OFT is specifically prevented from dealing with individual complaints on a case-by-case basis, and is also unable to let the consumer know the outcome of their investigations in any formal way."

(This is due to restrictions under Part 9 of the Enterprise Act 2002 which prevents the OFT from identifying businesses that are subject to requirements or warnings or under investigation.)

We are therefore not confident that without reform of the problems with complaint mechanisms under CPMA, that a risk-based approach can rely upon the ability of consumers to make complaints with no possibility of redress or recognition. Also, it is self-evident that in order to complain, the consumer must be able to identify the issue as causing them detriment. In many cases, this will not happen as the consumer is unaware they have been sold a toxic product.

We welcome the concept of proportionality in relation to fees and the recognition that exceptions to the general approach are permitted such as for credit unions. We would argue that those eligible currently for the group consumer credit licence for free-to-client debt counselling advice agencies should continue to be licensed free of charge.

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

We would suggest that it would be vital to take into account the OFT review of consumer credit licensing fees.[28] Fees should be allocated fairly between different types of licensed firms. It is clearly not proportionate that a small limited company would pay the same fee as a large bank. Any revised system should be able accurately to reflect the different costs of regulating different types of business under the regime.

"The CAB disagreed with the simplistic approach suggested within the consultation paper. They responded that the OFT should devise a system for charging fees that weighs the level of risk presented by an application against the size of the business, into a matrix. The CAB also requested that OFT should consider whether the use of an on-line fees calculator, such as that used by FSA, would negate the drawbacks of a more complex system which were highlighted in the consultation paper."[29]

[28] **http://www.oft.gov.uk/OFTwork/consultations/closed/2010/cclf**

[29] 2.42 **http://www.oft.gov.uk/OFTwork/consultations/closed/2010/cclf**

In setting fee levels the FSA or CPMA would need to take into account the appropriate level of fee relating to the regulatory scrutiny required by different types of consumer credit activity. We would urge any fee setting to fully take into account the OFT's experience of dealing with the increased risk associated with certain types of licence activity such as fee-charging debt management companies and so on.

Question 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.

We do not have any relevant evidence to provide relating to the current appointed representatives regime.

Question 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.

As free-to-client money advice providers who are part of the current group licensing regime, we would suggest that the current scheme has worked very well. We believe that it is important for our sector to be regulated.

We believe that the FSMA professional body regime could be adapted to meet the needs of the group licensing regime for charitable free-to-client debt advice providers.

However, we question whether the evidence relating to the fee-charging debt management companies' trade associations ability to self-regulate would justify extending this regime to either debt management companies or insolvency practitioners. (See our answer to question 21). Alternatively the Government could consider using the provisions in the Financial Promotions Order to devise carve-outs for charitable free-to-client debt advice providers.

Question 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 value the extremely important work of the Lending Standards Board in developing and monitoring the Lending Code as a voluntary code of good practice. This is an example of self-regulation working relatively well. However, this is due to the major trade bodies co-sponsoring the code and a commitment by major lenders to subscribe to the provisions of the Lending Code. Subscription remains on a voluntary basis and there can be difficulties in ensuring all subscribers comply with the Code. . The Code is subject to an external independent review but subscribers cannot be forced to accept any proposed revisions. This reduces the effectiveness of the Code as it can be affected by subscribers' own interests.

Other trade bodies have much less effective self-regulatory codes. Often, the content of voluntary codes can be subject to interpretation. This makes it difficult to take a consistent approach and it can be hard for advisers and consumers to work out what phrases such as "positively and sympathetically" mean in practice. This makes it harder for consumers to call companies to account in relation to a particular code.

However, we have had previous experience where self-regulatory codes are prevented from being effective because membership is voluntary. Where there is no membership requirement then despite good work on developing a code of practice, the trade body will have no ability to force non-member companies to comply. Lack of regulation and enforcement powers against members are also a major concern. We would also question the independence of the role of a trade body in policing its own members. There are also likely to be issues of the body having sufficient resources to carry out an effective monitoring and enforcement strategy that will have the ability to identify and discipline members where necessary.

As an example, within the debt management industry, there are two trade bodies[30] who each cover only a very small number of debt management companies. They have differing codes of practice and membership requirements. Recent merger talks have reportedly foundered.[31] Many companies operate without being members of either trade body.

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[30] DEMSA **www.demsa.co.uk/**
Debt Resolution Forum **www.debtresolutionforum.org.uk/**

[31] **http://www.debtresolutionforum.org.uk/news/**

The recent OFT Debt Management Compliance Review[32] found widespread non-compliance with the OFT Guidance and many instances of bad practice.

The proposals in the paper to formally incorporate the provisions set out in existing voluntary codes may be a way forward. We would advocate regulatory control rather than devolving such powers to self-regulation and guidance. If self-regulation was to continue, compulsory membership would be required at the very least.

Question 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 unable to identify any categories of consumer credit activity that would be suitable for deregulation at present. There is a danger of such deregulation resulting in unintended consequences for consumers and an erosion of the current protections. If there were any such areas identified, we would suggest careful research and analysis of the particular activity would be required to explore the possible consumer detriment that could result. An equally robust substitute scheme would need to be in place to ensure effective protection for those consumers affected.

We would caution against any temptation to water down protections by way of a code of practice or similar. Many trade bodies have codes of practice in place but if there is no requirement for membership of the trade body and where the body does not possess the resources to provide effective and rigorous investigation of their members, this cannot be a substitute for regulation.

We note that the paper makes the suggestion that in some cases control via other parallel regulation or professional standards would be sufficient. The example given relates to whether:

"Charities Commission rules provide adequate safeguards for the clients of free debt advice provided by charitable organisations."

We are not confident that the Charity Commission rules provide sufficient safeguards for clients of free debt advice. Such deregulation would be no substitute for the protection afforded by the OFT group licensing scheme and the requirement to adhere to the provisions of the OFT Debt Management Guidance. Achieving charitable status gives no indication of the professionalism and quality of the service being provided in such a specialist area where clients of such services are likely to be especially vulnerable and subject to extreme detriment if the service is inadequate or negligent.

[32] **http://www.oft.gov.uk/shared_oft/business_leaflets/credit_licences/OFT1274.pdf**

Question 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 are unable to put forward any further suggestions at this stage.

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

It is extremely important that the transitional provisions are clear, straightforward and treat consumers with existing agreements fairly.

From a consumer perspective much depends upon the extent to which existing rights under the CCA have been transferred into the new regime. We cannot see it as fair that from a certain date, contractual rights that existed when the agreement was entered into become invalid and unenforceable by the consumer. If for example, no equivalent to the time order provisions is established under the new rules, then vital existing protections for consumers with current consumer credit agreements would be lost. As the paper states at point 4.14:

"However, if the CCA gives significant additional rights and protections, consideration would need to be given to maintaining them unless a CPMA rule can be put in place for existing agreements that offers at least as much overall protection for the consumer. In addition, transitional arrangements would be needed to address processes underway at the date of repeal of the CCA, including, for instance, prosecutions, other legal actions and periods of right of withdrawal."

Under previous changes in the protection afforded to consumers with existing agreements such as the CCA 2006, existing agreements retained their additional protections (such as those relating to the automatic enforceability of agreements). New provisions only applied to new agreements entered into on or after a certain date. However, we appreciate that some new rights and protections can be granted from a set date to all existing agreements where that right is deemed advantageous and does not diminish existing rights. An example of this again relates to the CCA 2006 where the right to complain to the Financial Ombudsman was granted to consumers with existing credit agreements from a set date (although only for disputes that arose from that date onwards).

This example was in the context of the CCA 2006 being an amending Act and not replacing the entire CCA 1974 and rewriting the rules under a new regulator. However, the time, legal complexity of implementation and the costs to the credit sector, advice sector and Government were substantial.

Question 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 would expect existing consumer credit licence holders to have to demonstrate that they meet the different and enhanced requirements for FCA regulated firms on application. Whilst we appreciate there would need to be a lead in period, it does not appear proportionate to grant automatic authorisation as a regulated firm under the FCA where the firm has not demonstrated it is able to meet the higher requirements. Such an approach could have a detrimental effect on consumer protection.

The Government should therefore consider using the approach the FSA used to take on regulation of sale and rent back firms – a transitional period where the full regulatory regime does not apply, but which allows them time to adapt to the full regime. If they have not met the full requirements of the new regime by the end of the transitional period, they must cease to trade.

Alternatively applications could be staggered, perhaps enabling dual licensing under the CCA and FSMA rules for a set period with a cut-off date.

Question 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 firms could simply pay the difference between the OFT fee regime and the fees required by the new FCA regime. Clearly any transitional fee structure needs to be fair to those subject to the transfer from the current fee structure. There would need to be appropriate notice provided with a lead-in time to ensure this works.

We would urge the retention of an equivalent to the group licensing regime for free-to-client debt advice providers and other bodies within the regime. This should continue to be free of charge to those organisations that come under the scheme as these are not-for profit charitable bodies.

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

Yes. We believe that the Government should not let the planned reform of the regulatory system mean that vital reforms to consumer credit are deferred. We would suggest that a delay until 2014 for any further changes to take place would cause consumer detriment.

Question 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.

This is outside our area of expertise as we have no particular experience of similar previous transitions.

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The Money Shop

Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

22nd March 2011

Dear Sirs

Further to the HM Treasury Consultation, ***"A New Approach to Financial Regulation: Consultation on Reforming the Consumer Credit Regime".*** I am pleased to enclose for your attention a response from The Money Shop.

In the event that you require any additional information please do not hesitate to contact me by e-mail at caroline.walton@dfguk.com or by telephone on either 0115 934 7412 or

Yours faithfully

Mrs Caroline D Walton
Corporate Affairs Director

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The Money Shop

The Money Shop

The Money Shop is regulated by the Office of Fair Trading and has a nationwide network of over 370 stores providing a range of financial products including: cheque cashing, payday loans, pre-paid credit cards, pawn broking of gold and jewellery, foreign exchange and overseas money transfer.

