

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: FAMILY FINANCE LTD. 93 Commercial Street, Tredegar, NP223DN

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 Family Finance Ltd on “a new approach to financial regulation: consultation on reforming the consumer credit regime”.

Family Finance Ltd is pleased to submit a response to the recent consultation on “a new approach to financial regulation: consultation on reforming the consumer credit regime.” We understand and are concerned that the Government's 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. Employing nearly 70 staff, we have been providing consumer credit facilities locally, since 1953.

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

J R Phillips
Managing director

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: **Ferratum UK Ltd**

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

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Ferratum UK 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 Government's 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.

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- Our business falls into the “small to medium sized enterprise“ [SME] category
- Founded in 2005, Ferratum is a Finnish mobile micro loan company with wide European presence
- Offers small unsecured short-term loans to private individuals
- Over 700,000 customers in 15 EU countries
- We are about to launch our UK operation in the coming weeks

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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

Jane Shaw
UK Operations Manager
0151 448 7324



A NEW APPROACH TO FINANCIAL REGULATION: CONSULTATION ON REFORMING THE CONSUMER CREDIT REGIME

Response by the Finance & Leasing Association

Executive Summary

- The Government's proposals represent the most significant change to UK consumer credit regulation for a generation. The scale, complexity and economic impact of what has been proposed should not be underestimated. The FLA is committed to working closely with the Government to achieve a good result for consumers and lenders.
- The FLA does not oppose in principle the transfer of regulatory responsibility for consumer credit to the new FCA. But this will only work if the regulatory framework applied by the FCA is appropriate: otherwise, the market is likely to contract significantly.
- A regime based on the current Financial Services and Markets Act (FSMA) would fail this test. Many features of the current FSA regime make little sense in a market where the burden of risk lies with the lender rather than the customer (unlike in the deposit and savings markets).
- The problem can be mitigated if any new regime for consumer credit instead takes as its starting point the EU Consumer Credit Directive (the CCD), recently implemented in the UK via the Consumer Credit Act. This will also help manage the major issue of how to deal with existing loan books.
- If the FSA/FCA is – as suggested – also expected to design the detail of the new system and oversee the transfer, it will need resources which it does not currently possess, and a realistic timetable.
- Given the scale of change contemplated, we estimate the project will take between five and seven years (the last revision of the Consumer Credit Act – a much less radical exercise – took four).
- A detailed Impact Assessment which covers the full costs for both lenders and consumers of the new regime will be essential. The current Assessment fails to do this, as the Government's Regulatory Policy Committee has already indicated.

Introduction

1. The FLA represents the UK consumer credit, motor and asset finance sectors. Our members include banks, building societies and many other types of independent finance company. Last year, they provided £50 billion of consumer credit to their customers, a third of the UK total. This included credit and store cards, unsecured loans, store credit, second charge mortgages, and funding for half of all private new car sales.

2. On 21 December 2010, the Government published *A New Approach to Financial Regulation: Consultation on Reforming the Consumer Credit Regime*, which proposes to transfer consumer credit regulation from the Office of Fair Trading (OFT) to the new Financial Conduct Authority (FCA) by 2014. As the FLA represents credit providers of all sizes, including many which are not banks, we are well-placed to comment on the impact of the Government's proposals on the whole of the UK's diverse consumer credit market, including their likely effects on competition and on the availability of credit. We look forward to working closely with the Government to ensure that any new regime serves consumers and lenders well.
3. Our starting point is the observation that no evidence has so far been adduced to demonstrate problems with the current regime of consumer credit regulation so serious as to require a radical new approach. While we understand the Government's wish to consolidate all retail financial services regulation in the same place, and the practical question posed by the OFT's impending merger with the Competition Commission, the context for the Government's consultation paper (CP) seems to be the requirement to find a sensible new home for consumer credit regulation, rather than any obvious need for profound change in the current system.
4. This is important, because the credit industry has over the past five years collaborated closely with successive governments and the current regulator to implement a radical overhaul of the existing system. This includes a major revision to the Consumer Credit Act, the implementation of the EU Consumer Credit Directive, new Lending Guidance from the OFT, and a series of specific market improvements implemented via industry codes of practice. The result is a well-regulated UK consumer credit market. But that market has also shrunk significantly in recent years. Lower-income borrowers have been particularly hard hit by reduced credit availability. This is the background against which the Government's proposals must be assessed.
5. It is also important to remember that around 40% of the current UK market is provided by non-banks. And, looked at another way, 40% of all existing holders of licenses to provide credit are sole traders. Any new regime which ignores these facts is likely to cause a significant reduction in the size of the market and leave many current borrowers without recourse to regulated credit. We are therefore very concerned about the application to consumer credit of a regime closely based on the current FSA approach in the savings markets, as the CP proposes. Such a regime will not work for consumer credit because of the fundamental difference between credit (where the main risk lies with the lender) and banking/saving (where the main risk lies with the customer).
6. For example, the new regime would introduce capital adequacy requirements for all lenders, make lenders responsible for the regulatory compliance of their

intermediaries, require all existing lenders to re-apply for authorisation, apply a new approved persons regime, and impose significantly higher regulatory fees. This would be the most radical change to consumer credit regulation for decades, and by far the most costly. Any of these elements alone would mean that large numbers of small businesses could be expected to leave the market, and many others would in all probability withdraw from at least part of their current markets. Taken together as a package, the effect would be that the UK credit markets could shrink considerably, credit availability would be seriously restricted and market competition greatly reduced.

7. We would therefore like to work with the Government to develop a new regime which avoids such unintended consequences and achieves a workable framework for both lenders and consumers.
8. The rest of this response is divided into two sections. The first sets out five key principles which we believe should govern this large and important regulatory project. The second responds to the specific questions raised in the Consultation Paper (CP).

Section 1: Key Principles

1. **A vision for the future of consumer credit must be agreed.** This will in turn shape the scope and content of the new regulation, and avoid the currently very real prospect of serious unintended consequences. If the Government intends a significant reduction in the number of lenders, along with much tighter limits on the availability of consumer credit, then applying the current FSMA regime as suggested would certainly achieve this. But if the vision is of a competitive credit market comprising a broad range of different types of lender delivering real choice for consumers, a different approach will be needed. The FLA strongly supports the latter vision and we hope the Government will, too.
2. **The risks to lenders of providing consumer credit must be recognised throughout the process.** New regulatory requirements can then be pitched appropriately to take account of this risk. The FSMA regime was designed to protect consumers against the loss of their savings, homes and insurance cover if banks, mortgage lenders or insurers went out of business. The consumer credit markets are fundamentally different, because the main risk rests with the lender.
3. **Regulatory change must represent real value for money.** Every time new requirements are placed on markets, the costs to businesses and consumers rise. The new regime must be measured against a robust Impact Assessment at each stage of the process. The Regulatory Policy Committee has already raised major concerns about the Impact Assessment published as part of the CP. The Committee has drawn attention to the incomplete analysis of the administrative

burdens for firms, as well as of the impact on competition and possible consumer detriment.

4. **The timetable and resources applied to the design and implementation of the new regime must be realistic, and kept under regular review.** Recent experience shows that even incremental regulatory change in the consumer credit market usually takes around two years to design and a similar period to implement. But what the Government now proposes is a radical break with the past and represents the biggest change to the market in 30 years, with serious implications for all existing lending. Realistically, what is currently proposed will need somewhere between five and seven years from start to finish, including early design work, the transfer of responsibility to the FCA, development of and consultation on a new system, and then implementation across a market currently consisting of nearly 100,000 credit licence holders.
5. **A proportionate approach must be adopted.** The House of Commons Treasury Committee said, in its recent report on regulatory reform in the financial markets (February 2011):

'The challenge will be to produce a regulatory structure which reduces the systemic risks financial services pose while ensuring economically advantageous activity is not driven out by inappropriate regulation'

Section 2: Responses to the Questions

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

We agree that the UK consumer credit market will play a central role in the economic recovery and that the regulatory framework must keep pace with market innovation.

But the Consultation Paper paints a picture of a rapidly expanding credit market which has resulted in an increasing number of customers getting into debt difficulties. This is simply not the case. 2010 FLA market data shows that consumer credit provided by its members fell by 6% and the level of new business was down almost 25% on three years earlier. The rate of contraction in some sectors has been acute. For example, store card lending fell by 21% in 2010, store instalment credit by 18%, and unsecured loans by 24%, compared with the previous year. This contraction in part reflects tighter lending requirements under the CCD and the OFT's Irresponsible Lending Guidance, as well as more cautious consumers.

While some markets have bucked the overall trend, there is no evidence that UK consumer credit lending is forcing customers into financial difficulties. In an economic downturn, many customers find it harder to meet their obligations, and not just for consumer credit. This reflects changing circumstances including unemployment, rather than poor lending practices.

In addition to looking at how the market itself is changing, any new regulatory system must take full account of the raft of new regulations which has been introduced in the past five years. This started with the Consumer Credit Act 2006 (much of which was implemented in 2008), and includes the OFT's recent Irresponsible Lending Guidance (ILG), the package of new regulation in the credit and store card sectors introduced in 2010, and the implementation of the EU Consumer Credit Directive (the CCD) on 1 February 2011. No other financial services sector has faced such relentless regulatory change in such a short and recent period. Much of it is still bedding in. Before introducing more requirements, we urge the Government to take proper stock of how all this new regulation is working in practice.

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

We do not agree that there is a 'fundamental weakness caused by the split in responsibility for retail financial services between the CCA and FSMA regimes', and note that no evidence has been adduced in support of this assertion.

The truth is, that while it is certainly not perfect, and while it has a different statutory basis from the FSA, the CCA regime as operated by the OFT has been effective both in protecting consumers, and in ensuring that the UK consumer credit sector was not a key factor in the recent recession. It would be difficult to make a similar claim for the existing FSMA regime, which has – as the Government has publicly acknowledged – proven less than fit for purpose in a number of ways. Major changes would therefore be needed before it could be shown that a FSMA-based regime would improve on existing arrangements. (Which is not to argue that no improvement is possible – see below.)

There is also little evidence to show that consumers have, as asserted, been significantly confused by the "split" in regulation between the OFT and the FSA or have not been able readily to seek recourse when things have gone wrong. This is because there already is a single point of contact for consumer complaints in the form of the Financial Ombudsman Service (FOS). In practice, consumers are not concerned about who the regulator is, as long as there is a clear means of dealing with poor practice and it is easy to bring a complaint. This is already the case.

We do however agree that the inflexibility of the CCA has sometimes presented difficulties, not least because primary or secondary legislation is often needed to effect change, and the process is slow and bureaucratic. This has resulted in the current 'patchwork' of consumer credit regulation, as the regulator and the industry have sought to plug gaps via guidance and/or Codes of Practice. And we also welcome the suggestion that the opportunity should be taken to deregulate in areas – for example – where the CCA has 'gold plated' European regulation.

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

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

The risks faced by consumer credit customers are very different from those facing customers in the savings, insurance or mortgage markets. The main risk in the credit markets rests with the lender not the consumer.

Risks to credit customers of other kinds have been comprehensively addressed (throughout the life-cycle of every loan) via the current regulatory framework, which has recently been significantly strengthened and updated under the CCD. Key elements include:

- Consumer credit advertising is extensively regulated under the CCA, the CCD, the Consumer Protection from Unfair Trading Regulations 2008, the UK Code of Non-Broadcast Advertising, the Sales Promotion and Direct Marketing (CAP) Code, the UK Code of Broadcast Advertising (BCAP Code) and the ILG. Enforcement action is also carried out by the Advertising Standards Authority and Trading Standards.
- The CCD ensures that customers receive comprehensive information before they take out an agreement. The Standard European Consumer Credit Information form covers the key features of the product and enables customers to shop around for the best deal. The new 'adequate explanation' contains key information about the type of credit being sold – including what it might not be suitable for, and what would happen if the customer had financial difficulties.
- The OFT's new ILG requirements ensure that affordability and credit-worthiness checks are undertaken so that only applicants who can afford the credit are successful.
- The Unfair Terms in Consumer Contracts legislation, together with the Unfair Relationship test, mean that consumers can challenge onerous terms in their agreements.
- As already mentioned, customers are able to complain to FOS, and all lenders are required both by OFT requirements and by the relevant industry Codes of Practice to do all they can to help customers in financial difficulties.

One of the major risks facing customers which has not so far been adequately addressed involves Claims Management Companies, which seek to prey on vulnerable consumers. Robust regulation of CMCs is essential to deal with this abuse. We therefore welcome the recent work undertaken by the Ministry of Justice looking at how matters can be improved.

As regards disproportionate, inconsistent or duplicatory regulatory burdens, Appendix A to this response includes an extract from the FLA's recent response to the Government's Call for Evidence on Consumer Credit and Personal Insolvency, which outlines our concerns about (and the need to take action on):

- The sanction of unenforceability.
- The requirement for Multiple Agreements.
- Modifying Agreements, and the way in which they can impede lenders helping customers in financial difficulties.
- The abuse of the current Voluntary Termination provisions.

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

The FLA agrees with the following objectives:

- Clarity, coherence and improved market oversight
- Effective and appropriate consumer protection, including through a responsive and flexible framework
- Simplification and deregulation
- Proportionality and cost-effectiveness. (As discussed earlier, this objective is essential, not only because of the diverse nature of the credit market but because the proposed new system seems to have been proposed mainly to ensure that there is a single regulator for retail financial services, rather than to solve any clear and serious problem with the current system. As 40% of all consumer credit lenders are sole traders, and around 80,000 lenders are currently regulated only by the OFT, the transitional costs will be large and potentially prohibitive for many market participants.)

We also propose a fifth objective of promoting competition and consumer choice.

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 single regulator and a unified regime for retail financial services could provide a single market overview, which has been more difficult under the existing regime. This would mainly help where firms are providing a broad range of retail financial products and are currently regulated by more than one body. But as noted in answer to Question 4, the

vast majority of consumer credit lenders only provide one financial service and currently deal with one regulator, so what is proposed would provide little benefit to them, while guaranteeing higher costs.

While a unified regime might deliver clarity, coherence and improved market oversight, we believe that a uniform approach to regulation (which assumes that all firms are subject to much the same rules) should *not* be the primary goal, and that very careful consideration should be given to what is genuinely appropriate and proportionate, in light of the market profile of individual lenders and the risks posed.

For example, consumer credit licences currently cover a wide range of different services such as lending, brokerage, credit hire, credit referencing, debt collection, debt advice and so on. It might therefore not be proportionate or appropriate for all these activities to be regulated in the same way - or indeed via the FCA. On the other hand, as some lenders have licences which cover not only lending but also credit brokerage, debt collection etc, any split in the regulation of these services could result in lenders still being subject to more than one regulator.

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 Illegal Money Lending Teams (some operated by local authorities) have played a central role in dealing with loan sharks and in protecting vulnerable consumers. This important work must continue. While any regulator focuses primarily on the firms which come within its remit, action must continue to be taken against unscrupulous lenders who seek to avoid regulation. Responsibility for coordinating this activity should fall to the FCA to ensure that it remains properly funded and targeted.