Our typical payday loans are small (£250 on average), short–term of between 10 and 45 days. The payday customer is in employment and has a bank account and using the payday loan to help smooth out an emergency spend before payday.

The Money Shop is a co-founder of the Consumer Finance Association (CFA) and therefore fully supports the views submitted by the CFA to the Treasury in respect of the consultation **'A New Approach to Financial Regulation; Consultation on Reforming the Consumer Credit Regime'.** The CFA submission provides a detailed response to the consultation however in addition to this The Money Shop would also like to make the following observations below in respect of the 4 policy objectives being used by the Government to *consider "whether or not to proceed with the transfer of consumer credit regulation to a FSMA-style regime".*

However we believe that attention should firstly be drawn to the comments made by the Regulatory Policy Committee (as outlined in the Impact Assessment) in December 2010 who *"said that the analysis of potential costs and benefits of the proposal were incomplete...(and) in particular, three main areas of concern were highlighted :-*

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

Therefore it may be helpful to conduct a thorough analysis before a final decision is undertaken by government.

Objective 1 – Delivering Clarity, Coherence and Improved Market Oversight

Whilst the concept of a sole regulatory body is a well intentioned one, as it would provide the CPMA with an overview of the entire financial market, the concept of regulating consumer credit alongside other retail financial services is concerning, as unsecured consumer credit is a discrete market where, unlike other products, it is the lender who takes all of the risk. Given the wide and varied range of products available it is difficult to envisage how a sole regulator would be able to achieve successful consistency when the nature of the products and their customers are so diverse.

Furthermore, the consultation document confirms that 'the use of unsecured credit has grown significantly in the last two decades' and therefore we would be reluctant to see the expanding responsibilities of the regulators being subsumed into a FSMA-style regime which is already supervising other more demanding types of retail financial services. Chapter 4 of the consultation refers to the enormity of the task this regulatory reform poses and states that *"the currently licensed population incorporates 96,000 lenders ...a majority of which are not authorised by the FSA. A transfer would therefore represent a significant increase in the number and range of firms for which the CPMA has responsibility"*. Consequently if the unsecured consumer credit industry continues to grow, its uniqueness warrants a separate regime and it would seem logical to maintain a specific consumer credit regime based on the Consumer Credit Act, 1974 which has already proven to be successful.

The Money Shop understands that there are some overlaps across the financial services spectrum and therefore the creation of a sole regulator would provide greater coherence for those firms which are currently dual registered with both the FSA and OFT, as a single regulator would provide greater administrative convenience. However the document states that 45-75% of OFT licensed firms are not currently regulated by the FSA and the substantial increase in cost of fees could lead to significant market exit and thus cause consumer detriment.

The consultation advises that a single regulator would provide greater clarity and coherence for business and consumers, however we would suggest that the current regime is one that consumers are very familiar with. Customers are aware of OFT and Trading Standards and appear comfortable with the pro-active role they undertake in providing protection for the consumer. Therefore we believe that the relationship between OFT, Trading Standards and other professional organisations is a positive one and should ideally be retained.

Objective 2 – Ensuring Effective and Appropriate Consumer Protection, including through a more responsive and flexible framework

According to the comments made by the Regulatory Policy Committee *"it is very hard to measure the current levels of consumer detriment in relation to consumer credit...prior to consultation"*. Therefore if the current level of consumer detriment has not yet been established, it is difficult to see how this issue can be addressed when currently we do not know if there is indeed an actual 'issue' with consumer detriment.

However it can be argued that the transfer to CPMA could result in significant market exit through a number of factors such as increased costs, and increased reporting requirements which may prove too burdensome for some of the smaller organisations in particular. A significant level of market exit will almost definitely lead to consumer detriment as customers look for other unlicensed forms of credit instead.

Indeed the consultation paper states that it does "**not expect** *there to be any overall dilution of current levels of consumer protection, however it is unlikely that there would be a direct replication of the existing formulation of all CCA consumer protection in the* rulebook. If the new FSMA style regime is not providing a substantial increase in the level of consumer protection then it is questionable if we should be pursing Option 1. The enhancements introduced by the Consumer Credit Act and the European Consumer Credit Directive means that the consumers are already very well protected and therefore the customers would see little or no benefit in amending the regulatory regime.

Objective 3 – Promoting Opportunities for Simplification and Deregulation

Whilst the creation of a rule book offers an opportunity for simplification and flexibility, the regulatory regime would still be required to work within the legal framework of the European Consumer Credit Directive, regardless of which option the government chooses to adopt.

Furthermore given that the financial markets are so diverse and in particular the unsecured consumer credit industry, it is difficult to envisage how a significant level of simplification can be achieved while still maintaining and managing regulatory consistency across all market products. The rulebook approach is also likely to place a number of new obligations on some companies which may also contribute to further market exit.

Objective 4 – Proportionality and Cost Effectiveness

The consultation document states that level of risk will be used to allocate supervisory resources and some activities such as debt collection have low level of financial risk but may pose significant harm to consumers and therefore will require a high level of supervision and presumably a higher level of cost to the company.

The Impact Assessment states that an increase in compliance burden could lead to market exit or alternatively lenders may choose to pass the increased costs onto the customers, however either option could incur significant consumer detriment.

Conclusion

Consequently The Money Shop believes that the current method used to regulate the consumer credit market separately is successful and therefore our preferred option is Option 2 outlined in the consultation paper as retaining a specific consumer credit regime based on the Consumer Credit Act, 1974. Under the current regime with the OFT, there has been no regulatory failure and the consumers are aware of the regime and are familiar with how it operates. Crucially, in the Impact Assessment the Regulatory Policy Committee stated *"we have been severely hampered by a lack of evidence about the potential impact of moving to a FSMA –style regime"* and with this borne in mind we see little overall benefit in the government undertaking a new regulatory regime. We fully support the view detailed in the Impact Assessment which states that *"some creditors believe that the credit sector overseen by the OFT has been relatively stable, in spite of extensive legislative change. A change in regulator particularly one with limited of a wide and highly complex sector, could potentially be counterproductive in terms of uncertainty and upheaval*".

For further information please contact:-

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CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: **MORTGAGE GUARANTEE PLC**

RESPONSE to

A new approach to financial regulation:

consultation on reforming the consumer credit regime

respond to:

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or

Financial Regulation Strategy
HM Treasury
1 Horse Guards Parade
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16 March 2011

Consultation response from Mortgage Guarantee Plc on "a new approach to financial regulation: consultation on reforming the consumer credit regime".

Mortgage Guarantee Plc 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
Mortgage Guarantee Plc provides short term bridging finance to individuals and small businesses wishing to purchase properties in need of renovation or land for new build including social housing. Mortgage Guarantee Plc employs 5 people and further regulation such as that proposed would require an increase in staff which could not be accommodated in our present office, which in turn would involve additional expense in an economic climate where many small businesses are finding it increasingly difficult to survive.

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 and short term bridging 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

Kenneth Johnson
Managing Director

Subject: Consultation on Reforming the Consumer Credit Regime

I am responding as an individual to 'A new approach to financial regulation: Consultation on reforming the consumer credit regime'.

In short, I believe the Consumer Protection and Markets Authority to be misconceived (although I agree the micro and macro prudential supervision, especially of banks, should be relocated in the Bank of England, essentially as currently proposed).

A strong case was made by the heads of the Financial Reporting Council and the London Stock Exchange and others for a separate (wholesale and capital) Markets Authority (essentially as in the US). London hosts an international financial centre and it should be regulated accordingly by European and other international authorities. International banks and other financial institutions naturally have an interest in how it is run. Britain hosts the Wimbledon tennis and British Open Golf tournaments (and London will host the Olympics) in accordance with the agreed international rules. 'The City' should not operate under local rules like the Henley Regatta, and 'Brussels' can and should be involved in its regulation.

The retail financial (essentially banking and insurance) markets are domestic by nature and should thus be regulated separately. Consumer credit would naturally be part of the responsibility of a retail financial ('utility') regulator ('BankInCo'), which would also be responsible to assuring access to finance services (i.e. there would be a 'universal service obligation' in line with other regulated utilities) and that customers are 'treated fairly'. The competition authorities (also to be reformed) would be relieved from almost continued and over a decade long investigation of retail financial institutions (especially insurance companies and banks). The 'financial education' role taken over by

CFEB from the FSA 2010 might also be rolled into BankInCo (and so there would be no net gain in the number of 'quangos'!).

All that would remain would be to unpick the meaning of 'access to finance' and thus what the universal service obligation would be. The obligations to assure access and to 'treat customers' fairly, by abiding by extended Banking Codes, would become a condition of receiving a licence to take deposits and offer consumer credit and insurance.

Access to finance could narrowly mean access to payments services, including direct debits, to reduce consumer transactions costs. It might also include access to credit to help smooth consumption, in the face of irregular income or over the 'life cycle', or to engage in entrepreneurial activity; but this would be more contentious and links to the need to encourage both responsible lending and borrowing (and thus to raising consumer financial capability)

If the banks are not broken up into competitive units having no more than 10% of the retail market each (as in the US) and with commercial and investment banking separated, then the retail finance 'utility' regulator would need to guard against oligopolistic behaviour and cross-subsidisation. If, as seems likely, the return on equity in retail financial service provision fell well below that prevailing in investment banking, the big 'universal banks' might voluntarily divest themselves of their retail banking units; leaving the field open to Tesco, Virgin other potential providers.

Andy Mullineux
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HM Treasury
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Dear Sir/Madam

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National Housing Federation response to HM Treasury consultation on reforming the consumer credit regime

The National Housing Federation represents 1,200 independent, not for profit housing providers in England. Our members include housing associations, cooperatives, trusts and stock transfer organisations. They own and manage 2.5 million homes provided for rent, supported housing and low cost home ownership, including an increasingly diverse range of community and regeneration services.

We welcome the opportunity to outline our key thoughts on HM Treasury's consultation paper on reforming the consumer credit regime, in particular the proposal to transfer responsibility for consumer credit from the Office of Fair Trading (OFT) to the new Consumer Protection and Markets Authority (CPMA).