Trading Standards (TS) are an important aspect of consumer credit regulation and have provided the 'local face' of help with compliance, as well as enforcement action. This has been particularly helpful for smaller firms, many of whom are likely to find it daunting to deal with a single regulator based at Canary Wharf. We believe that accessible local compliance advice and enforcement should continue to be a part of the regulatory regime in light of the large number of small lenders, as long as its remit is clear and the advice provided is consistent.

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

The FLA believes that the starting point for consumer protection must be the provisions included in the CCD, as implemented in the UK through the CCA. There is a strong argument that protections which go beyond this effectively "gold plate" the CCD – for example, the sanction of unenforceability and the current system of Voluntary

Terminations. In practice, the sanction of unenforceability is used disproportionately by unscrupulous Claims Management Companies and the remedies available via the Financial Ombudsman Service and the Courts (using the Unfair Relationships Test) are flexible and wide enough to provide fair and equitable consumer redress. We have commented extensively elsewhere on Voluntary Terminations.

8. The Government would welcome further evidence relating to:

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

We estimate that around 250,000 small businesses have at least one leasing or hire purchase agreement regulated by the existing regime for equipment used for business purposes.

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

The only non-regulated groups of businesses are companies or partnerships with more than 3 partners. This leaves approximately 3.2 million UK businesses in scope out of the total population of 4.8 million.

The impact on the business lending market is in practice even more far-reaching. This is because asset finance companies cannot efficiently and practically operate one procedure for regulated agreements and another for non-regulated.

The CCA regime is not well-targeted on the business lending market, particularly as the EU's Consumer Credit Directive actually exempts business lending. The protections for customers offer little, if anything, in addition to what is already provided by the FLA's Business Finance Code.

Our business finance members have faced substantial implementation costs resulting from the CCD, involving putting in place new agreements and procedures and ensuring compliance. They are also concerned about the high cost of dealing with customers who are being advised to challenge business agreements as non-compliant because of irrelevant technicalities. Already some providers have decided to avoid offering finance to unincorporated businesses.

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

Conduct of business rules, layered on top of the existing requirements, could significantly increase the costs of lending, due both to the one-off implementation costs and the ongoing compliance burden. This would reduce competition and choice in the market. It would be much harder for small businesses to raise finance for business investment; particularly the tens of thousands of businesses that rely on help from smaller, independent finance companies. This could lead to business failures.

These costs and serious consequences would apply whether the conduct of business rules applied only to already-regulated SMEs (3.2 million) or the total population (4.8 million).

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.

One of the real benefits of the current CCA regime is certainty for both lenders and consumers. The CCA sets out very clearly what is expected of credit firms at different stages of the credit life-cycle. It is difficult to comment on how the credit industry would be affected by a rules-based regime in the abstract. Much will depend on what the rules actually look like. The closer they are aligned to those which apply under the CCA/CCD, the more limited the impact.

That said, the way in which FSA-style rules have thus far been applied to mortgages, insurance and retail deposits, gives rise to a real concern that the lack of prescription in key areas has generated confusion, leading in some cases to retrospective re-interpretation by the FSA. This approach has had significant adverse implications for both lenders and consumers.

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

The CP says that FSMA would deliver better outcomes for consumer credit customers. But, as already indicated above, there is no evidence for this. Consumer credit customers are already well protected under the current CCA/OFT regime, whereas the FSMA regime was found deficient in a number of ways during the recent economic crisis. It seems curious that an effective (if imperfect) regime is to be replaced with one which has so recently been found wanting.

It will also be important to ensure that consumer protection and competitive markets are both promoted. Consumers will not be well served if they benefit from theoretically extensive protection but are unable to obtain credit in the first place.

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

The current regime has allowed the OFT successfully to link consumer protection in the sale of goods and in the provision of credit. The FCA will need to ensure that such links are maintained in any new framework. Without a clearer understanding of where responsibility for sale of goods protection will lie in future, it is difficult to speculate about how this might be achieved.

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)?

The Government's objectives include clarity, increased market oversight, effective consumer protection, simplification, deregulation and cost-effectiveness. We have commented on these under Question 4 above. It is not clear that these objectives are likely to be better achieved under the proposed new regime.

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 already outlined what we see as the main advantages and disadvantages of transferring consumer credit regulation to the FCA. The benefits of a single regulator for a small number of large firms are obvious, although limited. But as the current regime has in no sense failed, the prospect for the rest of the market (i.e. the vast majority of lenders) is less clear. What is clear is that applying a FSMA-style regime as currently proposed could put a large number of current lenders out of business.

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?

The specific issues we believe the Government should consider are:

- A detailed Impact Assessment to identify how the size of the sector and availability of credit would be affected.
- The main differences/improvements consumers will see, and how these will compare with increases in the cost of credit – i.e. value for money.
- Whether the FCA will take on responsibility for all the services currently covered by the OFT (so as to deliver a single regulator). And if not, how will these other services be regulated?

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 believe that further thought could have been given to the scope of Option 2, and to the question of potential alternative regulators. But it could be argued that Option 2 was never going to be really viable as the demise of the OFT had been announced before the CP was published.

Consideration should nonetheless be given to an Option 3, which would see consumer credit regulation move to the FCA, but under legislation/regulation similar to that in the CCD (implemented in the UK via the CCA) and/or under a more proportionate FSMA regime which reflects the different risk profile in the credit markets. This would avoid the unintended damaging consequences for the credit markets described in this paper and allow a smoother transition of existing lending books. We would be happy to discuss this in more detail with the Government.

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.

The consumer credit industry and the businesses which operate within it are diverse. The OFT currently licenses around 100k firms, most of whom are not banks, and 40% of whom are sole traders.

The FSMA-style requirements set out in paragraph 3.6 of the CP include new rules covering (for example) authorisation, reporting, prudential provisioning, enforcement sanctions and so on. If all consumer credit firms move within the remit of the FCA, very different regulatory requirements will in practice be required across the market, taking account of the different services offered, the size of the organisations concerned and the risks posed to consumers. The CP says that the FSA has experience of dealing with smaller firms via the 500 authorised credit unions. But the scale of the task facing the FCA if consumer credit transfers to it will be very much greater, as over 80,000 firms might require authorisation. It is also worth observing that the credit union sector contracted by 37% following the introduction of FSA regulation, the main reason being that smaller unions could not cope with the sheer scale of the new regulatory requirements. This illustrates our concerns.

Three aspects of the current FSMA regime give rise to particular concerns, including the proposed new capital requirements, the Approved Persons regime and the idea of Appointed Representatives. We do not believe that consumer credit firms should be subject to capital requirements because there is no risk to the customer. Lenders would effectively be left holding capital against a risk which will not materialise, and which would restrict their lending capacity. (Increased capital requirements in the mortgage market have resulted in customers finding it harder to get mortgages, because lenders have had to restrict whom they lend to, as well as having less to lend.)

The Approved Persons Regime is onerous, and some existing FSA-authorised firms have struggled to recruit staff willing to be subject to the direct responsibility and liability which is involved. It is not clear what benefit the extension of such a regime to the consumer credit markets would bring. A much smaller market would be the likely result.

As regards the Appointed Representative Regime, lenders are unlikely to be prepared (or able) to take on responsibility for credit brokers and/or credit intermediaries, as was seen when the regulation of insurance intermediaries was introduced in 2005 (see also

below under Question 19) Given the highly intermediated nature of the credit markets in the UK, the introduction of such a regime would have a very serious adverse effect.

As already indicated, not only would each of these measures have an adverse effect on its own, the cumulative effect would mean that many small and medium-sized credit firms would simply not have the resources to continue in the markets.

We look forward to working with the Government and the FSA on a more proportionate regime for consumer credit, which takes better account of the diversity of lenders and lending in the UK markets.

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?

In developing a proportionate regime, we agree that a risk-based approach to regulation and setting fees will be essential.

With regard to the ‘statutory processes relating to rule making’, we welcome the prospect of detailed consultation with both industry and other interest groups as the regulatory framework develops. But as the financial services sector plays such an important role in the overall economy, we believe that Parliament should also be able to scrutinise and comment on regulatory change in financial services. Without this, the industry will not be able to challenge the regulator without taking legal action via Judicial Review, which is lengthy, expensive and potentially very disruptive for both the industry and the regulator.

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

The CP makes clear that fee levels will definitely increase as a result of the proposed new regime. This will be exacerbated by the additional costs associated with, for example, the new Money Advice Service, and must raise a further question about the new regime. Fees should recognise not only the size of a firm but also how much time the FCA is likely to spend supervising it. Firms will need sufficient advance warning of fee increases so they can prepare accordingly. Higher fees themselves are likely to drive some credit firms from the market.

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.

Many credit firms do not have direct experience of the Appointed Representative regime. When insurance regulation was transferred to the FSA in 2005, credit firms

decided not to take responsibility for the conduct of representatives providing insurance on their behalf and instead required the representative to be directly authorised.

This position has not changed. Lenders would not be prepared to take responsibility for other parties when providing credit. This will have important implications in the retail credit market (for example) where credit is made available via thousands of different retail outlets. A very similar set of issues arises in the motor finance market. Intermediated credit accounts for half of all the new car sales in the UK, and would be put at risk by this type of regime. We would welcome early discussions to ensure a more workable approach.

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.

FLA members are not subject to Group licensing.

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

The FLA Lending Code has been in place for over 18 years and is well-respected by both the OFT and FOS. It includes standards over and above those set out in legislation and has recently been used several times as a channel to introduce new regulatory requirements more quickly and efficiently than via statutory regulation.

We would hope and expect that Codes would remain an important feature of any new regime (although the detailed balance between statutory and non-statutory regulation can only be decided at a later stage in the process) and that the contents – e.g. of the FLA Lending Code – could be a useful starting point for the design of the new regime.

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

We believe that a detailed risk assessment should be undertaken of the different categories of consumer credit (including taking account of what is currently excluded from the CCD) as a basis for further discussion of areas for deregulation. This would help ensure the adoption of a proportionate approach.

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?

The main factors which should influence the scope of any new regulatory system are:

- Risk
- Proportionality

- Relevance
- Cost to firms
- Market impact

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

Applying a new regulatory regime retrospectively, as suggested, would be a significant departure from recent practice and quite different from the approach adopted when other areas of financial services markets have moved within the FSA's remit. It will certainly considerably increase the scale and complexity of the proposed transfer.

The problem would be eased somewhat if the eventual new regime were less dramatically different from the current CCD/CCA framework than currently proposed. But careful thought would still be needed as to whether different arrangements should be applied to lenders who have stopped lending (and are now effectively managing down their lending books) and lenders who are still lending and may want to bring all of their agreements (both new and old) under the new regime. Some lenders who have stopped lending may also have offered fixed-rate products and so would be unable to recoup any of the additional regulatory costs which subsequently arise.

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.**

This question can only be fully answered when it is clear whether the regulation of all current consumer credit services will transfer to the FCA. Consideration must also be given to what happens to the customers of firms who decide not to become authorised in the future, or who fail the authorisation process.

Elements for further work might include:

- An expedited form of authorisation process which recognises the potential volume (over 80,000 firms) and the fact that they already have consumer credit licences. It might also be possible to follow an initial streamlined process with a more detailed second phase for certain firms, while avoiding any hiatus in lending.
- A staged implementation process so lenders do not face a 'big bang' including all the new layers of regulation.
- A sensible implementation period. 12 months to introduce the new requirements falls a long way short of what will be needed for system changes and staff training in respect of such a radically different regime.

See also the points raised under Question 5 regarding lenders with licences covering several different activities.

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

Much will depend on how much fees rise under the new structure (see also comments under Question 18 above). Firms will need time to make provision for the change, especially as this will be only one aspect of the materially increased costs of the new regime. An incremental approach to fee increases over time might help a little.

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

The proposed new regime will affect every aspect of consumer credit lending from the requirements governing how credit is provided to how lending firms are managed. A staged implementation process over several years may be required, especially in light of the large number of firms involved.

We would urge the Government to consider the transitional arrangements at an early stage, so all the implications can be assessed.

One approach might be to focus initially on the lending requirements themselves, to ensure that consumer credit lending is not adversely affected during the transitional period. Other completely new aspects of regulation could be introduced later.

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.

In all sectors which have so far moved into the FSA's jurisdiction, the number of firms operating in those markets has dropped, mainly because smaller firms have struggled with the sheer scale of regulation. Some examples have already been quoted. This has reduced consumer choice and left markets with a smaller number of larger participants, who have the resources to manage expensive new compliance requirements. But the results would be even worse for consumer credit, which is unlike the other markets which have so far moved to FSA regulation. Over 100,000 firms are currently licensed to provide credit, 40% of which are sole traders. The existing comprehensive regulatory regime has only just been updated. And the new regime will be applied retrospectively. Without significant change in what is proposed, we could face a bigger contraction in the consumer credit markets than any in recent memory.

FLA

March 2011

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Appendix A

Extract from the FLA's response to the Government's Call for Evidence on Consumer Credit and Personal Insolvency

Q7: Which of these stakeholder proposals do you consider would bring benefits to industry or consumers and what would these be? Please provide evidence in support of your view.

1. The short timeframe for implementing the CCD meant that there was insufficient time to undertake a root-and-branch review of the CCA to ensure that any existing provisions did not compromise the maximum harmonisation status of the Directive. We therefore welcome a review of certain aspects of the CCA. This should be aimed at complying with maximum harmonisation and with the Government's deregulation objectives. While over 20 such issues are listed in Annex A to the CfE, this response focuses on four areas where we believe the Government should in particular be taking action. (Annex A also mentions Charging Orders. We have included our comments on this issue in answer to Question 14.)

Replace any remaining areas of automatic unenforceability of credit agreements with unenforceability without a court order or another appropriate penalty.

2. We strongly support the withdrawal of the sanction of automatic unenforceability for pre-April 2007 agreements. This is a draconian enforcement measure which is not replicated in other parts of the financial services market. It also fuels extensive action by Claims Management Companies (CMCs) who seek to game the situation and mislead customers that their agreements can always be avoided. This fails to provide a level playing-field for the provision of financial services. Its replacement with unenforceability without a court order is a sensible move which would not adversely affect consumers, while putting an end to the spurious actions brought by CMCs. We believe that automatic unenforceability where there is an error on a statement or a Notice of Sums in Arrears should also be withdrawn and replaced with unenforceability without a court order. Existing provisions on Unfair Relationships in the CCA already provide consumers with wide legislative protection if something the creditor does or does not do causes consumer detriment.

Rationalise/repeal section 18 of the CCA setting out the requirements which apply to multiple agreements.

3. We support the repeal of section 18 of the CCA on the basis that multiple agreements are not included in the CCD and therefore their continued existence

contravenes the principle of maximum harmonisation. Section 18 and the concept of multiple agreements were introduced when the original CCA limit was £5k. The idea was to stop lenders avoiding the legislative requirements by documenting two loans (for example for £4k and £3k) as one unregulated loan for £7k. The provision was maintained when the limit was increased to £25k. Now that the limit for personal lending has been removed altogether, the section 18 provisions are no longer required as all lending must now be compliant. Section 18 should be removed as a natural consequence of removing the limit.

4. Recent case law has also demonstrated how complicated the section 18 provisions are. In *SPML v Heath* [2009], the Court of Appeal criticised the fact that even the original draftsman of the section could not properly interpret it. It is a moribund provision which should be removed as part of the Government's commitment to deregulation.

Repeal or rationalise the CCA provisions which apply to modifying agreements.

5. We strongly support the repeal of section 82 of the CCA and especially where the customer is experiencing financial difficulties. For those agreements to which the CCD applies (unsecured agreements), we are concerned that as Modifying Agreements (MA) are also not covered in the CCD the 2010 Regulations go beyond the requirements of the CCD.
6. Under Section 82 of the Consumer Credit Act 1974, an MA is required where a lender and the borrower agree to vary or supplement the terms of an existing agreement. The MA for the purposes of the CCA is treated as if it revokes (even if it may not in reality) the earlier agreement, leaving one agreement reproducing the combined effect of both. It must comply with documentation requirements and be properly executed. Failure to comply would leave the agreement unenforceable without a court order.
7. A MA is currently required unless the lender is providing only temporary forbearance such as repayment of the arrears over a short period, or the credit agreement already contains powers to vary the terms in certain circumstances.
8. In seeking this reform, lenders are not looking to dilute consumer protection, but rather to improve their ability to offer more long-term solutions to customers experiencing hardship without the constraints of complex processes and documentation which can make it impracticable, coupled with the prospect of unenforceability claims. We accept that BIS and the OFT want to ensure that some controls are in place to protect against any relaxation of the requirements

and the FLA would welcome the opportunity to take part in discussions on this point.

9. To put the issue in context, some of the key requirements of an MA include:

- Compliance with prescriptive documentation and process requirements.
- Borrower consent.
- An adequate explanation of the new credit arrangement.
- A formal assessment of affordability.
- Documentation requirements

10. The Encyclopaedia of Consumer Credit Law states: *“The regulations are so complex that modifying agreements are, if possible, to be avoided”*.

11. In addition to the requirements listed above, Schedule 8 of the Consumer Credit Agreement Regulations 1983 that will continue to apply to certain agreements post the CCD implementation date including agreements secured on land prescribes further provisions for MAs:

- A statement (paragraph 5) of the total amount of credit to be provided under the modified agreement, calculated in a manner stated which involves computation of the amount of capital outstanding under the earlier agreement and the future charges less the rebate as if the loan was being settled early.
- The Total Charge for Credit must be recalculated (Paragraph 8).
- The APR (paragraphs 14, 15 and 16) in relation to the modified agreement, ie what has been paid so far and what is expected to be paid under the MA.
- Three early settlement examples (paragraph 24), looking at what happens if a customer settles early at any of the quarter, half or three quarter points in the term (or modified term).
- Following the ‘consideration period’ process requirements that mirror those for new lending.

12. In practice, some of these requirements have little relevance to customers in financial difficulties as it is rare for them to be in a position to pay off and settle the credit agreement early. This results in unnecessary information overload, at a time when all customers want is information which will help them take control of their debt situation.

13. Lenders want to do all they can to help customers with debt problems and to deliver flexible forbearance tools. Removing the MA provisions in the CCA will allow lenders to take a longer-term approach to assisting customers and bring the UK legislation in line with the CCD.

Review the need for sections 99 and 100 concerning Voluntary Terminations

14. Hire purchase and conditional sale agreements are subject to the Voluntary Termination (VT) provisions which allow customers who have taken out a regulated agreement to terminate it at any point in time and be liable for only half of the total amount that is owed to the finance company. If a customer exercises their right to VT then they must hand back the associated asset that has been financed, for example, a car.
15. The VT provisions were originally introduced in the 1930s as a form of consumer protection for those in financial difficulty. Since then, consumer protection regulation has dramatically improved but the out-dated VT provisions remain, and the cost to industry is significant. In 2009, the number of VT cases amongst motor finance providers increased by 28% to almost 40,000 cases. Total annual VT losses were almost £51 million in 2009, up from £48 million in 2008. The costs incurred by lenders – who have to recover and resell vehicles – increases the cost of credit for consumers generally.
16. We strongly support the repeal of sections 99 and 100 of the CCA dealing with VTs as they are a significant and unnecessary burden on business, and borrowers are protected by modern consumer credit regulation.
17. VTs have long been superseded by new and improved consumer protection rules including changes under the CCA and, more recently, the new Right of Withdrawal and Right of Early Repayment under the CCD. Legal advice sought by the FLA from senior counsel concluded that VTs were incompatible the CCD as a maximum harmonisation Directive. Appendix A to this response includes correspondence sent to the previous Government on this issue in July 2009.
18. The repeal of the VT provisions would reduce significant industry losses and therefore improve the availability of credit to consumers in what is an otherwise narrowing consumer credit market in difficult economic conditions.
19. The VT provisions are not used by customers in financial difficulty but are instead widely abused to avoid full payment of credit obligations. Independent research published by Oxera in 2004 found that only 10% of customers who VT'd were in

arrears. The remaining 90% of customers had not missed a repayment and were not in any financial difficulty. Feedback from finance companies confirms that the misuse of these provisions remains at the same high level with many customers simply wanting to escape their financial commitment.

20. The previous Government decided to retain the VT provisions in UK law and we would urge the Coalition Government to reconsider this position on both legal and policy grounds.



The Financial Inclusion Centre

Promoting fair, inclusive
financial services

HM TREASURY/ DEPARTMENT FOR BUSINESS INNOVATION & SKILLS (BIS)

A NEW APPROACH TO FINANCIAL REGULATION: CONSULTATION ON REFORMING THE CONSUMER CREDIT REGIME

SUBMISSION BY THE FINANCIAL INCLUSION CENTRE

INTRODUCTION

The Financial Inclusion Centre (The Centre) is a not-for-profit think tank dedicated to promoting fair, inclusive, efficient, and accountable financial services (see www.inclusioncentre.org.uk). The Centre is pleased to have this opportunity to make a submission to this important HMT/ BIS joint consultation on reforming the UK's consumer credit regime. The interests of mainstream consumer credit will be represented by other consumer organisations. Financially vulnerable consumers are our priority.

Our submission is in two parts. We have provided responses to the specific questions contained in the consultation document. However, we would ask that these questions be read in the context of the series of recommendations in Annex 1 which outline a different **approach** to consumer credit regulation to protect the interests of financially vulnerable consumers. Further details can be found in our Financial Inclusion Manifesto¹.

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For information on The Centre's work please see:

www.inclusioncentre.org.uk or contact info@inclusioncentre.org.uk

¹ See http://inclusioncentre.org.uk/doc/financial_inclusion_manifesto_full_report.pdf

THE NEED FOR REFORM

We recognise the important role consumer credit plays in the lives of consumers and the wider economy, so our response is not intended to be an attack on consumer credit provision per se. However, we would argue that the consumer lending sector is one of the biggest sources of continuing consumer detriment in financial services which needs to be addressed by regulatory reform.

At the macro-level, the UK's relatively permissive consumer credit regime has facilitated overconsumption of credit (secured and unsecured), allowing lenders and intermediaries to aggressively and, some would say, recklessly sell consumer credit.

This default position on the supply of consumer credit has left us with a legacy of overindebtedness which needs to be unwound. But it also has wider consequences such as affecting household living standards and ability to save, build up a pension, afford insurance and so on. Selling easy access credit – which turns into debt that has to be repaid after all – must undermine ability of many households to put money aside to build assets for the future.

The default position on consumer protection has also been too permissive. Consumer credit regulation has allowed providers to operate more or less freely with the presumption that 'innovation' or choice in consumer credit markets – even in the non-mainstream or sub prime sector – delivers positive outcomes for financially excluded consumers. Regulators have adopted a sceptical approach to the need for regulatory interventions – ie. intervening only when there is overwhelming evidence that markets are failing and there is a need to protect consumers, or when forced to by public opinion. When interventions have occurred these have tended to rely on classical interventions such as addressing information asymmetries with little effect on firm or consumer behaviour.

The result of this permissive regime has been serious consumer detriment in the non-mainstream consumer credit sectors - for example, the behaviour of high cost sub-prime lenders, commercial debt management firms, sale and rent back providers, and distressed debt sales. Moreover, new detrimental practices seem to be continually emerging as non-mainstream financial firms respond to 'opportunities' provided by overindebtedness and the ongoing financial crisis.

So, we warmly welcome the Government's views that the current consumer credit regime is in need of reform and strongly support the Government's preferred option set out in the consultation document – Option 1.

We are confident that the proposed new regulatory regime set out in the consultation paper will be a significant improvement on the existing regulatory regime. However, there are two main transitional risks to be addressed.

Firstly, it is important that the transition program does not distract from regulation and supervision of the existing consumer credit markets. We are entering a period of considerable economic uncertainty for many vulnerable low income/ overindebted households who are at risk of being targeted by sub-prime market providers (sub-prime lenders, commercial debt management firms, and so on) adopting aggressive market behaviours and practices. Existing consumer credit regulation

has not been particularly effective at protecting the interests of financially vulnerable/ excluded consumers. But it is important that this is not undermined further during the transition period.

Secondly, linked to this, we are concerned that less scrupulous providers will seek to aggressively expand market share under the current regime in the run up to the introduction of the new regulatory regime.

These risks will require careful oversight and management. But, we assume the Government is alert to these risks. Moreover, it is important to emphasise that these risks are far outweighed in our view by the benefits a coherent, more robust regulatory regime would deliver.

This is an ideal opportunity to make markets work for financially vulnerable consumers and provide them with a similar degree of consumer protection as that available to better-off, more financially capable consumers.

Financially vulnerable consumers receive ineffective protection from the existing financial regulatory system. First of all, they are less likely to get fair access to markets in the first place. Once in the market they are more likely to be sold inferior or downright risky products (sub-prime loans for example), they pay a higher price for products, get poorer quality service, and are more likely to suffer disproportionate consumer detriment if they are ripped off (any financial loss has a greater impact on someone on a low income).

However, it doesn't end there. When trying to resolve a problem they are more likely to encounter detriment. For example, overindebted consumers are increasingly exposed to commercial debt management firms and/ or sub prime lenders. Moreover, they are less likely to be aware of their rights to redress and exercise those rights.

Overall, the consumer protection regime which governs the sale of products that financially excluded consumers use (sub-prime/ door step lenders/ debt management companies etc) is less robust than the FSA's conduct of business and authorisation rules which govern the sale of mainstream market products.

In other words, we would argue that the UK's financial regulation system offers greater consumer protection for 'Middle England', not the most vulnerable groups in society who don't have the voice or financial clout to make markets and media sit up and take notice.

Protecting financially vulnerable consumers requires a more fundamental rethink of the role of consumer credit markets and a radically different **approach** to regulation of practices and behaviours in those markets. There is no meaningful evidence produced by any of the recent reviews of the high cost/ sub-prime market that suggests that normal competitive market forces or interventions such as information solutions are effective at controlling the behaviours or aggressive lenders or protecting the interests of vulnerable consumers.

The level of detriment particularly in the sub-prime lending, commercial debt management and debt resolution sectors requires a 'zero-tolerance' approach to market structures, business models,

distribution strategies, product 'innovation', and market practices that are detrimental to the interests of financially vulnerable consumers.

A new, proactive approach to consumer protection is needed including a range of robust regulatory interventions to deal with the obvious detrimental behaviours in the consumer credit markets generally but especially in the high cost/ sub-prime credit market.

The objective of these interventions should be to:

- achieve a rebalancing between savings and borrowing by changing the default position to make it more difficult for lenders to aggressively 'sell' discretionary credit and discourage unnecessary borrowing²
- restrict the opportunities for vulnerable consumers to be exposed to high cost/ sub-prime lenders in the first place;
- protect vulnerable consumers from unfair practices if they have genuinely no option but to use high cost/ sub-prime lenders; and
- protect vulnerable consumers from unfair practices if they get into financial difficulty.

The more robust approach to prudential regulation being adopted by the FSA should ensure that lenders lend more prudently. However, this needs to be complemented by some additional measures.

Perhaps the most important measure for protecting vulnerable consumers is to curtail the business model of high cost lenders by capping of charges (the argument for this is set out in Annex 1). However, capping charges is not the subject of this consultation document so we restrict our recommendations here to measures designed to i) promote a fair, accessible, and sustainable consumer credit sector, and ii) protect consumers during the transition process:

- the new FCA should become the single regulator for all secured and unsecured lending and lenders;
- consumer credit providers should be subject to a full authorisation process similar to that operated by the FSA rather than the current licensing process. This authorisation process should cover fitness and competence of firms and individuals. This should apply to originators of loans and secondary providers of services such as debt management companies and buyers of distressed debt;
- all consumer credit providers (secured and unsecured) should be subject to robust conduct of business regulations relating to marketing, promotions and advertising (including at the point of sale), and conflicts of interest (eg. DMP providers paying fees to introducers);

² NB: we are not against access to credit – indeed we count access to fair and affordable credit to smooth out peaks and troughs of income as one of the core financial needs. However, we think this is very different to discretionary 'lifestyle' credit which has been sold far too aggressively)

- authorisation and conduct of business rules must be toughened and aggressively enforced to ensure higher standards of behaviour more robust policy measures should be supervised and enforced
- a new risk based approach to regulating consumer credit products should be adopted. That is, products and services aimed at specific consumer sectors or involving new practices should be subject to a *pre-approval* process. New products and services should be submitted to regulators for assessment to identify potential detriment and develop appropriate regulatory response. In practice, this would mean that 'innovations' such as payday loans, or commercial debt management plans would be assessed for potential detriment in advance rather than allow detriment to emerge before action is taken by regulators;
- to protect consumers during the transition process, the FSA, OFT, Financial Ombudsman Service (FOS), and trade bodies such as the BBA, ABI, CML, FLA³, and Lending Standards Board should work with consumer organisations to producing new guidance and statements of best practice in retail financial services aimed at firms and consumers. These best practice statements would be suitable for all major financial product sectors. However, transactional banking, mortgage and credit products and practices are a priority given the potential for detriment in the wake of the financial crisis.

³ Financial Ombudsman Service, British Bankers Association, Association of British Insurers, Council of Mortgage Lenders, Finance and Leasing Association

Chapter 1

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

We agree in large parts with the description of the consumer credit market set out in the consultation paper. However, we would emphasise that we do not consider the growth in credit, the apparent 'diversity' and choice, or innovation in UK consumer credit markets to be particularly positive for consumers.

Our view is the relatively liberal, permissive approach to consumer credit regulation has encouraged oversupply and overconsumption of consumer credit at the aggregate level and has allowed significant consumer detriment to occur within the sub-prime sector. This 'default' position should be replaced with a new risk based interventionist approach and pre-approval process designed to prevent detriment occurring in the first place.

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 strongly agree that the current system of consumer credit regulation is unsatisfactory, and support the establishment of a unified consumer credit regime. However, as we set out above (and in Annex 1), the approach also needs to change with the default permissive regulatory approach replaced with a more prescriptive, preventative approach.