Housing associations currently perform a wide range of activities which are regulated under the Consumer Credit Act (CCA). These ancillary credit related activities are typically linked to their business as responsible social landlords, and include debt advice, debt negotiation, credit referencing and collecting third party debts. An example of these in practice may be where a housing association offers vulnerable tenants budget advice or helps them improve their financial skills.

Whilst these activities are rightly regulated by the CCA, it is imperative that the degree of regulation accurately reflects the risks. It needs to be acknowledged that these activities are performed to benefit tenants, often in pursuance of broader charitable and philanthropic objectives. Whilst low-risk and outside of housing associations core business, such valuable activities require housing associations to complete the time-consuming and burdensome process of applying for licences. We fully support the rationale behind requiring compliance with the less stringent CCA, but even this can be disproportionate to the risks associated with their work. Therefore, it seems difficult to justify requiring housing associations complying with the more complex and onerous Financial Services and Markets Act (FSMA) regime should the regulation of all consumer credit activities be transferred.

Another area of housing association activity currently regulated by the CCA is their provision of equity loans as a second charge on a property, when delivering

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government-funded low cost home ownership. Housing associations have, for the last 30 years, delivered a range of sustainable home ownership products to help households excluded from the housing market purchase their own home. A number of products have seen over 250,000 households on low to moderate incomes achieve their aspiration of home ownership. Of course, the provision of affordable and sustainable mortgage products is crucial in helping these households.

The most common equity loan product housing associations have typically delivered is Open Market HomeBuy. There were two forms of this product – MyChoiceHomeBuy and Ownhome. MyChoiceHomeBuy was an equity loan product used alongside a deposit and a conventional mortgage, funding between 15% and 50% of the property value. Interest is payable on the unsold equity and fixed at 1.75% or below in year one (rising by RPI plus 1% each year). OwnHome was again an equity loan product offered together with a conventional mortgage and funded between 20% and 40% of the property value. No interest is charged on the remaining equity for the first 5 years. For years six to ten, the equity loan is subject to a fixed interest rate of 1.75%, and from year 11 a fixed rate of 3.75%. Whilst both were discontinued in July 2009, as the Government focused investment on new-build home ownership products, they have helped thousands of households into home ownership. Many housing associations will continue to administer and manage existing loans where the full value has yet to be redeemed and the purchaser will be making interest payments on the loan, so would require FSA registration under the proposals.

Under the 2011-15 Affordable Homes Programme, housing associations are invited to deliver a new equity loan product, where they may offer a loan of up to 20% of the property value to the purchaser. Again, purchasers will pay 1.75% charge on the equity loan for year six, which will rise by RPI +1% per year thereafter. Under the new programme, housing associations will continue to deliver the government's Mortgage Rescue Scheme, which is designed to support vulnerable owner-occupiers facing repossession to remain in their home. Here, a shared equity option allows the household to remain as a homeowner. Their existing secured debt is reduced to an affordable level by an equity loan provided by the housing association. The equity loan is secured as a second charge with an interest charge of 1.75% per annum. This fee will rise by RPI + 0.5% per annum.

Therefore, the proposals to amend the regulation of the consumer credit regime have serious implications for housing associations and their ability to offer a range of equity loans, as the transfer of regulation of second charge mortgages to the Financial Services Authority (FSA) means they would have to become FSA registered. The FSMA represents very rigorous regulation. This appears wholly sensible for typical financial services provision, indeed we support the move to having one regulator for financial service providers. However, we believe it is wrong to conflate the services housing associations offer, in the form of equity loans, with this.

For equity loan regulation, we believe that that the existing CCA provisions offer a more appropriate level of regulation and consumer protection, notwithstanding the earlier concerns identified relating to the onerous and costly process of acquiring a licence. In addition to this, the sector is already independently regulated by the Tenant Services Authority (a function that will transfer to the Homes and Communities Agency in April 2012). As previously mentioned, the cost of compliance with an additional layer of regulation is disproportionate to the level of risk and will make the provision of equity loans very unattractive to housing associations due to the additional administrative and time costs incurred.

On a practical level, it is difficult to understand how suitable the FSMA regime is for the regulation of equity loans. As a requirement of both CCA and FSMA regulation, lenders must give borrowers particular information relating to the terms of their loan. For example, the Annual Percentage Rate (APR), the total charge to credit and the interest rate must all be provided. None of these can be provided for equity loans given the nature of the product – the loan is for a percentage of the open market value of the property at a particular point in time. Therefore, the APR equivalent, the total amount repayable and the interest rate equivalent are not known at the point the equity loan is granted – they are only known at the point of redemption. The CCA is flexible enough so as to allow housing associations to apply for a Direction from the OFT which exempts them from having to provide such information for equity loans. There is no detrimental effect on borrowers, as housing associations are able to give detailed examples based on assumptions as to house price increases. The FSMA regime does not offer similar flexibility.

It is clear, that if housing associations are to be able to continue offering equity loans to assist low to moderate income households, with a good credit history but without access to the ‘bank of mum and dad’, they must not be brought within the FSMA regime. To do so would be inconsistent and incongruous with the aims set out in the consultation. It would also jeopardise the ability of housing associations to deliver on a number of key government social and housing policy objectives, namely preventing repossessions and increasing home ownership opportunities for first-time buyers. There is a ministerial push to help first-time buyers, as reflected in the First-Time Buyers Summit hosted by the Secretary of State for Communities and Local Government and the Housing Minister. Moves to bring the regulation of equity loans offered by housing associations would reduce their capacity and appetite to assist in this.

Housing associations are currently exempt from FSA regulation of first charge mortgage lending, so when offering first charge mortgages fall outside the scope of the FSMA. This exemption is laid out in a statutory instrument (paragraph 48 of Part IV of the Schedule to the Financial Services and Markets Act 2000 (Exemption) Order 2001), and exempts housing associations and the Homes and Communities Agency from certain regulated activities. This currently only relates to ‘regulated mortgage contracts’, which is defined as first charges. Therefore, we believe that this exemption should be extended to incorporate the second charge lending activities of housing associations, so ensuring the provision of equity loans is not FSA regulated.

The option to extend this exemption to include the second charge lending activity housing associations perform, would represent a wholly sensible and logical step. As outlined, the activities for which housing associations are currently regulated by the CCA are very much on the borders of its purpose. They are low risk and wider housing association activity is already subject to regulation from the TSA. Moreover, the provision of equity loans by housing associations is preceded by a robust affordability check which ensures the consumer is adequately protected. We believe that housing associations provision of equity loans represents a low risk of consumer detriment, as consumers are already afforded a high level of protection. There is a simple way of restricting the exemption for the provision of credit by ‘registered providers’, as defined in the Housing and Regeneration Act 2008.

Notwithstanding the inappropriateness of regulation of housing association activity under the FSMA, the sector acknowledges the need to ensure a form of effective regulation of second charge lending. We believe this should involve the retention of the CCA for second charges granted by housing associations, as an existing approach which is well-known to housing associations and affords the consumer good protection. This would of course ensure consistency with EU legislation which requires there to be some form of consumer credit regime, under the Consumer Credit Directive.

Therefore, whilst we acknowledge the move to ensure that all financial service providers are regulated by the same body, we don't believe it is appropriate to include the activities of housing associations within this. It is wrong to conflate the activities of housing associations, in the pursuance of charitable and government housing objectives, with those of usual credit providers. The existing CCA framework, though disproportionate in parts, offers a more suitable means of protecting consumers. In addition to this, broader housing association business is regulated by the TSA. The exemption from FSA regulation housing associations are currently afforded when providing first charge lending should logically be extended to encapsulate second charge lending, by way of equity loans.

Yours sincerely

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Response

to the HM Treasury & Department for

Business, Innovation and Skills

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

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About the National Pawnbrokers Association (NPA)

The NPA was established in 1892 and is the Trade Association representing pawnbrokers in the UK. Membership is voluntary and today some 1,200 shops are members out of a total number of circa 1,600. The NPA Council comprises up to 14 individuals who have to be practicing pawnbrokers, assisted by a Chief Executive and his/her staff. The Officers of the Council (President, Vice President and Treasurer) are elected into office each year and Members of the Council serve for three years before re-election. There is a mixture of independent shops and the large chains of pawnbrokers serving on the Council to reflect the views of all members.

Members join the NPA for many reasons, not least to ensure that they are compliant with all the rules and regulations in relation to pawnbroking. Membership of the NPA also demonstrates to consumers a greater degree of assurance that the trading practices of NPA members represent the highest in the industry. In addition, should there ever be a dispute (which is recognised by the OFT as being rare) the NPA has often informally mediated to resolve the matter on behalf of the consumer as well as the pawnbroker. All members have been vetted before they joined the Association and we have a Code of Conduct to help ensure that standards are kept consistently high.

We shall only answer questions which are either relevant to the pawnbroking industry or where the Association holds a view: -

Executive summary

The NPA welcomes the opportunity to respond to the Government's consultation paper.
The key points we wish to make are as follows: -

1. The NPA rejects Option 1 for the reasons given below and would recommend Option 2. If this were not possible, a third option would be preferred where one regulatory authority is established, but consumer credit type businesses are regulated in the style of the OFT using as a basis the CCA 1974 and other business continue to be regulated according to the FSMA style.

2. We do not object in principal to there being one regulator, but strongly recommend that the style of regulation currently used by the OFT is retained in the new structure for all unsecured credit and pawnbroking. One of the key stated objectives is for proportionality. We all agree that the amount of regulation required to oversee a £100 loan (which is the average size of a pawnbroking loan) needs to be much less than a loan that jeopardises a person's home if they default. Although the consultation recognises that point, we have grave concerns that on past performance by the FSA, the amount of regulation (even accepting a light touch) will be far greater for some industries than is necessary.