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

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

Please see Annex 1 for a description of the consumer detriment faced by consumers in these markets and assessment of the effectiveness of current regulation.

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

We support in general the policy objectives set out in para 1.18 and as mentioned elsewhere we believe the new regulatory architecture would deliver significant benefits for consumers by bringing unsecured consumer credit within the FSMA/ FCA regime.

Although there are a number of potential risks associated with merging the two regimes, we are confident that the benefits far outweigh any risks and these policy objectives are attainable.

However, changing the regulatory architecture in and of itself will not deliver a regulatory regime that protects vulnerable consumers. A more interventionist, prescriptive approach to consumer credit regulation is also required.

This policy of more intrusive regulation, including early intervention in the early stages of product development lifecycle, is currently central to the Government and FSA plans for regulating retail financial services.

We would urge the Government to read across this approach to the regulation of consumer credit. As we point out, consumers of non-mainstream consumer credit products and services are particularly vulnerable and deserve an equivalent level of consumer protection.

Chapter 2

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

We agree that a unified regime would deliver greater clarity, coherence, and market oversight of the totality of consumer credit markets.

Whilst the bulk of total consumer credit outstanding in the UK relates to secured credit, having a deeper understanding of unsecured credit on consumer behaviour would help policymakers make better macro-prudential regulatory interventions.

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

As the consultation document sets out, the OFT regulates 96,000 firms – 16,000 are also authorised by FSA for FSMA regulated activities. In theory, a unified regime therefore could include an additional net 80,000 firms within a FSMA regime.

Of course, in practice, it is to be expected that many of these OFT firms would choose not to migrate to the FSMA/ FCA regime due to more robust regulation (which could prove positive for consumers as oversupply in financial markets causes as much detriment as overconcentration of providers). However, it suggests that the FCA would still have to cope with tens of thousands of additional firms on top of the existing 28,000 firms the FSA regulates.

This does not negate the arguments for unifying regulation. However, the increase in firms that would come under the FSMA regime has to be managed. One possible way of doing this would be to allow FCA to have overall responsibility for policymaking, supervision, and enforcement but to allow Trading Standards to undertake day to day monitoring of activities. This would be an appropriate use of Trading Standards local presence and local market knowledge.

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.

While we fully agree that the FSMA/ FCA regime offers considerably better consumer protection compared to the CCA/ OFT regime, there are certain features of the CCA which offer additional protection for consumers – namely, the ability to challenge credit agreements in court on grounds of

unfairness to the debtor, court discretion on enforcement of improperly executed agreements, and provisions for joint liability of creditors for certain breaches by suppliers of goods and services.

We believe these elements of the current regime should be retained. So in effect, we would support an amended Option 1.

8. The Government would welcome further evidence relating to:

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

No comment

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 agree with the arguments set out in paras 2.13 – 2.16 in the consultation document that the flexibility of a FSMA style regime would provide significant benefit for consumers. As the Government points out a rules based regime can be much more responsive than a legislative approach.

Of course, this very much depends on the powers, duties, and importantly culture and approach of the FCA.

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 a FSMA/ FSA style supervisory approach provides a much better approach for ensuring effective and appropriate consumer protection. As we highlight elsewhere, this is not just in terms of supervision but applies to the entire regulatory ‘supply chain’ - policy formulation, policy implementation, authorisation, supervision, enforcement, and resolution (complaints and redress).

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 think this an important issue – but not for the reasons set out by the Government in paras 2.19 – 2.21.

We support the retention of provisions for joint liability of creditors for certain breaches by suppliers of goods and services. This indeed is one area where the current regime offers synergies.

However, some of the other ‘synergies’ in the current regime far from providing benefits to consumers actually result in major consumer detriment. The fact that consumers may regard consumer credit and buying goods and services as a single transaction is not a positive dynamic. The provision of credit at the point of sale exploits behavioural vulnerabilities – for example, the aggressive selling of store card credit.

Therefore, we would argue that a new consumer credit regime should try to detach as far as possible the provision of credit from the sale of the good/ service. This could be done through better targeting of methods such as linking shop staff remuneration to the sale of store cards, and improved disclosure of risks and costs of credit. This would be consistent with the approach followed by the FSA in tackling conflicts of interest in the retail investment markets.

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

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

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

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

We strongly support the view 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.

In theory, consumer protection in consumer credit markets could be improved by raising the OFT regime to the level of FSMA/ FSA regime. However, this would probably involve a similar level of legislative and regulatory reform without gaining the advantages provided by a full FSMA/ FSA regime. We would be left with the same duplication and overlaps evident in the current set up.

We also believe that a unified regime would deliver additional regulatory benefits – not just within the consumer credit sector. Effective policymaking and regulation depends on policymakers being able to take a 'holistic' view of consumer and provider behaviour across the full spectrum of financial services. For example, we believe it is self-evident that the liberal, permissive approach to consumer credit regulation followed in the UK over the past two decades has contributed to the low level of savings/ pension provision in the UK. In plain terms, the different approaches to regulation meant that it became too easy to borrow and too difficult to save. The balance of regulation must be improved and a unified regulator makes that balance easier to strike.

Chapter 3

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

We have set out elsewhere the key principles for a new approach to consumer credit regulation. However, we would like to emphasise the need to apply FSMA/ FCA standards of approvals and authorisations for individuals working in commercial consumer credit firms. The FSA requires approval of senior management and individuals working in customer facing roles.

This is a key requirement and means that individuals can be fined, suspended or banned from financial services.

It is critical, given the behaviours in the consumer credit sector, that this approach should apply to consumer credit firms under the new regime.

However, we would argue that it is justified and necessary to differentiate between commercial consumer credit providers/ service providers and debt advice charities. Commercial firms have inherent conflicts of interests which justify regulation to control behaviours that may damage consumer interests.

These conflicts of interest do not exist in charitable organisations. Therefore, such an intervention is not required. More importantly, applying a full FSMA / FSA consumer credit regime to debt advice charities would be far too burdensome for these organisations and would seriously limit their ability to function with severe adverse consequences for vulnerable consumers who rely on the services provided by debt advice charities.

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

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

We agree that a risk based approach to regulation and differentiated fee-raising arrangements is appropriate.

However, it is important that the risk based model is based not just on the size of the firm but on the risks the particular business model poses to consumers and the level of regulatory scrutiny and resource required to supervise these firms. In practice, this means that the fee levied should take into account:

- conflicts of interest (such as the use of commission/ sales targets);
- vulnerabilities of consumers in the firms target market; and
- the business model itself including pricing and fee structures.

We are not at all concerned that an increase in regulation would result in many commercial consumer credit providers exiting the market. This would not be a bad outcome for vulnerable consumers. As we explain elsewhere, the classical model of economics – which holds that the greater supply and ‘choice’ of products and providers leads to enhanced consumer welfare – does not work in complex markets such as consumer credit where consumers are particularly vulnerable to aggressive selling practices.

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

No comment

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

We have no real experience of the group licensing regime. However, we would very much support the view that some form of existing group licensing regime for charities such as Citizens Advice and Consumer Credit Counselling Service (CCCS) should be carried over to a new FSMA/ FCA regime.

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.

History suggests that self regulation has not been very effective in retail financial services. However, there may well be an opportunity for self-regulation to build on the foundation provided by tough statutory regulation.

More importantly, to protect consumers during the transition process, the FSA, OFT, Financial Ombudsman Service (FOS), and trade bodies such as the BBA, ABI, CML, FLA⁴, and Lending Standards Board should work with consumer organisations to producing new guidance and statements of best practice in retail financial services aimed at firms and consumers.

These best practice statements would be suitable for all major financial product sectors. However, transactional banking, mortgage and credit products and practices are a priority given the potential for detriment in the wake of the financial crisis.

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. The sub-prime consumer credit sector has a track record of 'innovating' to evade regulation or push the boundaries of regulation.

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?

See above, page 5, for principles of an effective consumer credit regulatory regime.

⁴ Financial Ombudsman Service, British Bankers Association, Association of British Insurers, Council of Mortgage Lenders, Finance and Leasing Association

Chapter 4

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

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.**

It is difficult to provide a complete answer to this question without availability of detailed cost benefit analysis.

As a matter of principle and in we strongly believe that the more robust consumer protection measures under the FSMA/ FSA regime should be applied to existing licensed firms, not just new potential licensees.

There are two main reasons to support our belief:

- the need to protect the interests of financially vulnerable consumers in the credit markets; and
- the reputation of the Financial Conduct Authority (FCA)

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

No comment.

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

We are confident that the proposed new regulatory regime set out in the consultation paper will be a significant improvement on the existing regulatory regime. However, there are two main transitional risks to be addressed.

Firstly, it is important that the transition program does not distract from regulation and supervision of the existing consumer credit markets. We are entering a period of considerable economic uncertainty for many vulnerable low income/ overindebted households who are at risk of being targeted by sub-prime market providers (sub-prime lenders, commercial debt management firms, and so on) adopting aggressive market behaviours and practices. Existing consumer credit regulation has not been particularly effective at protecting the interests of financially vulnerable/ excluded consumers. But it is important that this is not undermined further during the transition period.

Secondly, linked to this, we are concerned that less scrupulous providers will seek to aggressively expand market share under the current regime in the run up to the introduction of the new regulatory regime.

These risks will require careful oversight and management. But, we assume the Government is alert to these risks. Moreover, it is important to emphasise that these risks are far outweighed in our view by the benefits a coherent, more robust regulatory regime would deliver.

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

No comment.

This marks the end of The Financial Inclusion Centre response

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ANNEX 1: A NEW REGULATORY APPROACH

Major regulatory reforms are needed to protect the interests of financially vulnerable consumers.

Financially vulnerable consumers receive ineffective protection from the existing financial regulatory system. First of all, they are less likely to get fair access to markets in the first place. Once in the market they are more likely to be sold inferior or downright risky products (sub-prime loans for example), they pay a higher price for products, get poorer quality service, and are more likely to suffer disproportionate consumer detriment if they are ripped off (any financial loss has a greater impact on someone on a low income).

However, it doesn't end there. They are less likely to be aware of their rights to redress and exercise those rights. Moreover, the consumer protection regime which governs the sale of products that financially excluded consumers use (sub-prime/ door step lenders/ debt management companies etc) is less robust than the FSA's conduct of business and authorisation rules which govern the sale of mainstream market products.

In other words, the UK's financial regulation system primarily protects the interests of Middle England, not the most vulnerable groups in society who don't have the voice or financial clout to make markets and media sit up and take notice.

STRUCTURAL REFORM

The current reforms to the UK's financial regulatory architecture represent a once in a generation opportunity to put the interests of financially vulnerable consumers on a par with more fortunate consumers and to bring greater coherence and consistency to the UK's consumer protection regime relating to consumer credit. The Financial Services Authority (FSA) is being split with the prudential regulation of financial firms going to a new body, The Prudential Regulatory Authority (PRA), based at the Bank of England. The PRA's job will be to ensure that financial institutions are financially sound and prudently managed.

The Government also plans to create a new dedicated Financial Conduct Authority (FCA). We very much support the creation of a dedicated FCA as it gives a better focus on consumer protection. However, it is critical that the FCA looks after the interests of all consumers especially financially excluded groups.

So, we are campaigning for the new FCA to be required to protect financially excluded consumers. We argue the FCA should have four balancing objectives derived from long established consumer principles:

- protecting consumers from unfair market practices;
- promoting efficient, competitive markets;
- promoting financial inclusion and provision; and
- promoting financial capability (with the Consumer Finance Education Body CFEB).

NEW REGULATORY APPROACH

However, reform of the regulatory architecture is not sufficient. A new, proactive approach to consumer protection is needed including a **range** of robust regulatory interventions to deal with the obvious detrimental behaviours in the high cost/ sub-prime credit market (these are set out in more detail see below).

The objective of these interventions should be to:

- restrict the opportunities for vulnerable consumers to be exposed to high cost/ sub-prime lenders in the first place;
- protect vulnerable consumers from unfair practices if they have genuinely no option but to use high cost/ sub-prime lenders; and
- protect vulnerable consumers from unfair practices if they get into financial difficulty.

There is no meaningful evidence produced by any of the recent reviews of the high cost/ sub-prime market that suggests that normal competitive market forces or interventions such as information solutions are effective at controlling the behaviours or aggressive lenders or protecting the interests of vulnerable consumers.

The scale of consumer detriment in this sector is such that the overall objective of any new regulation should be to change the default position from the current position where lenders have significant freedom to aggressively sell high cost credit to the detriment of vulnerable consumers to a position where the opportunities for selling high cost credit are restricted. In other words, we should aim to get to a position where credit is actively and consciously bought in a controlled environment rather than aggressively sold in a relatively lightly regulated market.

This requires a range of actions on the part of regulators. Perhaps most importantly, the business model of high cost lenders must be curtailed through capping of charges and the authorisation and conduct of business rules must be toughened and aggressively enforced to ensure higher standards of behaviour.

SPECIFIC REGULATORY INTERVENTIONS

Capping charges on loans

One of the most obvious consumer detriments faced by vulnerable consumers is the exorbitant charges they pay on legal sub-prime loans of various types.

The APR on a one year £1,000 loan from a mainstream lender ranges from around 8%-19%, while a consumer borrowing from a home-credit company s/he can expect to be charged 122%-325% APR. Moreover, research has found that if borrowers need small, short term loans the APR charged by home credit companies on a £100 loan over 3 months can range from 600% APR to over 1,000%

APR⁵. Similarly, the typical APR for borrowing £100 for one month from a payday lender is 1,290%⁶. By comparison, a typical credit union loan would cost roughly 22% APR⁷.

Lenders complain that the APR method of comparing the cost of short term loans can make sub-prime/ doorstep credit seem exorbitant. However, many consumers will be stuck in a cycle of revolving credit and as a result the actual cost of credit will be extremely high and the APR is a reasonable reflection of the comparative cost of credit.

However, things can be even worse for consumers who are forced to borrow from unlicensed lenders or loan sharks. According to the Government, a loan from a loan shark is on average three times the cost of the same loan from a legal lender, and that interest rates of between 8000% and 117,000% have been uncovered⁸.

Illegal lenders by definition operate outside of the regulatory system, so the only way to tackle these people is through legal interventions and prosecution, and by raising awareness amongst target groups of the risks involved with illegal lenders.

However, that still leaves the issue of what to do with hugely expensive yet legal lenders. One way of dealing with the high cost of unsecured loans would be for government or regulators to cap charges applied to expensive unsecured loans. This has been extensively debated and there are arguments for and against capping charges. These arguments are complex and we can only summarise these in this submission.

On the one hand, opponents argue that a charge cap would restrict the ability of legal sub-prime/ doorstep lenders to serve large parts of the market they currently serve. The consequences of this would be to simply push more people into the hands of illegal loan sharks. Opponents also argue that rather than cap charges it is better to rely on financial education and information to promote competition in the sub-prime market thereby putting downward pressure on lending costs.