3. The NPA believes that an FSMA style approach will inevitably be much more costly than the current approach taken by the OFT. The impact on companies is likely to be enormous and despite assurances of proportionality, the result will be higher prices and less consumer choice. If fees were increased to £1,000 or more per annum, you should be aware that many smaller companies will leave the industry resulting in less competition and reduced consumer choice. (***See point 7 below***). Those that choose to stay will have to pass the increased costs onto their customers.

4. We do not think it is necessary for a pawnbroker to demonstrate in the licensing process that they have sufficient funds to operate their business. If they do not have the funds they will not be able to lend. Again, we think that the requirement for capital adequacy is not proportional to the consumer risk and may deter new entrance into the market, resulting in reduced consumer choice.

5. We do not see how setting up the new regulator, repealing the CCA 1974 and in its place developing a 'principals based' approach, can possibly be effectively achieved by 2014. However, we think it may be possible to set up the FCA, retain the CCA 1974 and introduce an OFT style regulation for unsecured lending and pawnbroking in that time.

6. We think that that the CCA 1974 has served consumers well and is a comprehensive piece of legislation that has stood the test of time. By repealing it in its entirety, we believe that many important consumer protections could be unwittingly lost, particularly for very small industries such as pawnbroking, where its voice may not be heard. Additionally, thirty years of case law will also be made redundant over night, resulting in huge uncertainty for consumers and lenders alike. The CCA has been amended and refined in many ways over time to become, in the main, the effective legislation it now is.

7. Pawnbrokers offer a vital service to consumers, some of whom cannot obtain credit from High Street banks. The majority of consumers choose pawnbrokers for the no-nonsense, straightforward, simple, quick, convenient and transparent transaction that it is. Pawnbroking has over the past 10 – 15 years become more mainstream due to its growing popularity with consumers for precisely these reasons and as we have seen with the Early Settlement Regulations, to move to a new

governing regime could potentially upset the basic principles of transparency and simplicity which is what customers enjoy. This may see very many consumers at detriment when looking to borrow a small sum of money that is often simply to satisfy a very short-term cashflow problem. The number of pawnbroking consumer complaints is minimal (four complaints last year according to FOS). With complaint levels very low the NPA does not understand why a successful style of regulation that has served consumers well over the years needs to change. .

8. We can report that already four small independent pawnbrokers have decided to sell their businesses citing their difficulty in complying with the CCD that became mandatory on 1st February 2011. The NPA expresses real concern that ever more regulation will force even more independents out of the industry with consumers being the losers in the long run. The independents often bring innovation to the market (a good example in our industry is online pawnbroking, developed by a small independent and now copied by most of the large chains) that encourages the rest of the industry to react. The loss of these businesses may rob consumers of choice and reduce competition

9. After implementing the provisions of the CCA 2006, complying with the Irresponsible Lending Guidance and then very recently adopting the CCD, we think that there should be a period of reflection to allow the industry to settle and give it more certainty. The amount of management time that has had to be devoted to ensuring compliance to so much new regulation in such a short time has been enormous, putting real strains on companies big and small. When on average, the sum of money lent is £100 and is secured by the customer so they cannot find themselves in unsecured debt as a consequence, the argument for exemptions for certain industries such as pawnbroking, must surely be valid when seeking proportionality of regulation (and compliance cost) in the lending industry.

10. The NPA is concerned that it is the Government's stated ambition that the FCA will be a 'consumer champion'. This implies that there will be an inbuilt bias towards consumers without the necessary fairness necessary in an effective regulator to understand both consumers and industry before drawing conclusions. The existing aims and objectives of the OFT are fully supported by the NPA.

11. The NPA recommend that a further period of consultation is required to work out the best way of incorporating the CCA 1974 into the FCA and adopting an OFT style approach for industries like pawnbroking.

Questions

Chapter 1: The case for reform of the Consumer Credit Regime.

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

a) We take issue with parts of the assessment of the consumer credit mark. It paints an alarming picture inferring that the current level of regulation is not tough enough and needs to become more proactive and more focussed (1.5). The NPA's view of the OFT style of operation is that despite concerns of their interpretation of parts of the CCD and occasional delays in Consumer Credit Licenses being assessed, the OFT are a strong regulator and are passionate about regulating the lending industries for the benefit of consumers. They are very active but often get things done by talking to industries rather than resorting to immediate enforcement action. They do take enforcement action where necessary but our opinion is that they try to exhaust other avenues first. They do take an interest in understanding the issues affecting business and are willing to listen. The NPA has had a strong professional relationship with the OFT for many years and respect their knowledge of the industry at all levels.

b) It correctly says that there has been an increase in the number of pawnbroking shops but in the next sentence states that there has been an accompanying rise in the number of consumers struggling to pay their debts with an increased demand for debt advice and support (1.9). In our opinion this could lead to a mistaken view that pawnbrokers are the cause of this problem when they are not. In fact pawnbrokers offer a lifeline to many consumers who cannot obtain credit from High Street banks (and have not been able to access such credit for many years – not just during the current credit crisis). Consumers who need credit will go to extraordinary lengths to get it and we think it is agreed by everyone that it is better they obtain it from a licensed provider rather than resorting to an illegal lender. The increase in people resorting to debt advice is likely to be caused by the state of the economy.

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?

a) Although there are a few companies that currently need to be licensed and regulated by more than one body, the majority of companies just have one regulator. We would not wish to exaggerate the problems so caused. We would need much greater reassurance that the application for a licence and level of regulation for consumer credit will not be more onerous than it is at present. Pawn broking is characterised by a few large chains and many independent shops. The independents do not have the time or resources to devote additional work and money into a more robust licensing system. The CCA 2006 introduced a competency test that helps ensure that licence holders are 'fit to practice'. The NPA devotes much of its time to helping ensure that members are compliant with all rules and regulations. We are told that there are no problems with the industry and this surely supports the notion that the current level of licensing is fit for purpose. If the barriers to entry are raised higher, the consequence will be that both new entrants will be deterred and even existing licence holders may be forced to leave the industry. In the last week alone four companies have notified the NPA that they wish to withdraw from the industry because of the increased burden caused by the Consumer Credit Directive. The small independents are important for the industry because they bring innovation and strong competition. If more leave, the result will be less competition and reduced consumer choice.

3) The Government would welcome further evidence relating to the consumer credit regime.

a) Pawnbroking customers face very few, if any risks, when going to a pawnbroker. The average loan is only £100 (University of Bristol Research Report – Pawnbroking customers in 2010 - August 2010 attached). Under the CCA 1974 the pawnbroker is obliged to wait a minimum of 6 months if the debt cannot be paid. Again, given the protection of the CCA, customers with loans of £100 or more must be given notices that their pawned items may be sold if they do not redeem. Of course all pawnbrokers want customers to redeem and actively encourage them to do so and the redemption rate of c. 75% proves this. Only in a minority of cases will customers not be able to afford to do so. Often customers do not wish to redeem their goods (they may not wish to wear the item any more or it may be damaged) rather than not being able to afford to redeem. The risk lies purely with the pawnbroker because they run the danger of not covering their costs if items sell for less than was anticipated.

b) The pawnbroking industry is growing steadily (and has been since the 1980's – long before the present credit crisis) and the NPA believes that in part the growth is due to the CCA 1974. It gives protection to consumers and gives a framework for the industry that encourages fair lenders to offer much needed lines of credit. There is a real risk that if the CCA is repealed, many of these rights would be lost. Our reasoning for that is clear. The NPA was not even included on the circulation list when the CCD consultation paper was initially sent out and whereas banks and other lending institutions had years to make their case known to legislators, the pawnbroking industry had virtually no time to respond fully. The industry is comparatively small (the average loan book per shop is circa £160k) and risks being both overlooked and unintentionally swept up in wider legislation that is often, frankly, tightened for other lending markets that have acted considerably less well than the average pawnbroker. The absurdity is that secured credit (which includes pawnbroking) and loans under 200 euros are specifically excluded from the Directive, but the UK Government alone in the EU decided to include them. There is real concern that customers will be the losers if the CCA is repealed in view of our recent experience and much of the protection that they currently enjoy will be lost. The NPA has campaigned with BIS and the OFT consistently for clear transparent agreements that can easily be administered by businesses and easily understood by customers. The result is that around 80% of customers are repeat customers because they know how pawnbroking works and are happy and satisfied with the service. (95% were satisfied or very satisfied in the University of Bristol Research Report – Pawnbroking customers in 2010 - August 2010).

c) Although many pawnbroking companies only offer a pawnbroking service, the larger chains promote personal loans with insurance protection and so may have two regulators. They feel that the style of regulation adopted by the OFT is much more appropriate to the types of business they operate. It is less time-consuming for them but still gives high levels of protection to consumers.

d) The amount of new regulations being shouldered by pawnbrokers over the past few years has been staggering. The CCA 2006 introduced the Unfair Relationship test that brings uncertainty to lenders. In the same legislation, the Consumer Credit Licensing regime was strengthened (some thing that the NPA approved of at the time). New entrants to the market have to demonstrate that they are not only trustworthy, but they have the skills to perform as a pawnbroker. Again, that is something we applaud because the role of the NPA is very much to ensure standards are kept high, but its introduction does add to the burden shouldered by new entrants. We are of the opinion that the current level of licensing assessment is about right and think that moving to another regulatory regime will simply add another level of bureaucracy without delivering further consumer benefit. That could raise the barrier to entry too high for small players to come into the industry, with a consequent loss of consumer choice and less competition.

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

a) We do not believe that it will be possible to repeal the CCA, develop a Handbook of Rules in its place and set up a new regulator by 2014. At best we consider that setting up the FCA and transferring the CCA 1974 with only modest changes required, would be possible within such a challenging timescale. The implementation of the CCD was delayed by 6 months because it was not ready in time even after years of discussion. The changes suggested in the consultation paper are much more comprehensive and would need to be completed in only three years.