On the other hand, supporters of charge caps argue that, as well as the social justice point (ie. that it is morally wrong to let disadvantaged households be exploited in such a way) there is the policy argument that allowing non-mainstream lenders to charge such high APR rates simply sustains a business model which enables sub-prime lenders to aggressively promote and sell expensive debt to households who can ill afford to meet repayments. It is hard to argue with the view that these high APRs actually contribute to chronic overindebtedness.

Moreover, the lack of any constraints on the business models of sub-prime lenders means that they are able to squeeze fair lenders such as credit unions out of local markets. It is difficult to see how not-for-profit lenders can stand any chance of thriving unless high cost credit provider business models are constrained.

⁵ Source: Moneyfacts/ LendersCompared.org.uk as at end February 2009

⁶ Source: Moneysupermarket.com – as at end February 2009

⁷ Some credit unions charge less - see <http://www.abcul.org/page/about/borrowing.cfm>

⁸ <http://campaigns.direct.gov.uk/stoploansharks/common-myths.html>

Furthermore, there is evidence to suggest that, far from acting as a bulwark between vulnerable consumers and illegal loan sharks, high cost legal lenders such as home credit providers may be acting as a channel pushing consumers towards illegal lenders⁹.

We accept that there is a risk that some consumers would be exposed to illegal lenders if the business model of legal sub-prime lenders was curtailed by charge caps. However, on balance we have concluded that allowing the market to set charges represents the far greater risk. Unfettered charges sustain a detrimental business model which must have contributed to current level of overindebtedness and is likely to be contributing to illegal lending rather than act as a bulwark between vulnerable households and illegal loan sharks.

There is no reason to hope that relying on information solutions and market forces will be effective at bringing down charges. Consumer behaviour in markets such as the sub-prime lending sector does not conform to conventional economic market theories based on addressing information asymmetries. Consumers in the home credit market have been found to be price insensitive and price competition amongst providers is weak¹⁰.

Therefore, we conclude that it is better to introduce a cap on loan charges. We propose that the rate should be capped at 3% per month. This rate should be phased in over 3 years.

Moreover, in recognition of the risk of borrowers being displaced into the illegal sector, it is critical that this lead time is used to build capacity in the not-for-profit community lending sector (see Expansion of the Growth Fund and Social Fund, below).

Capacity building

Despite the clear advantages of not-for-profit community based lenders in terms of low cost loans, they have achieved comparatively little penetration in disadvantaged communities compared to commercial home-credit companies/ door-step lenders/ payday lenders.

Community based lenders have nowhere near enough capacity, whether in terms of financial or human resources, to meet the need for fair, affordable credit. Looking at the last available data (2005/6), consumers borrowed over £4 billion from commercial non-mainstream lenders of all types including home credit-door step lenders, sub prime lenders, and catalogue companies¹¹. Community based lenders such as credit unions and community development finance institutions accounted for @ £340 million¹².

There is a very real risk that the numbers of consumers who are left with no choice but to use expensive or even unregulated lenders will grow significantly. Recent research undertaken by The

⁹ Research published in 2006 highlights the significant degree of crossover between home credit use and illegal lending. 53% of illegal lender users claim to have used a home credit firm in the previous 12 months. Indeed, amongst illegal lender users, the highest incidence of recent problem debt was with home credit firms. See p33, Illegal Lending in the UK, 2006, PFR/ Polaris on behalf of the DTI, <http://www.berr.gov.uk/files/file35171.pdf>

¹⁰ See para 11, http://www.competition-commission.org.uk/inquiries/current/homecredit/notice_of_possible_remedies.pdf

¹¹ Home credit companies alone lent £1.3 billion and received £1.8 billion in loan repayments in 2005, while credit unions had outstanding loans of £337. Source: Table 7, Short Changed, New Philanthropy Capital, July 2008. However, this probably underestimates the true scale of high cost lending in the UK. Members of the Finance and Leasing Association (FLA) lent around £40 bn in consumer credit in 2008. Many of the FLA's members fall outside the mainstream/ high street lender category.

¹² once Government loans are factored in this rises to under £1 billion.

Financial Inclusion Centre for Circle Anglia estimated that consumers borrowed nearly £30m from illegal loan sharks at Christmas 2009 and will end up repaying over £80m (the average APR charged is estimated to be 825%)¹³.

Increasing capacity amongst community based lenders would also allow government to cap charges on legal sub-prime lenders whilst managing the risk that consumers would be 'displaced' into the hands of illegal loan sharks (see above).

Similarly, the social fund has provided welcome respite for many vulnerable households through emergency loans. However, worryingly, we expect that with prolonged unfavourable economic conditions and expected growth in the unlicensed lending market, more households in need of emergency, short term loans will be vulnerable to exploitation by extortionate lenders (both legal and illegal).

So, alternative sources of affordable lending are needed. Capacity building is needed via a combination of public funds and other sustainable private sector funding mechanisms. This expansion of the community lending sector should be funded through a combination of a financial inclusion levy on banks and other significant financial institutions and Social Investment Bonds (see Financial Inclusion Manifesto).

A new approach to regulating consumer lending

The consumer lending sector seems to be one of the biggest sources of continuing consumer detriment in financial services (for example, the behaviour of sub-prime and other high cost lenders). Moreover, new detrimental practices seem to be continually emerging as non-mainstream financial firms respond to 'opportunities' provided by overindebtedness and the ongoing financial crisis (for example, the growth in payday lenders, sale and rent back providers, commercial debt management providers, and distressed debt sales) .

Furthermore, consumer detriment in the sector affects some of the most vulnerable households in society who are unable to get access to fair, affordable credit products and services from better regulated, high profile, mainstream financial providers whose behaviour is constrained by reputational risk.

We argue that the sheer scale of existing and potential consumer detriment in this sector warrants a radical new approach to regulating consumer credit. So, we make a number of high level recommendations for reforming consumer credit regulation.

In our view, the existing approach to regulating consumer credit is too permissive, reactive, and fragmented.

The regime for obtaining a consumer credit licence is not robust enough. Moreover, the trigger for regulatory interventions is too onerous. This is understandable of course as regulators have to follow

¹³ See The Real Cost of Christmas, The Financial Inclusion Centre – commissioned by Circle Anglia, January 2010, http://inclusioncentre.org.uk/doc/The_Real_Cost_of_Christmas_FINAL_VERSION.pdf

the necessary due process. However, this can leave consumers vulnerable, and means that regulatory interventions often end up ‘closing the stable door after the horse has bolted’.

At the moment we have a fragmented system where the FSA has responsibility for overseeing bank accounts but once the account becomes overdrawn, the OFT takes over responsibility. This makes it more difficult than is necessary for coherent, regulatory oversight of banking.

The UK’s relatively permissive consumer lending regime has allowed lenders and intermediaries to aggressively and, some would say, recklessly sell consumer credit. In other words, extending access to greater credit choice has been the default position. This has been a risky policy approach as consumers have already been ‘primed’ to borrow by aggressive marketing and advertising of consumer goods. We believe that this ‘priming’ made many consumers susceptible to selling of consumer credit and must have contributed to the high levels of overindebtedness in the UK.

Moreover, there is a strong case for arguing that this permissive approach to borrowing in the UK must have undermined consumers’ willingness and capacity to save - as can be seen by the corresponding high levels of overindebtedness and low savings ratios in the UK. Selling easy access credit – which turns into debt that has to be repaid after all – must undermine ability to put money aside to build assets for the future.

So, if we are to achieve the necessary rebalancing between savings and borrowing, regulation should be reformed to change the default position to make it more difficult for lenders to aggressively ‘sell’ discretionary credit and discourage unnecessary borrowing¹⁴.

The more robust approach to prudential regulation being adopted by the FSA should ensure that lenders lend more prudently. However, we think this needs to be complemented by some additional measures.

Therefore, we make a number of additional recommendations to i) improve consumer protection and in turn, ii) promote access to affordable credit on a sustainable basis:

- the new FCA should become the single regulator for all secured and unsecured lending and lenders;
- consumer credit providers should be subject to a full authorisation process similar to that operated by the FSA rather than the current licensing process. This authorisation process should cover fitness and competence of firms and individuals. This should apply to originators of loans and secondary providers of services such as debt management companies and buyers of distressed debt;
- all consumer credit providers (secured and unsecured) should be subject to robust conduct of business regulations relating to marketing, promotions and advertising (including at the point of sale), and conflicts of interest (eg. DMP providers paying fees to introducers);

¹⁴ NB: we are not against access to credit – indeed we count access to fair and affordable credit to smooth out peaks and troughs of income as one of the core financial needs. However, we think this is very different to discretionary ‘lifestyle’ credit which has been sold far too aggressively)

- a new risk based approach to regulating consumer credit products should be adopted. That is, products and services aimed at specific consumer sectors or involving new practices should be subject to a *pre-approval* process. New products and services should be submitted to regulators for assessment to identify potential detriment and develop appropriate regulatory response. In practice, this would mean that ‘innovations’ such as payday loans, or commercial debt management plans would be assessed for potential detriment in advance rather than allow detriment to emerge before action is taken by regulators.;
- charges on loans should be capped (see above).

Best practice compliance statements

The FSA, OFT, FOS, and trade bodies such as the BBA, ABI, CML, FLA¹⁵, and Lending Standards Board should work with consumer organisations to producing new guidance and statements of best practice in retail financial services aimed at firms and consumers. These best practice statements would be suitable for all major financial product sectors. However, transactional banking, mortgage and credit products and practices are a priority given the potential for detriment in the wake of the financial crisis.

The FSA and OFT already produces a number of guides and factsheets for consumers and issued a range of guidance for lenders on a number of matters relating to the mortgage and credit markets. However, we do not think that these guides are very consumer friendly. Moreover, from our experience, many financial services providers seem to find it difficult to interpret what treating customers fairly or reasonable behaviour means actually means in practice.

We believe the market would operate better if regulators produce clear statements of good practice aimed at industry and consumers (and their representatives such as advice agencies).

The objective of these practice statements should be to:

- make it clear to firms operating in the mortgage and credit markets the behaviours and practices the FSA and OFT consider are in breach of legislation. This should be done through statements of good practice with clear examples of behaviours that potentially breach the spirit and letter of legislation and regulatory principles;
- alert consumers to the sorts of detrimental practices they should avoid and to the potential for redress;
- help debt advice charities and other consumer organisations understand consumers’ rights and understand the application and scope of consumer protection and financial regulations.

Financial firms should publish in an easily accessible place on their websites:

¹⁵ Financial Ombudsman Service, British Bankers Association, Association of British Insurers, Council of Mortgage Lenders, Finance and Leasing Association

- their policies and practices;
- how these comply with the relevant regulations and best practice compliance statements; and
- where policies and practices are in breach of requirements, what remedial action is being taken.

Regulating the commercial debt management sector

The growth in the commercial debt management plan (DMP) has been a source of real concern for consumer representatives. The OFT should urgently take action to protect consumers from the detrimental practices of these commercial providers – including the high level of charges.

Our research has found that a borrower with £15,000 debt using a commercial debt management company could end up paying nearly £3,000 in charges. This simply adds to the debt burden and means that borrowers could end up taking an extra year to clear off their debts compared to using a not-for-profit advice agency and is particularly galling given that free debt advice from not-for-profit debt advice charities is widely available.

As we describe above, the OFT has a significant body of legislation at its disposal to protect consumers in the unsecured lending markets including the provision of debt advice. However, we are concerned that this legislation (or the way it is being implemented) does not provide vulnerable consumers with sufficient protection against commercial DMP providers.

With regards to unsecured lending markets, consumers are supposed to be protected from entering into a transaction without being in full knowledge of the facts, and from unfair practices and behaviours that materially distort, or is likely to materially distort, the economic behaviour of the ‘average’ consumer.

It is difficult to see why an ‘ordinary’ consumer in full possession of information about the options available to him/ her would knowingly choose to use the services of a commercial DMP provider rather than contact a debt advice charity (there may be exceptions for owners of small businesses who have very complex affairs).

The OFT also operates the Consumer Codes Approved Scheme (CCAS)¹⁶. This scheme formally approves and promotes voluntary business-to-consumer codes of practice which set higher standards of customer service. One of the approved codes is run by the Debt Managers Standards Association (DEMSA). However, this association appears to have a limited number of members from debt management sector¹⁷.

The obvious answer is for the Government to simply prohibit commercial debt management provision (or at least impose much stricter pre-approval terms when licensing firms). It is difficult to see what socially useful purpose these organisations serve given the existence of not-for-profit debt advice agencies.

¹⁶ http://www.offt.gov.uk/shared_offt/Approvedcodesofpractice/offt748.pdf

¹⁷ <http://www.demsa.co.uk/members.htm>

The argument that these commercial providers provide additional capacity and benefits for consumers is not sustainable in our view. If these commercial providers are able to find a market for their services it is surely because consumers are insufficiently aware of the availability of not-for-profit debt advice charities and/ or the debt charities do not have sufficient capacity to meet consumers needs.

Given the scale of the debt problems facing many households and the clear detriment represented by commercial DMP providers, it is incumbent on the authorities to make the necessary capacity available and to better promote awareness of NFP debt advice charities.

However, Government is unlikely to prohibit outright these providers. But the potential for consumer detriment is so great that new measures are needed urgently to protect consumers.

New regulations relating to best practice and acceptable behaviours in the commercial DMP market should be urgently introduced covering:

- ‘best interests’: OFT should issue clear and robust guidance on what represents borrowers best interests with regards to DMPs using clear illustrations to ensure that providers understand the OFT’s requirements;
- critically, fees should be capped and must be clearly, transparently and fairly disclosed in a prominent position on promotional material regardless of which distribution channel is used by DMP providers. Illustrations should be used to explain the impact of fees on debt repayment schedules;
- the pitfalls of using DMPs should also be prominently, clearly and objectively communicated to potential clients;
- DMP providers and introducers must alert borrowers of the existence of not-for-profit debt advice providers;

Moreover, all lenders should commit to refer or ‘hot-key’ borrowers to debt advice charities and not refer them onto commercial DMP providers.

Regulating distressed debt sales

Lenders are under pressure to protect their positions or cut losses on loans at risk of default. One way of doing this is to sell on distressed debt to third party firms who take on the responsibility for collecting the debt.

There are different approaches to distressed debt sales. However, in simple terms it involves a lender/ creditor selling non-performing loans to a specialist buyer after trying unsuccessfully to recover the debt. The price paid for the distressed debt can vary but is usually very heavily discounted from the ‘face-value’ of the loan. Typical prices recently have been between 5%-20% of the debt’s face value. The price reflects the buyers’ views on how difficult it is likely to be to recover the debt.

The size of the debt resale market is difficult to gauge as there is very little published research on the subject. However, estimates suggest that in 2008, around one-third of defaulted unsecured debt (around £9 billion)—was sold on by banks and other creditors¹⁸.

A number of factors suggest that the market for distressed debt sales could grow significantly:

- new accounting regulations increase the cost of holding defaulted debt for lenders which will encourage them to consider selling more debt and selling it earlier;
- companies from other sectors such as utilities and telecommunications are reported to be looking at debt sales as an alternative to debt collection;
- the financial crisis has affected the market for complex investment products so investment banks are considering entering the debt sales market. Similarly, institutional investors such as private equity funds who can take a long view on investments are finding portfolios of deeply discounted distressed debt portfolios attractive.

Clearly, if the original lender has already tried unsuccessfully to recover the debt, there is the potential that the new buyer will resort to more aggressive techniques unless constrained by regulation or reputational risk. However, specialist debt buyers are usually not regulated, nor are they mainstream household names so they are not constrained by reputational risk. Therefore, we think there is a considerable risk of vulnerable consumers being exposed to aggressive practices.

To protect consumers, we make a number of recommendations:

- all originators of loans and providers of secondary services such as distressed debt purchases should be authorised and regulated by the FSA;
- debt sellers and buyers should be subject to robust conduct of business regulations relating to marketing and promotions, conflicts of interest, and treating customers fairly including ensuring that affected borrowers have access to unbiased, NFP debt advice;
- lenders wishing to sell distressed debt portfolios to third party agencies should be required to apply for express consent from regulators before selling the debt. Regulators should ensure that the interests of borrowers are fully protected under the terms of the debt resale¹⁹;
- lenders selling debt portfolios should be required to communicate clearly to affected borrowers explaining the consequences of debt resales, how their rights are affected, and 'hot-key' borrowers to NFP debt advice providers.

Investigation into unfair contracts terms, pricing and commercial practices in the mortgage, unsecured credit, and commercial DMP sectors

As with the FSA and mortgages, the Office of Fair Trading has a significant body of legislation at its disposal to protect consumers in the unsecured lending markets (including the provision of debt advice).

¹⁸ http://www.financialhelpline.co.uk/news/archive/UK_consumer_debt_sales_market_sees_dramatic_growth

¹⁹ in effect, this would be similar to the process life insurance companies have to go through to satisfy the FSA that policyholders interests are protected when closed life insurance funds are sold to third parties

This includes the ability to revoke credit licences if firms are not fit for business²⁰, measures to protect against unfair relationships^{21, 22} and unfair contract terms²³.

The legislation can be quite complex to interpret. For example, even extremely high charges that might seem extortionate to ordinary consumers, are not necessarily unfair in the eyes of the law or even covered by the law (as the recent decision by the Supreme Court on unauthorised overdraft charges demonstrates). However, charges may be considered unfair if they are not disclosed fairly and transparently.

Other examples might include:

- where the interest rate, or other fees or charges, are so much higher than those in the particular market sector, or payable by borrowers in similar situations, as to make the relationship as a whole unfair to the borrower;
- the borrower may be unaware that a fee would be charged in a particular case, or the level of the fee, or how this might impact on the debt;
- the lender may have failed to disclose relevant information, or may have done so in a false or misleading manner, misrepresenting key elements;
- the information may also have been unclear or ambiguous, and so may not have been readily comprehensible.

The net result is that consumers may have found themselves entering into a transaction without being in full knowledge of the facts. Moreover, consumers are also supposed to be protected from unfair practices and behaviours that materially distort, or is likely to materially distort, the economic behaviour of the 'average' consumer.

In our view, there is reason to believe that some of the behaviours by firms and terms in the contracts in the sub-prime mortgage, unsecured credit, and commercial debt management plans (DMPs) sectors exhibit the characteristics described above.

Further information on commercial DMPs can be found above but other examples include extremely high SVRs being levied on sub-prime mortgages (see above), and margins on credit card rates at record levels²⁴.

Without access to commercially sensitive information it is impossible to say with certainty whether these terms and practices are unfair. Therefore, we urge the FSA and OFT to conduct a joint comprehensive investigation into unfair contract terms and practices in these markets. The FSA should convene a working group with the Office of Fair Trading, FOS and consumer representatives to investigate more closely whether:

- the terms in sub-prime mortgages and unsecured loans markets are unfair and run contrary to the unfair contracts regulations;

²⁰ http://www.ofg.gov.uk/shared_ofg/business_leaflets/credit_licences/ofg969.pdf

²¹ http://www.ofg.gov.uk/shared_ofg/business_leaflets/enterprise_act/ofg854.pdf

²² The Consumer Protection from Unfair Trading Regulations 2008 (CPRs) implement the Unfair Commercial Practices Directive (UCPD)

²³ http://www.ofg.gov.uk/shared_ofg/reports/unfair_contract_terms/ofg311.pdf

²⁴ See 'Are banks and building societies playing fair?' The Financial Inclusion Centre, www.inclusioncentre.org.uk under publications

- the product pricing structures used by lenders have the effect of exploiting borrowers locked into sub-prime mortgages;
- the net margins on unsecured credit products such as credit cards and overdrafts are justified;
- the terms in commercial DMPs contravene unfair contracts regulations and the selling and marketing of DMPs contravene unfair commercial practices regulations.

The working group should establish a plan of action for dealing with any breaches and ensuring consumers obtain due redress.

About The Financial Inclusion Centre

The Financial Inclusion Centre is an independent research and policy innovation think-tank dedicated to promoting financial inclusion and fair, efficient, competitive, and accountable financial markets.

For general information on the Centre's work please see: www.inclusioncentre.org.uk

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

Introduction

The Financial Services Consumer Panel (“the Panel”) is a statutory body established under s.10 of the Financial Services and Markets Act 2000 (FSMA). Initially established by the Financial Services Authority in December 1998, the Panel advises the FSA on the interests and concerns of consumers, and reports on the FSA’s performance in meeting its objectives in the regulation of financial services. It also looks at the impact on consumers of activities outside, but related to, the FSA’s remit.

Executive Summary

The Financial Services Consumer Panel welcomes the consultation on reforming the consumer credit regime. We view this as a critical issue that requires consideration, particularly in the context of other current changes to the regulatory regime for financial services. Reviewing consumer credit regulation now presents a unique opportunity to strengthen the regulatory overview and rationalise the approach to consumer protection across the financial services market. Like the recent HMT consultation, it should provide a platform to shape future legislation.

Credit plays an increasingly critical role in the economy. The regulation of credit is particularly significant due to the high proportion of consumers who use it, the size and nature of the sub-prime market and the extent of detriment that can result from irresponsible lending and borrowing. Crucially, credit regulation also has a key role in mitigating the size and impact of the illegal lending sector, prevalent in the most deprived areas of the UK. Regulation, therefore, needs to specifically address issues of access, price, responsibility and fairness right across the credit market, which is characterised by a high degree of variation and products, methods and targeting, and a plethora of small, often sole, traders.

The document presents two options for the future regulation of credit:

1. Consumer credit is regulated under a new FSMA-style consumer credit rulebook by the FCA.
2. Consumer Credit continues to be regulated under the CCA. The regulatory authority with responsibility for consumer credit under this option would not be confirmed until the outcome of the consultations on the future of the competition and general consumer functions of the OFT.

The consultation document clearly favours Option 1 stating that “There is no doubt that the application of FSMA-style requirements to consumer credit firms could lead to important consumer protection and market oversight benefits.”

The Consumer Panel, while favouring a unified regime under a single financial services regulator, feels that the potential consumer benefits arising from FSMA-style regulation may not be as clear cut or assured as the view presented in the consultation document. The Consumer Credit Act (CCA) was developed following an extensive consultation process involving a wide network of consumer stakeholders and its provisions have served customers well. The outcome of the proposed regulatory reform needs to enhance current levels of consumer protection. While welcoming the current consultation and recognising the considerable progress the FSA has made in terms of consumer protection over the last 18 months, the Consumer Panel fears that some of the limitations associated with the FSMA style of regulation could undermine the current level of consumer protection, at least in the short-term. However we are also aware of the persistence of gaps in the regulation of retail banking which have not been addressed by the FSA taking over regulating the deposit taking side of retail banking, a situation we feel could be tackled by a single regulator for all retail banking services.

Therefore, we present, below, a case for transferring responsibility for consumer credit to the FCA as part of a risk-based approach to regulation, including retention of the Consumer Credit Act provisions, alongside well-resourced intelligence and enforcement functions at local level, for the higher risk elements of the market. A comprehensive model of assessing the level of risk presented by different categories of lender requires detailed consideration, but could include factors including the size of the firm, size and nature of target market and product offerings. We feel that this offers the optimum combination of the two existing regulatory models – providing consistency and clarity across the market, greater efficiency in the regulation of the retail banking activities of authorised firms and, crucially, comprehensive scrutiny and enforcement in relation to small traders and, especially those operating in the sub-prime market.

There are, however, some important timing issues that must be taken into account during this consultation and the stages that follow. The development of the FCA is still at a very early stage and its ethos, culture and approach to consumer protection are not yet known. Decisions about the future of credit regulation must take account of the development of the FCA, to ensure that its structure and operating style are appropriate in the context of those decisions. Transferring the regulation of consumer credit to the FCA will add significantly to the remit of this new body: it is essential that the implications are fully understood, effectively resourced and costed. In addition, this consultation closes before the reports of the Independent Banking Commission and the Lending Code Review are published. Again, these important initiatives must feed into the post-consultation process to ensure a well-informed and joined-up approach.

There is, inevitably, some concern that reform of credit regulation creates the risk of reducing resources to this area in a way that will weaken consumer protection. The Consumer Panel urges the Government to undertake any subsequent reform following the consultation process with a view to the potential longer-term social and economic outcomes rather than the short-term costs associated with effective change.

Given these issues we recommend that, should a decision be taken to transfer responsibility for credit regulation to the FCA, the Government launches a staged consultation process covering the detail relating to this transfer and its implementation. The Panel feels strongly that consumer protection in relation to credit must be enhanced by a transfer of responsibility and absolutely must not be diminished, even in the short-term, while the new regime beds in. In the context of

remaining gaps and overlaps in retail banking regulation, which evidence suggests have been heightened during the transition to FSA regulation, it is critical that regulatory reform will deliver, at the very least, a comparable level of consumer protection from the outset.

Consultation questions

Chapter 1 – The case for reform of the consumer credit regime

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

The Consumer Panel agrees that the wider institutional reform represents a good opportunity to reconsider the approach to credit regulation and, provided that the FCA is able to deliver excellence in consumer-focused regulation, offers the chance to significantly enhance protection for consumers of credit. The FSA has demonstrated significant progress over the last 18 months in terms of consumer protection and we are relatively optimistic that this agenda will be pursued in the FCA. The powers outlined in the latest HMT document “A new approach to financial regulation, building a stronger system”, if realised, present a strengthened consumer protection authority which should deliver better consumer outcomes.

We also agree that in the uniquely diverse, large and rapidly growing consumer UK credit market, consumers require a regulatory model that offers the optimum outcomes. In particular, we support the view that regulation must be able to recognise and respond, rapidly and flexibly, to the wide range of risks and consumer outcomes that characterise unsecured borrowing, without imposing disproportionate barriers to market entry or deterring competition.

The current model of credit regulation, despite being extensive, multi-layered and complex, still results in gaps and overlaps in activity which cause consumer detriment.

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?

The consultation paper lists these as:

- accountability for some objectives split,
- lack of coherence in consumer protection and market oversight,
- confusion and duplication,
- too reactive and insufficiently flexible,
- deterrent to effective deregulation.

The Panel agrees that lack of accountability, lack of coherence, and confusion and duplication have been inherent in the current split in responsibility. However we are sceptical that deregulation of consumer credit regulation is a desirable goal when there is a high risk of consumer detriment.

We also feel that the Consumer Credit Act (CCA) offers key aspects of consumer protection that should not be lost. The Panel has, at times, been critical of the FSA’s legalistic interpretation of its responsibilities under FSMA,

examples include a lack of effective implementation of the Treating Customers Fairly principle and a reluctance to exercise Own Initiation Variation of Permissions on authorisations. It is critical, therefore, that transfer of credit regulation to the FCA under a FSMA-style regime offers at least a comparable level of consumer protection as the CCA and, preferably, delivers a significantly enhanced model of consumer protection. Ultimately, the success of the proposed regulatory change must be measured against this benchmark.

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;**

Whilst not attempting to provide a comprehensive list of risks the following are those that the Panel believe are significant.

Events leading up to the recession saw irresponsible lending and easy access to credit, an industry focused on short term profits and consumers focusing on short term costs, benefits and affordability. These factors led to more complex pricing structures and products and failures in consumer protection. Lack of competition, unfair business models, and failure of regulation continue to present risks to consumers. These are illustrated by the entrenchment of bank charges, rather than up-front costs, as a significant profit vehicle.¹

“There is a continuing lack of transparency about the real cost of banking services and it is difficult for consumers to help drive down the cost of unarranged overdrafts or other charges, whether explicit or hidden, by shopping around. The voluntary approach to dealing with unauthorised overdraft charges relies on banks improving themselves, yet they have patently failed to do this in other areas in the past.”²

Unfair bank charges continue to pose significant risks to consumers and are largely beyond their control. The nature of the charges themselves is such that the poor pay more for banking services and significant cross-subsidies apply. Their lack of transparency inhibits competition and choice.

Further risks are evident in the rationing of credit and increases in the cost of credit. The lack of mainstream credit options for those on low incomes and those who prefer not to use credit products that are delivered and/or repaid via a bank account has seen the increase in use of sub-prime lenders and this market is likely to expand.³ In addition, in the current credit-constrained climate, even some of the sub-prime lenders are shifting to a more up-market

¹ Paul Johnson, “Free or Fee: Are „free“ products good for consumers?” in Consumer Focus, Rethinking Financial Services, Focus on Finance Review, June 2010.

² Financial Services Consumer Panel submission to the HMT/BIS Consumer Credit and Personal Insolvency Review, December 2010

³ Consumer Focus, Keep the Plates Spinning, August 2010

target population, leaving the most vulnerable consumers at risk of falling prey to illegal lenders.

In a time of restricted availability of credit, and in particular of personal loans, credit card interest rates have continued to rise. Whilst the base rates are at a historic low of 0.5%, average APRs are now 38 times base rates, the highest margin on record.

The Panel also believes that the system of minimum repayments on credit cards is another area in need of attention. Under the current system, it is possible for consumers to make an acceptable level of repayment and yet still remain in debt for many years. For example, on a £3,000 credit card debt at 17.9% APR, a customer making a monthly minimum repayment of 2% of the outstanding balance would take 41 years to clear the debt in full, at an interest cost of £6,300. Changes to the Lending Code to ensure the minimum repayment is set at least at 1% of the principal do not, in the Panel's view, go far enough. The information provided to borrowers about their options in setting repayment levels, and the impact of choosing only to make the minimum repayment, are not sufficiently clear.