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.

a) We understand the Government's preference to adopt an FSMA style regulator for consumer credit. As explained above we think that there will be real consumer detriment should the CCA 1974 be repealed and a principals based approach put in its place. We are not averse to having just one regulator but we do suggest that the OFT style approach is retained for pawnbroking and other consumer credit products.

b) The industry needs a period of quiet to reflect on the impact of the CCA 2006 and the CCD. The amount of new regulation has been breathtaking with little apparent understanding of the impact on the firms (and their Trade Associations). Neither is there in our opinion any real understanding of consumer behaviour and attitudes. Is it really necessary for more regulation in an industry that is more regulated than any other in the EU? The creation of an FSMA style rulebook will inevitably mean more, not less, regulation despite assurances that a risk based, proportionate approach will be taken and having just borne a considerable amount of cost we feel further and higher regulatory cost on what are often small businesses (the businesses the Government say will lead the country out of the current economic crisis) to be unreasonable.

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

a) Trading Standards form an important partnership with the OFT and considerable amounts of information flows between the two bodies. Trading Standards are represented in every region of the country and are in a great position to see first hand what is happening on the ground and report their findings to the OFT. The consequence is that a detailed picture can be drawn at a granular level allowing for proper analysis and considered decision-making.

b) The consultation paper makes little mention of the role of Trading Standards and how they might liaise with the FCA. If there is no linkage and little or no communication the result is likely to be a London centred regulator relying heavily on detailed returns from regulated companies. The cost of completing and submitting those returns would have a serious impact on the firms involved. Many smaller companies will decide to exit the industry with the consequence of less consumer choice and less competition. Surely the current approach of only dealing with consumer problems where there are problems makes much sense?

c) It is the NPA's opinion that Trading Standards have improved in the past few years from an organisation primarily there to enforce and prosecute to one that gives advice and support to companies – most of whom just want to do things correctly. Any loss of such support and guidance would be regretted.

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.

a) As stated in 4a and in the Executive Summary, we believe that the Government should reconsider its position and transfer the CCA 1974 with only minor changes needed to make it fit into the new regime. There is genuine concern that many of the principles of consumer protections and fair trading built up over years in pawnbroking could be overlooked if the CCA was repealed. Even more importantly, all the CCA case law that helps guide companies and gives a firm framework will be lost at a stroke, giving rise to uncertainty for both lenders and consumers.

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

a) The NPA does not have an opinion.

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.

a) With flexibility comes uncertainty. Uncertainty could give opportunities for unscrupulous lenders and produce a lack of clarity for all concerned. This cannot be a desired consequence.. The prospect of frequent changes in the future (because it is much easier to amend a Handbook of rules than pri mary legislation) inevitably leads to higher costs for business and therefore prices for consumers and is not something that we support.

10) The Government welcomes views on the impact of a FSMA-style supervisory approach and appropriate consumer protection

a) We are very concerned about the cost of the new regulator. The FSA has an annual budget in excess of £500m per annum, whilst the OFT has a budget circa £10m. The new Consumer Financial Education Body (CFEB) budget is in excess of £46m, quite apart from the costs of running the FCA (formerly called the CPMA). We assume any increases in cost will have to be paid for by licence holders (and ultimately by their customers). There are many small independent pawnbrokers who will not be able to pay more than the current level of fees (currently circa £1,000 every 5 years).

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.

a) The NPA does not have an opinion.

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)?

a) The NPA favours the creation of the FCA with all consumer credit and pawnbroking to be regulated according to the CCA 1974 and all FSA regulated products being regulated according to their current regime. We think this simple approach will serve customers well and will allow the industry time to recover from the recent explosion in consumer credit regulation. There should be a robust market, strong competition and wide choice for consumers. The Government's preferred Option 1 is likely to negatively impact on all three. It is our opinion that the reality of trying to neatly fold all lending institutions under one umbrella is not a realistic aim and does not reflect the different industries and products available in our diverse credit market. One size does not ever fit all.

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?

a) The disadvantages as stated many times in this response are the likely huge increase in costs of regulation (to be borne by customers), uncertainty for lenders and loss of consumer choice. We want a vibrant industry that meets consumer needs and competes strongly for customers. The Government's preferred Option 1, is likely to reduce competition and increase prices for consumers. If there was evidence that consumers were dissatisfied then we might be more inclined to support this option, but we know from extensive research that that is not the case.

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?

a) The NPA does not have an opinion.

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?

a) Please refer to our answer to Q5 above.

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.

a) Bearing in mind the track record of the FSA, the NPA think it highly doubtful that the FCA will in fact introduce a truly proportionate approach to regulation. We would need firm assurances that smaller firms in particular would not be impaired by this approach.

b) We do not think it is appropriate in the pawnbroking industry for licence applications to show the adequacy of their capital funding. This is an industry that is well run, properly regulated and there is no evidence of consumer detriment using the current CCL procedures. We envisage that many small firms will not wish to apply for a licence if their capital funding has to be shown. Those that require bank lending will not know the level of support they will get until after their application has been approved. A typical pawnbroking shop starting from scratch will only build its customer base slowly and many will have a loan book under £50,000 after a year of trading. As trading develops the income from the existing business will help fund further expansion. Ultimately, if a business does not have sufficient capital it will not lend, so there will be no consumer detriment. We are not aware of that ever happening in the industry and so it would seem odd to impose this requirement when it appears completely unnecessary.

c) There is a real danger that if Option 1 is adopted it will damage the UK's economic recovery be cause the lending industry will be deluged in red-tape and damaged by the likely increased costs of regulation. We are also concerned that smaller lending groups such as pawnbrokers will be unintentionally caught up in significant 'heavy' legislation that is in place to protect consumers in industries where default has potentially dire and life changing consequences and this is not so in pawnbroking for the reasons previously stated.

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?

a) In 3.21 it states that 'fee levels would need to reflect any increased costs associated with achievements in the regulatory regime'. Firstly that presupposes that that the current regime is in adequate (which we do not agree) and that it is acceptable to increase the costs to industry. If 40% of firms regulated by the OFT at present are sole traders, we are very concerned that they may not be able to pay any more than they do at present. We would need to see strong evidence and a cast-iron commitment that full consultation is undertaken and a proper risk based assessment is made before such changes are made. It is extremely likely that any increases in fees will mean many small traders will leave the industry and the larger firms will put up their costs to consumers. The consequence will mean less consumer choice and those that do have the service will pay more.

b) In 3.25 the list of fees does not state whether these are paid annually or every 5 years. As the current fee is under £1000 every 5 years, even keeping to that frequency, but increasing the amount to £1,500 would be a very significant increase. If that fee was annual, the effect would be catastrophic. It is understood that the costs of supporting the CFEB will be in the region of £46 million annually, which by itself will increase licence fees substantially.

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

a) Other than the opinions expressed above, the NPA does not wish to elaborate further.

19) The Government welcomes:

a) evidence relating to experiences of the current appointed representatives regime;
b) 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
c) evidence relating to the implications an appointed representatives regime might have for firms and consumers.

a) The NPA does not have experience of appointed representatives and so will not comment.

20) The Government welcomes:

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

a) The NPA does not have an opinion.

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).

a) The NPA does have a Code of Practice and we ask members to self-certificate each year by way of a declaration.

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.

a) We believe that pawnbroking should continue to be regulated to ensure high levels of consumer protection, a level playing field and consistency within the industry and would not comment on other categories.

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?

a) We think the notion of a FSMA-style framework is flawed, being too costly and bureaucratic for simple consumer credit unsecured lending and pawnbroking. If one body has to oversee all regulatory supervision we suggest that the OFT-style regulation is transferred to the new body along with the CCA. The OFT is a robust and effective regulator and we support it fully. There have been no substantial failures (that we are aware) despite the many companies and sectors that it regulates. Ultimately with consumer credit it is the lender who takes the risk, not the consumer, so the levels of regulation need to reflect that.

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

a) This is not an issue for pawnbroking because the term of the loan is short (usually either 6 or 7 months).

25) The Government welcomes views on:

a) how existing licensees could be dealt with; and

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

a) The NPA believes that existing pawnbroking licence holders should have their licences grand-fathered and should not have to re-apply under any new system.

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

a) The NPA does not have an opinion

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

a) The NPA does not have an opinion

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.

a) The NPA does not have an opinion

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From:**PENRICAN CREDIT LIMITED**

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 *Penrican Credit Limited* on "a new approach to financial regulation: consultation on reforming the consumer credit regime".

Penrican Credit Limited 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 a family company established for 22 years with ten employees providing finance to individual users to purchase second hand motor vehicles.

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

David Shoesmith, Director

Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
London SW1A2HQ

21st March 2011

Dear Sirs,

Response by Retail Money Market Limited (trading as RateSetter) to Consultation on Reforming the Consumer Credit Regime

Thank you for the opportunity to respond to the Government's proposals for reforming the UK's consumer credit regime.

In our response, we provide an overview of RateSetter itself, explain why we support Option 1 and give our answer to each of the consultation questions.

We would be happy to discuss the issues further at your convenience.

Overview of RateSetter

1. RateSetter is a person-to-person (P2P) lending and borrowing platform[1] operated by Retail Money Market Limited at www.RateSetter.com. RateSetter was launched in the UK in October 2010. Retail Money Market Limited is based in London and employs 9 people. It has completed two rounds of equity financing from private investors totaling £1.5 million.

2. Since launch, RateSetter has facilitated over £2.6 million in loans, with zero defaults up until now.

3. RateSetter lenders remain in control of the management of their money, including the amount, interest rate and diversification. The RateSetter lending and borrowing process results in direct one-to-one loan contracts between each lender and borrower for the amount lent. Each lender receives repayments of principal and interest, while loan contracts are administered so that each borrower need only make a single monthly repayment at an APR that reflects the average of all lenders' rates plus arrangement fees.

[1] "Person-to-person (P2P) finance platforms" facilitate funding via direct, one-to-one contracts between participants. P2P finance platforms have grown in number and scale, attracting individual lenders looking for alternatives to savings and investments, as well as consumer borrowers.