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

Under the CCA and the OFT's jurisdiction there are some key provisions and approaches to consumer protection that, we would argue, need to be preserved regardless of where responsibility for regulation sits. In particular, we refer to elements of the CCA and the Consumer Protection from Unfair Trading Regulations that provide for:

- strict liability
- render contracts unenforceable,
- cooling off periods and termination rights,
- the liability of creditors such as card issuers for supplier breaches (s.75),
- hardship provisions, particularly in relation to re-opening agreements and to repossessions,
- the powers to make orders in unfair relationships
- the right to reject interest rate hikes
- early settlement provisions (with a rebate of part of the interest charge) which provide an opportunity to pay off a loan early, allowing goods subject to a credit agreement to be taken in part -exchange.
- prescriptive information requirements, (eg interest rate disclosure has been a feature of statements on credit products but it has taken a super-complaint to get interest rates on savings account statements)
- regulation of financial promotions and misleading advertising

In addition, the current regulatory approach is far more transparent than that currently taken by the FSA, revealing details of prosecutions, market investigations and undertakings, rather than just successful enforcement action. The Panel believes strongly in the power of transparency as a consumer protection tool, providing consumers with the opportunity to make choices based on on-going regulatory intelligence. We would argue, therefore, that the FCA should have clear obligations and powers to perform

its role in a transparent and accountable way using reputational regulation to facilitate consumer choice.

The OFT, under its consumer protection legislation, can also impose fines, specific requirements on firms and restrictions on their activities under their licence, and require them to rectify unfair behaviour in a more responsive and specific way than the FSMA rules. There are clear, responsive and flexible avenues for taking action. The operation of “stop now” orders is particularly effective in limiting consumer detriment from unfair practices and allows intervention without the sometimes cumbersome requirements in the FSMA for CBAs and consultations. Regulation of credit should retain these important protections and include a greater appetite to fine those who are causing consumer detriment.

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

The aim is to achieve cost effective regulation of firms, recognising that costs are usually passed on to consumers by way of price increases. Whilst duplication exists because of the split in regulation, creating a unified regulator and addressing the risks now crystallised in this market requires effective regulation and sufficient resources.

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

The stated objectives of the proposed regulatory reform are :

- clarity, coherence and improved market oversight;
- effective and appropriate consumer protection, including through a responsive and flexible framework;
- simplification and deregulation
- proportionality and cost effectiveness.

The Panel supports most of these objectives for reform. In particular, we would welcome a properly resourced regime that has the necessary powers to secure better market information and ensure earlier identification of risks to consumers. We remain very sceptical, however, that deregulation is desirable in the credit market where the risk of consumer detriment is high.

Chapter 2 – Options for the 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.**

The current split of regulatory responsibility between the FSA and the Office of Fair Trading has made regulatory action more problematic, particularly in areas that straddle jurisdictions, and has resulted in consumer detriment.

Whilst the OFT and FSA published their first action plan for delivering better regulatory outcomes in 2006, and on 1 November 2009 a new concordat was agreed between the regulators setting out where responsibility for various parts of BCOBS and the Payment Services Regulation lies, it is still not clear

how effectively overlapping regulatory issues are dealt with on a day to day basis.

Recent examples indicating persistent problems include:

- Set off - The question of set-off and how its misuse is being tackled is an example of the lack of clarity that can arise. For example, does the Principle of Treating Customers Fairly apply to the entire set-off process, or only the part that relates to accounts in credit, and how does this work in terms of enforcement?⁴ The division of responsibility has been cited as an obstacle to the FSA dealing with the issue and consumers continue to experience detriment as a result.
- Unfair bank charges - The issue of unfair charges, and particularly unauthorised overdraft charges, should be part of banking conduct regulation but there was no overview of this area because of the credit/banking regulatory split, the failure of self-regulation under the Banking Code to deal with the issues, and the lack of jurisdiction of the FSA in the area until November 2009. No action has been taken since the failure of the OFT's Supreme Court action in 2009, despite the court indicating other options to tackle the issue.
- PPI – The mis-selling of PPI continues unchecked. Consumers may justifiably view the credit transaction and sale of PPI associated with it (and in fact often included and financed by the credit agreement) as one transaction.
- Packaged products – The growth of packaged products, including an expansion of packaged credit cards, creates significant barriers to competition. Costs are not transparent and increasingly credit cards and preferential savings rates are being offered only if you have a current account with the same provider. Regulation of packaged products is likely to be split or fall between the gaps between providers.

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 current OFT model relies on local level enforcement from Local Authority Trading Standards Services (TSS). An enforcement presence at local level means that surveillance, inspections and complaints investigations can be organised according to the risks to particular local communities and using the full array of consumer protection tools. The credit market is diverse. For example, some of the higher risk activities are perpetrated by small businesses in the homes of the financially excluded, in other cases credit is linked to sales of goods and services such as second hand cars and home improvements.

⁴ Financial Services Consumer Panel, Regulation of Retail Banking Conduct of Business, A review of the first year of the new regulatory framework, November 2010.

General consumer information, assistance and advice, including consumer credit advice, is currently provided by Consumer Direct and this level of service needs to be maintained for consumer credit queries preferably as part of a single consumer information/advice service. Consumer Direct is also a useful source of information to the regulator.

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

The Consultation Paper talks about delivering an “at least equivalent” level of consumer protection. The Panel would argue that the aim should be for enhanced consumer protection, determining what might be equivalent carries risks of different standards and consequences applying in practice. In addition to retaining the protections contained in the CCA and the Consumer Credit Directive (CCD), the guidance provided by the OFT on credit related issues such as debt management and irresponsible lending guidance should be retained.

The enforcement powers and principles and some of the very useful guidance from general consumer protection provisions should also be imported such as the standards established in the consumer protection enforcement principles, defined causes of action and strict liability, and the detailed approach to unfairness.

A well-resourced, responsive, and pro-active local enforcement approach is a key factor in maintaining and enhancing the current level of consumer protection.

In addition the current CCA toolkit should be enhanced through:

- rule making powers to outlaw emerging unfair practices;
- redress powers and a s404 type power in terms of past practices
- a review of the level and type of sanctions available.

8. The Government would welcome further evidence relating to:

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

The consultation paper notes the significant problems – lack of coherence and strategic oversight - that arise from the artificial division of regulatory responsibilities for consumer credit and other retail financial services. Paragraph 1.17 reviews the problems that affect individuals and very small businesses but, in the Panel’s opinion, the weaknesses are more wide ranging.

The Panel has drawn the FSA's attention to specific examples of potentially poor conduct in banks" lending to businesses, such as opaque pricing of business loans and aggressive demands for collateral. We have argued that the FSMA definition of "consumers" (Section 138 (7)) covers non-financial business consumers, who thus warrant protection under the FSA's Principles of Business. But the FSA has rejected our call for action, arguing that matters relating to non-FSA regulated lending fall under the jurisdiction of the Office of Fair Trading.

This response leaves exposed those non-financial businesses that are not given protection by the Consumer Credit Act, by competition policy or by redress mechanisms, such as the Financial Ombudsman Service. The resulting regulatory underlap is a matter of considerable concern: it is well known that small and medium-sized enterprises (SMEs) and larger "mid-capitalisation" companies that seek external finance are heavily reliant on banks.⁵

The Consumer Credit Act offers businesses protection but is narrow in scope. Only credit agreements up to £25,000 (and the equivalent for hire agreements) qualify and the provisions are limited to sole traders, unincorporated partnerships of up to three persons and other unincorporated bodies.⁶ Although sole traders are the predominant legal form of business in the UK, they account for a comparatively small part of the business lending activities of banks.⁷

Competition policy alone may fail to provide effective protection against financial firms' abuse of their business customers. Market incentives may be misaligned, so that the simple promotion of competition makes things worse for consumers rather than better. Implementation of competition policy has also been subject to long delays, arising from policy-makers' inertia and the time required to analyse evolving market structures and devise remedies.⁸

⁵ " .. SMEs that do seek external finance are almost entirely reliant on banks, in the form of bank loans, overdrafts or other working capital products such as invoice discounting and factoring. ...Mid-sized firms .. defined .. as having a turnover of £25 million to £500 million ... tend to be largely reliant on banks for external finance". "Financing a Private Sector Recovery", Cm 7923, July 2010, HM Treasury and BIS, paragraphs 3.7, 3.11 and 3.12.

⁷ According to a special BIS survey, the stock of loans by four major UK lenders to firms with an annual turnover of under £1 million was £35 billion in August 2009. (Table 1, "Trends in lending" October 2009, Bank of England). At that time, the money supply measure M4 stock of lending (including secured lending) to private non-financial corporations, unincorporated businesses and non-profit making institutions was £535 billion, data not seasonally adjusted, and £544 billion when the data are adjusted for seasonality and the effects of securitisations (Tables A4.1 and A4.3, "Bankstats", Bank of England, 1st March 2011).

⁸ Cruickshank Report (2000), "Competition in UK Banking"; Competition Commission (2002), "A Report on the Supply of Banking Services by Clearing Banks to Small and Medium-Sized Enterprises within the UK", Cm 5319. Further evidence of a "complex oligopoly" is provided by Heffernan, S. (2003), "UK Bank Services for SMEs: Are they Competitively Priced?", Cass Business School, Faculty of Finance Working Paper.

Protection for disaffected business consumers of financial services is also offered by the possibility of redress through the Financial Ombudsman Service, but the protection is again limited to the smallest enterprises. So-called “micro-enterprises” can bring complaints to the ombudsman as long as they have an annual turnover of less than two million euros and fewer than ten employees. Sole traders and firms with fewer than ten employees comprise the vast majority of private sector enterprises in the UK, but account for only a fifth of private sector turnover.⁹

The Panel draws these conclusions:

- The protections afforded to very small businesses under the Consumer Credit Act need to be replicated should credit regulation move to the FSA.
- Despite its inherent disadvantages (cost, capture), conduct regulation is a necessary complement to effective competition policy.
- There exists a potentially large conduct regulatory underlap affecting medium-sized enterprises and mid-capitalisation non-financial businesses.
- In view of past ingrained habits and current statutory powers, it would be highly incautious to assume that the new financial conduct regulator would see such businesses as part of its consumer protection mission.
- Consideration should be given to an extension of the protections afforded by the Consumer Credit Act and the Financial Ombudsman Service to larger credit and hire agreements and larger businesses.

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.

The Panel recognises that the FSMA regime does, in principle, offer capacity for greater flexibility than the Consumer Credit Act. However, in practice we have not always found this to be the case. Should credit be incorporated within a FSMA- style regime, the Panel would want to see the FSMA provisions applied in a more flexible, consumer-focused way than has sometimes been the case.

The Panel has, in the past, found the FSA’s regulatory approach and the application of FSMA in some cases to be cautious, slow and unresponsive, with the FSA attributing this, in part, to the lack of scope and powers in FSMA. However we have noticed a considerable step-change in the regulation of in-credit retail banking services since the FSA took over direct regulation of this area from the self-regulated Banking Code in November

⁹ Source: Department for Business Innovation & Skills (October 2009), “Small and Medium-sized Enterprises (SME) Statistics for the UK and Regions 2009”. The turnover figures exclude financial intermediation.

2009, as we detailed in our report into the first year of FSA regulation of retail banking.

On the other hand, we have also recognised the considerable improvement in the FSA's willingness to intervene at an earlier stage where it identifies consumer detriment. Its desire to use the tools granted by FSMA to protect consumers has also risen following the financial crisis, while its enforcement remit has strengthened considerably.

The requirement, under normal circumstances, to conduct cost-benefit analysis and carry out full public consultations before making or amending rules or undertaking significant regulatory initiatives is time consuming and does not provide the regulator with either the flexibility or responsiveness to act in circumstances that require an immediate response. The Panel has previously expressed concerns about the quality of CBAs, the lengthy process, often focused on quantitative analyses without any real assessment of consumer benefits and social outcomes, and the potential for them to be subject to industry lobbying and influence. In particular, the FSA's cost benefit analyses have focussed much more heavily on the costs and benefits to industry rather than the financial and wider social benefits to consumers.

We welcome the proposed temporary product intervention powers for the new regulator and encourage these to be extended into the areas of mis-selling and unfairness.

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

The Panel has been critical of the FSMA style supervisory approach in the past but recognise the current and proposed improvements in moving to a more conduct focused regulator prepared to intervene and more detailed prescription.¹⁰ We applaud the FSA's new intent and support the new approach: to see it strengthened further, we want to see it linked to clear consumer outcomes and regular monitoring and reviewing. The approach may be able to effectively include credit but consultation and changed methods of enforcement, including enforcement at local level, would need to be part of any transfer.

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

The OFT oversees related consumer law and so has a broad perspective on consumer protection issues and standards. The application of standard consumer principles such as fitness for purpose and safety, strict liability provisions, and the use of market investigations, information gathering powers and consumer networks are all advantages of the current approach and overview.

¹⁰ Hector Sants, Speech to the BBA Seminar on the Financial Conduct Authority, 2 March 2011.

The role of local trading standards services in taking referrals from Consumer Direct means that the full range of consumer protection tools can be applied in investigating consumer complaints about goods and services that may then result in enforcement action.

The provision for joint liability where there is a link between a credit agreement and a contract for the provision of goods or services is an important protection for consumers and supports the principle of a unified system of protection. It is particularly relevant in providing consumers security in internet and cross-border transactions.

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)?**

and

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?**

and

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?**

and

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?**

As outlined above, the Consumer Panel is supportive of a unified regime which has real potential to overcome some of the current problems and provide better consumer protection. We feel strongly, however, that the new regime must offer at least the level of consumer protection afforded by the current CCA and associated consumer protection legislation. It will also be essential to assess how and whether an FCA of the type envisaged will be of a scale that is „workable“. Ensuring a well resourced regulator which is fit for purpose, given its considerable remit, will be critical. We have also highlighted the importance of including a well-resourced, local intelligence and enforcement function within the new regime.

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.**

The FSMA regime would have to adapt to the diversity of the credit market and the prevalence of small, local firms, especially within the sub-prime sector. In recognition of this, the Panel advocates a risk-based approach to

credit regulation within the new regime. This would combine a relationship-management approach to the regulation of lending activities by bigger, national firms operating largely in the mainstream, with a proactive local enforcement approach to the regulation of smaller enterprises and sub-prime lenders. Categorisation of credit suppliers to the different risk categories should be made on the basis of factors such as size, product offerings, and size of target customer groups.

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

The Consumer Panel's view is that self-regulation has failed to deliver the desirable consumer outcomes in other financial service areas, most notably in relation to the industry's oversight of the Banking Code.

Given the extraordinarily important economic and social role of banking and the lack of a consumer culture in the sector it is an area that should not be left to self-regulation.¹¹ Movement to a unified regime, where consumers understand what the rules are and where and how they are able to seek redress, should not logically leave aspects of the regulatory environment outside the scope of the regulator.

In the consumer credit market, the sheer number of firms regulated, and the very local scope of many of them, would make effective self-regulation an extremely difficult proposition.

Self-regulation should enhance consumer experience and not be a substitute for necessary consumer protection. While there are good examples of trade body codes of practice in the credit market, it should be remembered that membership is voluntary and less well intentioned or less competent businesses will either not join or will migrate to the more lax regime.

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.

The Consumer Panel is concerned at the potential for deregulation to reduce the degree of protection afforded to consumers.

Chapter 4 – Implementation and transitional arrangements

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

We agree with the proposal that agreements already in existence and regulated currently under the CCA should be included in any transfer of consumer credit regulation to the FCA provided that the new regime delivered an at least equivalent level of protection for the consumer.