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to be required under the Consumer Credit Directive. The prescriptive nature of the CCA documentation actually does not seem to make it as clear to consumers as they, and we, would like. For example, there is a requirement to include all intermediaries that are involved in a transaction meaning that if a borrower has obtained a loan from RateSetter having initially been directed to us by an intermediary, for example a price comparison site, both RateSetter and the price comparison site appear on the front page of the contract information which means that far more important information gets relegated further down the documentation which makes it harder for the consumer.

Answers to Consultation Questions

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

   Yes

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

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

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

      (i) Misunderstandings arising from the complexity of paperwork, including multiple agreements for the one overall transaction;

      (ii) Misunderstanding, or taking decisions based on, promotional or 'teaser' rates that rise to standard rates at a later time, e.g. credit card balance transfers;

      (iii) Costs arising from failing to understand complex or hidden fees (e.g. early settlement charges, card balance transfers fees, overdraft defaults or overdraft-related 'services' such as overdraft reserves, interest rates on credit cards held beyond the period in which the initial promotional rate applied).

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

      (i) Provisions designed to improve transparency, though the cost of some outweigh the benefit (e.g. highly prescriptive form and content rules);

      (ii) Provisions relating to linked and multiple credit agreements and the classification of different types of credit may introduce undue complexity in scenarios involving supplies of multiple goods or services that combine in a single service (e.g. life or general insurance premiums financed by credit).

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(iii) The unfairness test (though its effectiveness is undermined by the lack of clarity in its application).

(iv) Controls over debt collection.

(v) Advertising rules (though these are insufficiently flexible to cope with innovation).

(vi) Cancellation rights.

(vii) Inclusion of certain fees and charges in the APR calculation.

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

(i) Dual FSA/OFT licensing in context of general insurance financed by credit or relating to credit agreements;

(ii) Dual FSA/OFT licensing in context of supply of multiple goods or services that combine in a single service (e.g. card terminals in connection with the supply of payment services to SME's);

(i) Anti-money laundering supervision of FSA authorised businesses by (a) the OFT for CCA licensees and (b) HMRC for authorised payment institutions who are pure money remittance businesses.

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

Yes

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.**

A unified regime would:

(i) eliminate the artificial distinction between the use of credit and other financial services;

(ii) improve the ability for consumers to consider their finances as a whole; give greater clarity for consumers;

(iii) enhance UK influence of EU regulation of consumer credit and financial services overall by ensuring a single channel for policy and regulatory feedback;

(iv) increase control over bank activities and how they are funded currently.

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.**

The CPMA may benefit from localised enforcement through Trading Standards network.

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.**

Effective regulation of P2P finance platforms would enable a shift in the regulatory burden from lenders and borrowers to the platform operator. In particular, the platform operator acts as the repository of documentation and enables the formation of contracts in a consistent and transparent process. In addition, the operator is a convenient focal point for:

(i) Senior management systems and controls;

(ii) Minimum capital requirements;

(iii) Segregation of lender funds;

(iv) Orderly administration of loan contracts in the event that the platform ceases to operate for any reason;

(v) E-business IT systems controls; and

(vi) Complaints handling.

8. **The Government would welcome further evidence relating to:**

    a. **the use of consumer credit by small and medium sized enterprises (SMEs);**

    Not applicable to RateSetter

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

    Not applicable to RateSetter

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

    Not applicable to RateSetter

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.**

(i) Innovation should be easier if it can take place under a single, rules-based regime. However, the CPMA must be responsive to perimeter queries and issue guidance to assist firms in understanding what is permissible, without regard to extensive legal advice (e.g. the FSA's "Approach" document in relation to payment services). This will enable new entrants to set up quickly and efficiently, rather than lose momentum in the face of regulatory uncertainty.

(ii) The simple application process for varying a firm's scope of permission under the FSMA regime allows firms to more easily diversify their service offerings, thereby increasing competition and innovation.

(iii) Bringing credit within the same regulatory framework as credit institutions and financial institutions would also pave the way to EU passporting and a single market for consumer credit.

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

Given the likely number of firms requiring supervision, it would be appropriate for the CPMA to adopt a complaints-led approach, relying on self-reporting and complaints data, and targeted audits where appropriate. There would then be scope for closer supervision based on the scale of particular firms.

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.**

FSMA-style remedies should not be inconsistent with Sale of Goods-related remedies. It is worth retaining the liability of supplier and creditor to consumers under Section 75 of the CCA which is dealt with as between supplier and creditor under contracts for the supply of merchant services by the creditor to the supplier. Such merchant services agreements fall within the scope of the Payment Services Regulations 2009, for which the FSA is the supervisory authority.

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)?**

Yes. It is not at all clear why the use of credit instruments is not viewed as providing a financial service and regulated as such, particularly as the country's largest financial institutions are heavily engaged in both credit and other financial services.

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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?**

Additional advantages include: improved customer experience through consistent treatment of multiple services and reduced paperwork; lower costs for providers that may result in lower prices, better service, new products and/or product improvements.

We are not aware of any disadvantages.

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?**

Yes, the Government should consider the following opportunities in assessing the merits of option 1:

(i) The proportionate regulation of P2P finance platforms, which are growing in number and scale and attracting individual lenders looking for alternatives to savings and investments, as well as consumer borrowers;

(ii) Improvements in the consumer purchase experience (e.g. scope for reduction or simplification of contractual documentation requirements);

(iii) The requirement to treat customers fairly should yield greater transparency in relation to fees and charges;

(iv) The advantages of a unified regime (see answer to Question 5);

(v) Enhancements to consumer protection (see answer to Question 7);

(vi) The boost to innovation and competition (see answer to Question 9);

(vii) Enhanced prudential supervision (see answer to Question 16);
(viii) Bringing P2P finance platforms within the FSMA regime would broaden the scope for "horizontal credit intermediation"[2] to be used as a more transparent and stable alternative to "vertical credit intermediation"[3]. Specifically:

(a) The one-to-one legal relationship between the borrower and each participating lender (or his assignee) is maintained for the life of the loan via the same loan

[2] A credit intermediation process in which loans are made in separately assignable units at inception.
[3] A credit intermediation in which assets are split and re-packaged for the purposes of altering maturity, coupon and risk (e.g. asset-backed securities, collateralised debt obligations and credit default swaps): "Shadow Banking", NY Federal Reserve Board, July 2010 (http://www.ny.frb.org/research/staff_reports/sr458.pdf)

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origination and servicing platform, eliminating uncertainty as to loan ownership and enforcement entitlements;

(b) The intermediary has no balance sheet risk, and therefore no temptation to engage in regulatory, tax or other arbitrage;

(c) The interest rate and maturity of each loan do not need to be altered to enable the lender or his assignee to achieve diversification across different loans, loan terms and borrowers;

(d) The basis of the original underwriting decision remains transparent and available as the basis for assessing the performance of the loan against its grade, as well as for pricing the loan on assignment, making due diligence easy;

(e) To the extent that credit risk were to concentrate on certain borrowers or types of borrowers, those risks would remain visible throughout the life of the loan, rather than rendered opaque through fragmentation, re-packaging and re-grading; and

(f) The scope for moral hazard is also contained by the combination of these features.

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.

Proportionate application of each type of requirement outlined in paragraph 3.6 would be appropriate for all types of consumer credit businesses. Such requirements might include: at least one Approved Person; senior management systems and controls; the obligation to identify and manage operational risk; minimum capital requirement to cover adequate customer service, complaints and IT requirements; segregation of funds (where applicable); obligations to treat customers fairly; complaints handling; orderly administration of loan books on cessation of business; regular reporting; and complaints-led supervision.

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.**

(i) Number of current consumer credit borrowers (this is a more proportionate measure of size for P2P finance platforms, which enable lenders to diversify by making many small loans to different borrowers; and also reflects the scope of supervisory work involved in the protection of borrowers, and lenders' risk);

(ii) Income from consumer credit business (again, pertinent to P2P finance platforms, which do not assume balance sheet risk);

(iii) Fees should not be so expensive as to discourage participation in the regime and encourage loan sharks.

19. **The Government welcomes:**

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

     N/A

  b. **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**

     N/A

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

     N/A

20. **The Government welcomes:**

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

     Not applicable to RateSetter

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

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We see no reason to distinguish professional bodies from other types of membership-based organisations, so long as they all meet the same prudential obligations referred to in answer to Question 16 above.

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.

RateSetter's Terms and Conditions are a self-regulatory code, as they comprise an agreement amongst RateSetter, lenders and borrowers as to how RateSetter works in practice. In particular, we designed the RateSetter Terms and Conditions to ensure clarity and transparency that RateSetter does not constitute a collective investment scheme, insurance, deposit-taking or other investment activity.

The RateSetter Terms and Conditions cover (i) eligibility to be a lender or borrower; (ii) registration and membership set-up; (iii) how the borrowing and lending processes work; (iv) segregation of funds; (v) how loan contracts are concluded; (vi) how loans are serviced; (vii) the operation of the RateSetter Provision Fund and processes for the recovery of missed payments; (viii) the fees and charges that apply; (ix) variation (x) termination; (xi) use of personal data; (xii) liability for user content posted on the platform; (xiii) limits on liability; and (xiv) complaints handling.

We are also in the process of agreeing a P2P finance industry code with other P2P finance platform operators to cover the same sorts of rights and obligations that are addressed in the RateSetter Terms and Conditions. We are happy to share the final industry code as soon as it is finalised.

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.

Given RateSetter's regulatory position to date, we believe there is still a case for RateSetter to remain subject to self-regulation (or co-regulation, to the extent that the CCA applies in certain limited respects). This would of course minimise the cost to both RateSetter and the CPMA. However, we advocate the creation of a proportionate regulatory framework for P2P finance platforms, to preserve the reputation of the nascent P2P finance market segment by ensuring that operators design their platforms to address the underlying operational risks. We believe it is important that any new entrant fully understands the operational risks of running a P2P platform.

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 benefits of such a new regime are adequately explained in our answers to other questions.

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

The transition arrangements under the Consumer Credit (EU Directive Regulations) 2010 (and related CCA regulations) provide a reasonable precedent for the transition to FSMA regulation of consumer credit agreements.

25. **The Government welcomes views on:**

   a. **how existing licensees could be dealt with; and**

   Given the substantial difference between the CCA and FSMA regimes – and the potential for new business to be included (such as P2P finance platforms), it would not seem possible to 'grandfather' existing licensees automatically into the FSMA-style regime.

   Instead, every existing business that offers consumer credit that is within the scope of the new framework, whether or not that business is an existing CCA licensee, should be given a year to apply for CPMA authorisation; but not be able to carry out a controlled activity if it's application is ultimately rejected once the new regime takes effect.

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

   N/A

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

Given the likely rise in fees, it would make sense to have some form of transition relief.

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

It will be important that consumers be made aware of the transition timetable and its implications, so as to avoid uncertainty during the transition period.

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.**

N/A

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Yours Sincerely,

Rhydian Lewis

Rhydian Lewis
Chief Executive Officer, RateSetter

Cc: Peter Behrens, Chief Operating Officer, RateSetter

Cc: Giles Andrews, Chief Executive Officer, Zopa Limited

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RMI

Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
London
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14 March 2011

Dear Sirs

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

The RMI represents the interests of retail businesses within the automotive industry, one of the largest industrial sectors in the UK, employing 570,000 individuals in 70,000 businesses. The Retail Motor Industry sector alone has a turnover of £14billion. The RMI has 8,000 members representing the interest of New and Used Vehicle Dealers, Vehicle Repairers, Motorcycle Retailers, Petrol Forecourts and Vehicle Auction Houses.

The RMI welcomes the opportunity to respond to the Governments consultation – A new approach to financial regulation: consultation on reforming the consumer credit regime.

The ability to provide consumer credit is vital to businesses in the motor retail sector and virtually all our members who sell new and used vehicles have facilities to provide consumer credit to customers who require it. In view of this we are concerned that any changes to Consumer Credit, and specifically the regulatory authority overseeing it, are not detrimental to our members or restrict consumers in being able to source credit for vehicles they purchase. We believe the sector plays an important role in giving consumers access to credit at a reasonable price when buying a vehicle, which in some case they may not be able to obtain elsewhere. This has been highlighted during the economic downturn when sources of credit from banks and direct lenders has dried up, with only the most creditworthy customers able to obtain credit from these sources. In these circumstances many consumers have turned to dealers to provide the credit for their car purchases.

We would like to make the following responses to your questions:-

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

   The consumer credit market is changing rapidly and the motor finance sector is no different. We have seen an increase in importance of Point of Sale (POS) finance particularly through the recession. POS finance is up 4% between 2009 and 2010, with 52.1% vehicles funded this way last year compared to 45.8% in 2009. This market has seen considerable development over the last decade with new finance products being introduced so that not only traditional hire purchase is available, but contract purchase and leasing style products are also widely obtainable.

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 responsibility for consumer credit and other retail financial services?**

There would be benefits of one regime for financial services as opposed to the current one where responsibility is split between the FSA and the OFT. However the two regimes are very, very different and moving consumer credit licensing to the FSA or its new equivalent would not be as straightforward as straight merger. The impact of moving credit licensing may produce more downsides than the benefits that appear at first glance. We agree that confusion may occur with consumers when they have to deal with two rather than one regulating authority, but there may easier way of dealing with this such as clearer information and consumer education.

As far as the regulatory framework is concerned we except that the CCA and other regulations impacting finance is very different to the FSMA that governs insurance. We agree that dealing with two regimes may be complex, however currently the consumer licensing regime is fairly straightforward, most regulated firms cope well with its demands and the cost is relatively low. FSA regulation has proven difficult and costly for our members, with many needing to recruit extra staff or use outside consultants to help with compliance. We have seen a number of dealers stopping providing insurance following FSA regulation.

3. **The Government would welcome further evidence relating to the consumer credit regime, including a 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.**

No response

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

See question 5

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 broadly in support of one authority regulating retail financial services, and believe it would bring more clarity and cohesion to regulation of financial services. However we are very concerned about how that one regulator will regulate and its consequential impact on businesses in the motor retail sector.

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 response

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.**

   No response

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

   See question 9

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.**

   We are able to see the benefits of a flexible regime that allows the regulator to revise its rulebook in a dynamic way to reflect new products and new business circumstances. However this approach is potentially very woolly and open to interpretation as in the case of the FSA's 'Treating Customers Fairly'. It also means that you get regulatory 'creep' as FSA develops its rulebook without reference to Parliament. Although legislation is slow and not always reactive it does allow independent scrutiny of regulations.

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

    No response

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 the new regime.**

    There is an important link between the sale of goods and finance regaulations in sectors such as Motor Retailing where there is credit provided with the sale of a vehicle. The OFT's powers in these areas have generally worked well together. It is important in the future that the role played by the OFT is not reduced or lost by consumer credit being removed to another body. There is a risk that with two or more bodies involved that issues will be lost in the 'cracks' between them and that consumers will have difficulty knowing which body is regulating. Currently if a consumer has an issue with a car he has bought on finance he will go to Trading Standards regardless of whether it is faulty goods or finance issue. Under the proposals the customer will have to decide and understand which agency is best to deal with it.

Further, under the current structure the OFT have the ability to look at the record of business with trading standards when evaluating a credit licence. Thus allowing the OFT to decline a licence to a business that has breached consumer regulations not just in the realm of consumer credit. Being able to look at the whole picture allows the OFT to review how well a business operates within consumer law as a whole before giving a licence. In the retail motor sector this is important where dealers at the margins will not be adhering to basic consumer law and carrying out illegal practices such as clocking. Not only will these dealer be refused a licence but by not giving them one it may also be used as a stick to stamp out other illegal practices.

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)**

    See question 15

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

    See question 15

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?**

    See question 15

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 ?**

    We do not believe that moving consumer credit regulation to the CPMA(FCA) is the right move currently. Businesses are still coming to terms with significant changes to consumer credit regulation brought about by the new Consumer Credit Act in 2006 and more recently the implementation of the Consumer Credit Directive, not to mention several other smaller pieces of regulatory change. The impact of these changes has been costly and time consuming for business particularly for compliance. For instance the new consumer credit licences application forms have been far from simple to complete with our members employing accountants and even lawyers to help them.

    We feel that more change will be difficult for businesses to cope with and is likely to add further compliance cost. We do not as such disagree with another body regulating credit but the experience of the sector with dealing with the FSA has not been good. When we survey our members shortly after FSA regulation of insurance we found that on average each member spent on £10,000 per dealership site applying and complying to the new regime. This is on top of the additional time spent by dealer staff carrying out compliance work.

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 businesses?**

We have serious concerns over fees as they are currently much higher for the FSA than OFT, particularly as the FSA require an annual fee. Further reporting requirements for FSA have proven onerous for small businesses with many requiring additional outside help such as accountants to complete them. It is both fees and reporting that have lead to many small businesses stopping their registration with the FSA and pulling out of the insurance market.

17. **Do you agree that statutory processes relating to CPMA rule-making, a risked 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?**

This may work, however we have seen annual fees rise considerably over the past few years and the FSA actively encouraging business to de-register from them. We are concerned that in the short term fees will be held down but in the longer term the remit of the new authority will extend and with its costs increase.

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

The Government needs to be aware that for you average small business the move from the OFT's application and maintenance fee to the FSA application and annual fee will see business fee costs rise nearly 8 fold, when looking at a 5 year period. This would be an unacceptable additional burden on small businesses.

The following factors should be considered when assessing fees :

- Many firms will have only recently applied and paid for a consumer credit licence, it would be unfair to expect them to reapply to the FSA before the OFT would levy a maintenance payment.
- A number of firms are already FSA authorised and this should be extended automatically to cover consumer credit licensing if required and without cost if they hold a valid licence from the OFT.
- Much of the cost of FSA regulation to business has not necessarily been in the fees. It is the additional cost is complying with the rule book, in particular reporting, training and procedures.
- The new authority will need to understand they are dealing with SME's with limited resources, funds and staff.

19. **The Government welcomes:**
    - **Evidence relating to experiences of the current appointed representatives regime**
    - **Views on how an appointed representative model might apply to different categories of consumer credit activities, including how current business models and network might lend themselves to such an approach; and**
    - **Evidence relating to the implications an appointed representative regime might have for firms and consumers**

The appointed representative (AR) model has not been particularly successful in the motor retail sector. It was particularly slow to take off with very few appointed representative networks being available at the outset of FSA Insurance regulation in 2005. Few insurers were willing to take the risk. Over the past 6 years a few networks have been set up particularly to sell mechanical breakdown insurance/warranties, this has allowed some very small firms to no longer register with the FSA. However, the vast majority of the sector are still registered having found no viable alternative. The credit sector may prove different as dealers do have stronger relationships with their finance houses than insurers, but there are many reasons why dealers may still find being AR difficult. AR networks do not work well where dealers represent more than one vehicle franchise or where they sell a number of products from differing insurers. Also motor retailers tend to use more finance houses than insurers, having a range of lenders to hand rather than just one or two insurer, again making it difficult to be an AR .

20. **The Government welcomes:**
    - **Evidence relating to experiences of the current group licencing regime**
    - **Views on how the professional bodies regime might be adapted for different categories of consumer credit activities**

No response

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 (SME's)**

No Response

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 Response

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 response

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

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,**

If the move were to take place we feel that existing licences should continue to be treated as they are currently and only new licences coming under the new rules. It would be unfair for businesses to be judged by rules that did not exist at the time that an agreement was put in place. It would also be a particular issue for any business that chose not to become registered under the new authority and stopped providing credit.

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.**

If the move occurs we believe that existing licence holders should be transferred automatically to the new authority. This would avoid additional cost and administration for our members. Review of these licences can then be undertaken over a period time enabling a considered and orderly approach from the new licensing authority. In the case of existing FSA authorised businesses their approvals should just be extended to cover consumer credit providing a valid licence is in place.

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

See question 25

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

The retail motor industry came under FSA jurisdiction in January 2005. For the previous 12 to 18 months motor dealers had dealings with the FSA through the application process for authorisation. This was not an easy experience for our members, the application process was complex and information given by the FSA was not clear or helpful leading many dealers to use consultants to complete the process. Understanding the FSA rulebook was also difficult for businesses that are not Financial Services companies. The Rulebooks are full of terminology that retailer such as dealers do not normally see during there every day business.

A number of motor retailers chose not to become authorised in 2005 preferring to stop providing insurance altogether. Some continued to provide some sort of mechanical breakdown cover taking the form of an uninsured guarantee. These were a direct side effect of FSA regulation, until then few dealers provided these products preferring to give customers a more secure insurance backed warranty. This could be a good case of unintended consequence of regulation that is too onerous or expensive for business.

For those businesses that became authorised many found that the cost of regulation outweighed earning potential from insurance. When we surveyed members in 2007: 28% made less than £1000 from insurance, this would not cover the cost of annual fees, FOS levy and PII cover; further 75% of our members made less than £20,000 per annum. This set against start up cost of £10,000 began to make regulation uneconomic for some businesses. Over time smaller dealers left authorisation, they either joined one of the few networks available, or stopped selling insurance products. Some of the slack was picked up by authorised representative and by 2007 9% of members were part of a network. At the same time 69% of our member were FSA authorised leaving 22% not selling insurance at all. Prior to regulation almost all vehicle dealers sold some form of insurance. We believe that more dealers have left authorisation in the past two years as FSA fees have increased sharply.

FSA regulation has hardest hit the smallest businesses where costs and compliance are just not economical. Larger businesses with higher levels of insurance business have been able to cope better, although they have been faced with increased costs for supplying insurance. Appointed Representative networks heralded by the FSA as a viable alternative were slow to be set up not helped by the unwillingness of insurance to take on the risk of third parties. Dealers were on the whole left with a stark choice of becoming authorised even if uneconomic or stop selling insurance.

If you require further information, please feel free to contact us. Finally, we would welcome an opportunity to meet with you to discuss our concerns.

Yours faithfully

Louise Wallis
Head of Business Development

Tel: 01788 538336
Email: louisewallis@rmif.co.uk

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: **RICHMOND INVESTMENTS LIMITED**

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 Richmond Investments on "a new approach to financial regulation: consultation on reforming the consumer credit regime".

Richmond Investments 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 Principal Lenders established since 1934 . dealing in unsecured loans and have 2 employees

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

Philip D Ross.
Director

Sent by e-mail to **financial.reform@hmtreasury.gsi.gov.uk**

Financial Regulation Strategy
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

22nd March 2011

Dear Sirs,

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

Royal & Sun Alliance Insurance plc, is a member of the RSA Insurance Group (RSA), a multinational insurance group writing business in 130 countries with major operations worldwide. In the UK, RSA operate solely in the general insurance market. Our response to this consultation relates only to the potential impact of the proposed reforms on the general insurance market.

Our key thoughts about the Government's proposals are as follows:

- We support the Government's proposals, under option 1, to transfer consumer credit regulation to the Financial Conduct Authority (FCA) under a FSMA-style regime. We agree that this will provide a flexible and responsive regulatory regime and improve regulatory oversight;

- The payment of insurance premiums by instalments should be removed from the consumer credit regime. Provision is already made in the Consumer Credit Directive for such payments to be out of scope but the CCD has not been implemented in this way in the UK (leading to differences with certain other EU jurisdictions). They present a very low risk of customer detriment and existing conduct of business rules and TCF principles already provide adequate consumer protection;

- Insurers would incur considerable costs in transitioning to a new consumer credit regime which, in the light of the low risks posed and the protection provided by existing regulation, would be contradictory to the Government's stated objectives of simplification, deregulation, proportionality, and cost-effectiveness;

- 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. In particular, the funding and operation of the Financial Services Compensation Scheme (FSCS) should be given careful consideration and should avoid inappropriate cross-subsidy from other market sector sub-schemes; and

- The Government should give careful consideration to the timing and processes for increasing the responsibilities of the FCA. Any further changes in regulation at a time when they are undergoing significant regulatory and structural change themselves will be extremely difficult and the Government will need to ensure that it does not divert the new regulator from its core objectives.

Please feel free to contact me should you require any further information. I can be contacted on 0207 337 5280.

Yours faithfully,

Alison Rayner
Head of UK Regulatory Risk & Compliance
RSA Group

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;**

In the general insurance market, a policyholder who chooses to pay their insurance premium by instalments is not subject to the same level of risk as consumers in other markets who choose to pay for goods and services under a credit agreement.

An annual insurance contract, paid by instalments, can be cancelled at any time. The policyholder pays only for the period of cover received and is not required to pay for the unexpired period of insurance.

Under other forms of credit agreement, the customer pays a regular amount until the amount owed is paid in full. Any default in payment results either in the return of the item purchased or in the accumulation of debt until the balance of payment is made.

Therefore, policyholders who pay insurance premiums by instalments do not face the same risk of debt and insurers should not be subject to the same burden of regulation as providers of credit operating in other markets.

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

We support the Government's proposals to transfer the responsibility for regulation of consumer credit to the FCA. In the case of regulation of credit in relation to the payment of insurance premiums by instalments, we believe the current FSA regulations (which we expect to be retained to a considerable degree under the FCA) are adequate to provide the necessary level of consumer protection.

A customer who pays for their annual insurance contract by instalments benefits from the consumer protection provided under the current FSA regulations. These include conduct of business provisions relating to:

- "fair, clear and not misleading" communications and financial promotions; and
- the provision of information relating to the contract's main characteristics (including information about price, and the contract's features, benefits and limitations) prior to the conclusion of the contract.

In addition, TCF Outcome 3 requires firms to ensure "Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale". Together, the conduct rules and TCF principles ensure that consumers are given appropriate information about any terms associated with instalment payments.

Therefore, we strongly encourage the Government to exclude insurance premiums from the scope of any new FSMA-style consumer credit regime, because the current regulations are already adequate, to avoid unnecessary duplication, and in accordance with their objectives for simplification, deregulation, proportionality and cost-effectiveness.

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

The Consumer Credit Directive (CCD) specifically excludes insurance contracts from its scope. Therefore, the Government should take the opportunity of transferring responsibility for consumer credit regulation to the FCA to remove the current "gold-plating" of regulation. There is already adequate regulation and the low risk of customer detriment makes further regulation both disproportionate and unnecessary.

Therefore, insurance contracts should not be subject to the consumer credit regime.

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

We agree with the Government's objectives in transferring consumer credit regulation to a FSMA-style regime and, therefore, making the FCA responsible for the new regime. In particular, we support the objectives for simplification and deregulation and to remove unnecessary and unjustified regulation.

Therefore, as we have set out above, we believe that general insurance contracts should be excluded from the consumer credit regime, in accordance with the Government's objectives of proportionality and cost effectiveness.

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.

We agree with the Government's proposals for reform and that a move to a FSMA-style regime as part of the new FCA will deliver the best outcomes. However, please see our responses to Questions 3 and 4 about the deregulation of insurance contracts and Questions 10, 14 and 26 about the associated costs and fee structures.

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

As we have stated in our response to Question 3, we believe that the current FSA conduct of business rules and TCF principles are sufficient to provide the necessary level of consumer protection for insurance contracts paid by instalments. Therefore, insurance contracts should be excluded from any new FSMA-style regulation in order to avoid unnecessary duplication.

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.

We agree with the Government's assertion that a FSMA-style regime will provide a more flexible and responsive framework than a regime set out in legislation. We are also pleased to note that any changes will be subject to the appropriate consultation and cost-benefit analysis.

However, we would also remind the Government of the costs of moving to a new regime and would encourage them to give full consideration of the exclusion of insurance contracts before insurers incur significant transition costs.

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

We require clarity about the potential impact a FSMA-style regime will have on the funding and operation of the Financial Services Compensation Scheme (FSCS).

As an insurer, we are already subject to payment of levies in our fee-block and do not believe insurers should be subject to any increase in levies, even if insurance contracts remain in the scope of the consumer credit regime. The risk of an insurer failing is not increased by any such change in the regime.

We believe that the consumer credit regime should be dealt with in a separate sub-scheme and would strongly oppose any arrangements that would result in any cross-subsidy from other schemes or sub-schemes. Also, existing members of the FSCS should not be retrospectively responsible for any liabilities incurred by consumer credit market participants under the previous regime.

Q12. 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)?

We agree, but please also see our response to Question 4.

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?

As the Government has stated in the consultation paper, their objectives in moving to an FSMA-style regime under the FCA, in accordance with Option 1, include the opportunities for simplification and deregulation in seeking a regime that is both proportionate and cost effective.

In our responses above, we have given reasons why insurance contracts should be excluded from the new regime and would ask the Government to give due consideration to the significant costs that insurers would incur in moving to the new regime including, changes to processes and systems, customer documentation and communications, and for staff training. In our view, such costs will be disproportionate to the consumer benefits, if any, that might be achieved.

We also believe that the costs of funding the new regime (including any fees and levies in relation to the FCA, FOS and FSCS) should be borne by the users of the regime in proportion to their relevant size and scale of activities.

Finally, we suggest that careful consideration should be given to the timing of any transfer of responsibilities to the FCA, or to any alternative regulator. The financial services industry is already facing a period of significant regulatory reform and the potential impact and disruption of any further changes taking place at the same time, must be taken into account when deciding on any transitional arrangements.

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?

As we have stated throughout this response, we believe there is considerable justification for the payment of insurance premiums by instalments to be excluded from the consumer credit regime.

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 believe that the costs of funding the new regime (including any fees and levies in relation to the FCA, FOS and FSCS) should be borne by the users of the regime in proportion to their relevant size and scale of activities

Please also see our comments in response to Question 10 with regards to the operation of the compensation scheme and the cross-subsidy between sub-schemes.