¹¹ Financial Services Consumer Panel, Regulation of Retail Banking Conduct of Business, A review of the first year of the new regulatory framework, November 2010.

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: **First Response Finance Ltd**

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 First Response Finance Ltd
on “a new approach to financial regulation: consultation on reforming the
consumer credit regime”.**

First Response Finance Ltd is pleased to submit a response to the recent consultation on “a new approach to financial regulation: consultation on reforming the consumer credit regime.” We understand and are concerned that the Government's 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 currently offer a Hire Purchase product to the non-standard consumer credit market and employ approximately 180 staff. We intend to extend our products and services in the future so that we can increase both our growth and more importantly offer our customers good value products according to their needs.

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 the 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

John Fellows
Company Secretary

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: **FIRST SENIOR FINANCE LTD**

RESPONSE to

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16 March 2011

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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 specialised mobility house lending within the mobility and healthcare industry. We have 4 employees and a network of 35 dealers within the healthcare

industry which we service. Because of the nature and size of our business any further changes to laws and regulation will have a major impact on our business at a time when we are trying to expand to offer further finance products to the industry and take on more employees to maintain the very high standard of service that we currently operate to. We have recently had the massive financial cost of implementing the Consumer Credit (EU Directive) Regulations 2010 and any further changes would greatly affect our business and our plans to develop and grow in the next 12 months. The financial services industry is already heavily regulated by both English and European law and further change seems to be totally unnecessary.

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.

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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.

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Yours sincerely

Carla Nicholls
Director

CONSUMER PROTECTION & MARKETS ACT
Financial Conduct Authority

RESPONSE to CONSULTATION

A new approach to Financial Regulation

Consultation on reforming the consumer credit regime

FROM

George Wilkinson*
George Wilkinson Associates

TO

financial.reform@hmtreasury.gsi.gov.uk

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

19th March 2011

**This submission is supplemented by a separate document containing a profile of
George Wilkinson**

1.0 Responder

George Wilkinson of George Wilkinson Associates – is a specialist in key operational aspects of consumer credit and has been involved in matters of regulation since the Crowther Report - and the associated drafting of the original Consumer Credit Act many decades ago. (Please see his profile – provided under cover of a separate email). Crowther fully noted the complexity of consumer credit – and was instrumental in its development and regulation and its mainly legal basis.

George Wilkinson is pleased to be able to respond to the recent consultation on **“a new approach to financial regulation: consultation on reforming the consumer credit regime.”** I am sure that there is awareness that large organisations with many specialist staff will be able to produce more detailed responses. I trust I will be able to get to the essence here.

2.0 Government preferred option.

I understand and am concerned that the Governments preferred option is Option 1 based on the Financial Services & Markets Act 2000. This could result in all companies involved in the credit industry, large and small, operating under FSA styled ‘rule -based regulation’. There is little said in independent research documents other than those by the FSA on the pros and cons of rules – and this should have been covered in depth as it is fundamental. I would like to be assured that this is not a ‘done deal’ as I am concerned that premature OFT and FSA changes might be in train.

In fact – such a clearly stated preference or prejudice can inhibit any proper debate of alternatives and give a stilted look to the consultation. Worse still – and given decades of both hard gained and practical expertise and distorted opinions and bias in the reporting of consumer credit – any change should surely be preceded by a convincing and fact based set of arguments for change. ‘Let’s do it because we want to – or it’s a muddle we don’t like – or big is best – or we need one big umbrella to cover everything’ appear to be the arguments.

3.0 Cost cutting context – the expense of the FSA.

This is all in the context of severe cuts backs in jobs – lower economic activity and without a clear definition of what will really be achieved by the bulk of what is being proposed. The FSA - of itself – is huge, expensive and growing in size and coverage. Where is the Treasury vigour that has been applied to quangos – and even to the cost of critical services? And where is the cost justification for such changes?

4.0 Dominance of large companies already with the FSA.

Is it any wonder that larger organisations already covered by the FSA – will settle for the proposed option 1? I would welcome sight of their arguments for and against this option in due course in order to understand their choice. But – in fairness – if an organisation already with investment products, savings, stock market dealings as well as complex banking facilities was considering their separate consumer credit – would they not just agree with the government? Are they discomfited with the OFT?

5.0 The smaller credit provider – unintended impact on competition and choice – market shrinkage

But what about the smaller lender – the specialist consumer credit provider – those providing leases, hire purchase to consumers and to the SME market? In the context of specialist legal aspects and the interpretation of rights and responsibilities for comparatively small (in FSA terms) markets - will rules be enough or adequate?

Will the FSA bother – or is this group likely to fall into the unintended consequences bucket and fulfil an unwitting desire for excessive potential simplification and allowing shrinkage to a few players? This should be seen in competition terms – as it can leave the SME and certain consumers in the hands of the Banks – who by the way are applying heavy weightings to certain sectors/segments within their credit criteria. There could be a large gap in the market. The Competition Commission in its imposition of change in Home Credit has seen the market dominance of a key major player increase at the expense of smaller players. A perverse outcome but changes of magnitude can suit large organisations and fell smaller ones.

6.0 The steady Evolution of consumer credit practise in areas of complexity and product tailoring (Credit cards and current accounts can be considered as simpler in comparison)

Consumer credit has undergone root and branch change over the last 35 years culminating in the Consumer Credit Directive implemented in February of this year. I believe that the current regulator of consumer credit, the Office of Fair Trading has kept up with these and many other developments – and has been provided with the right tools for regulation and enforcement.

These have evolved 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. I 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. If it is not broken – why is there a need to fix it? Putting aside PPI and complaints about bank charges – what are the causes for concern and have these been properly aired and quantified?

7.0 Dangers of carry across thinking and practise from the FSA

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 and refined approach this is unlikely to work. There is a marked difference between credit and savings/deposits. Credit is - where the risk lies with the lender and deposits and saving is where the risk lies with the depositor. I believe compliance costs will increase significantly, and there will be more credit related interventions unless there is a rational approach taken. This will require extra work and potential disruption - under the new regulator, especially for the small credit provider.

8.0 Lack of compelling case for change

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 any that is an SME. I 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.

9. Lending downturns – uncertainty of funds – flexibility and risk taking.

The restriction in the provision of consumer credit by major lenders and their imposition of restrictions and severe conditions has been well documented. Some argue this prevails despite huge government pressure.

In contrast – consumer credit and the provision by the smaller specialised lender has risen considerably in recent decades and enabled consumers and small businesses to access products and services to suit their lifestyles and to develop small and often new enterprises.

As a direct result of the negative impact of ‘the credit crunch’, bank funding to the SME sector in particular has been severely curtailed, resulting in a significant downturn in lending with its consequences on growth and job creation.. 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 and uncertainty about regulation going forward will stifle much needed growth even more.

10 My business is small – small lenders are being squeezed out

I advise many businesses and am a SME myself. Those that I advise are lenders across a large spectrum – but there are clear differences between large lenders with automated credit scoring and policy and exclusion rules and small flexible lenders. These need support and not rules-based oversight. As much lending by smaller providers requires lines of credit from majors – I have noted that many of these are classed as high risk with reduced or even closing down of credit lines. A major US multi-national has had problems raising funds – so small wonders SME lenders struggle.

11 Importance of the SME – as both lender and borrower

Business Innovation & Skills [BIS] in October 2010) showed that the SME accounted for a significant number of all enterprises, private sector employment and turnover. The number of companies and the number of sole proprietorships continue to rise and to grow – and have need for flexible credit. This is especially so for those with a small number of employees. It is worthy of note that the consultation paper highlights that a substantial number of OFT licensed firms are sole traders.

12 Risk of radical change

The proposed new regime will be the most radical change in consumer credit regulation for a generation. I believe that the major changes that consumer credit has gone through in 1974, in 2006 and recently with the implementation of the Consumer Credit Directive should not be changed once again just to fit FSMA 2000.

These changes of themselves need to bed down – to be refined and adjusted rather than turned over. It could be argued that these very proposed organisational changes are a huge distraction and could inhibit and delay really needed changes needed. 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 will apply. This should be seen in the context of - low growth, higher unemployment and severe lending restrictions.

13 Regulatory Standards and Expectations

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 the SME 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 SME 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. This has to an extent already started to happen.

14 Complexity of change for smaller businesses

The changes currently outlined within the consultation paper would be a most complicated and costly change for all parties but for small ones especially. Large numbers of small businesses could be expected to leave the market as about a third that have a 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.

15 Non banks – undertaking consumer credit tasks – as licensed

As you are no doubt aware around 40% of all consumer credit 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.

16. My concerns – in essence

The main areas of concern are -

- *More unwarranted changes* to consumer credit regulation
- Unneeded extension of a *new regime* to *small business lending*
- A costly and unneeded requirement for all existing lenders to re-apply for *authorisation*
- Significantly higher regulatory *fees*
- Uncertainty of the *legal position* on loan agreements
- Further *disruption/cost* to business during handovers and changes
- Lack of *experience* in consumer credit in the new Authority
- Loss of *Trading Standards Authority* experience

17 Consumer Protection – EC Directive – Nature of complaints

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. (If PPI and bank charges complaints are deducted – a more on going picture of complaints should arise.

Companies are concerned about their reputation, and treat consumers with respect and dignity. The risk lie 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 further and more costly monitoring and reporting. Consumers are already well protected.

18 Enterprise – SME – Over-regulation Risk

The Coalition Government are continually stating their declared policy that enterprise and the SME are pivotal in the UK economy to avoid 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.

19. Option 2.

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.

George Wilkinson
19th March 2011

Footnote

Appendix E questions have been considered though not specifically referred to in this response. The bulk of almost 40 of such questions may require proper research and resources to answer fully. This is more likely to be forthcoming from larger participants.

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: Guardian Finance 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 Guardian Finance Limited on “a new approach to financial regulation: consultation on reforming the consumer credit regime”.

Guardian Finance 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 Government's 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 being a self-funding Hire Purchase and Personal Loan finance company serving Leicestershire. We were established in 1942 and are proud to offer personal service at competitive rates to local clients. We are pleased to state that over two thirds of our new business transactions arise from satisfied previous clients. We employ six people all of whom have been with us for many years. Our NEWEST employee having served with us for sixteen years. As well as the accolade of so much repeat business we regularly receive messages of thanks, both verbal and written, from satisfied clients. We have been members of the Consumer Credit Trade Association for many years.

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

Andrew Bent

Director

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: Hertfordshire Savings & Loans 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

22 March 2011

Consultation response from Hertfordshire Savings & Loans Limited on “a new approach to financial regulation: consultation on reforming the consumer credit regime”.

Hertfordshire Savings & Loans 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 Government's 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, as it is a young business based on 4 people and distributing personal loans and leases on a direct distribution basis.

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 guidance notes can supplant detailed regulations 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:

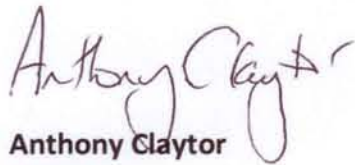
- further unwarranted changes to consumer credit regulation
- the extension of the new regime to small business lending
- a requirement for all existing lenders to re-apply for authorisation for both existing and past business
- significantly higher regulatory fees
- the loss of the certainty of the 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 the lenders outside of the banks, large finance houses and building societies take no deposits. 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

A handwritten signature in dark ink, appearing to read 'Anthony Claytor', with a stylized flourish at the end.

Anthony Claytor
Director



Empowering the credit profession

14 February 2011

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

Email financial.reform@hmtreasury.gsi.gov.uk

DRAFT RESPONSE TO THE HM TREASURY AND BIS CONSULTATION ON REFORMING THE CONSUMER CREDIT REGIME

The Institute of Credit Management is the largest professional credit management organisation in Europe. Its members hold important, credit-related appointments throughout industry and commerce, and we feel it appropriate to comment on this consultation.

The Institute supports the key objectives identified by the government and acknowledges the benefits of a simplified and more cohesive regulatory structure. We have two specific comments, however, that we would urge you to take into account:

1. Under the current regime, when the OFC identifies poor practice it makes details of its concern and action public but does not name the specific organisations concerned citing Part 9 of the Enterprise Act as preventing it from doing so. We do not believe this is helpful for the public nor their advisors.
2. There can be no argument that consumers need a system that affords them effective and appropriate protection but this needs to be balanced against the need to allow creditors effective and appropriate methods of enforcement where a debtor has failed to discharge his payment responsibilities without good reason or cause.

Should you have any queries, please do not hesitate to contact me.

Yours faithfully

Glen Bullivant
Chair of Technical Advisory Committee

Website www.icm.org.uk

Institute of Credit Management

The Water Mill, Station Road, South Luffenham, Oakham, Leicestershire LE15 8NB

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**RESPONSE OF THE INSOLVENCY PRACTITIONERS ASSOCIATION
TO THE HM TREASURY CONSULTATION:
“A NEW APPROACH TO FINANCIAL REGULATION: CONSULTATION ON REFORMING THE
CONSUMER CREDIT REGIME”**

We wish to respond only to 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”**

In deciding whether to grant a group licence, the OFT considers whether the public interest is better served by granting a group licence than by obliging each person/business to apply separately for individual standard licences. We understand that, in applying this public interest test, the OFT considers the administrative time that would be saved in granting a group licence to cover a number of group members compared with that needed to service individual licences for those members; thus, the smaller the number of members a group licence seeks to cover, the less likely it is that the public interest test will be met. We believe that this has the potential to discriminate against bodies with relatively small numbers of members, but which are capable of successfully regulating and monitoring their members' compliance with the CCA.

In addition, whilst there may seem to be little saving in the costs expended in supervising compliance with the CCA in granting a group licence to a body with a relatively small number of members, we believe this narrow view overlooks the advantages of having one supervisor responsible for monitoring compliance of a group that are subject to a number of regulatory requirements. For example, not only do insolvency practitioners undertake some consumer credit licensable activities, but they are also required to comply with other statutory instruments. The IPA is recognised in relation to its authorised insolvency practitioners as follows:

- The IPA is a recognised professional body (“RPB”) under Section 391 of the Insolvency Act 1986 (“IA86”).
- The IPA is also a supervisory authority under Regulation 23 of the Money Laundering Regulations 2007 (“MLR07”).
- The IPA is also a competent authority under the Debt Relief Orders (Designation of Competent Authorities) Regulations 2009.

We note that the professional bodies recognised by the Treasury under S326 of the FSMA are, along with the IPA, designated as RPBs under the IA86 and supervisory authorities under the MLR07. Whilst, in regulating insolvency practitioners, the IPA has had no cause to seek recognition previously under the FSMA, it would seem sensible for the CPMA to maintain a list of recognised bodies for the purposes of regulating the FSMA *and* the CCA (or its successor), which would comprise all professional bodies that are currently recognised by the Secretary of State and HM Treasury as competent to regulate and monitor its licensed members.

In this way, each insolvency practitioner would be accountable to its professional body for compliance with matters arising under IA86, MLR07, FSMA, and CCA. This would seem to be a far more efficient and effective way of regulating and monitoring compliance; not only would there be cost-savings for the government bodies ultimately responsible for supervising the different statutory provisions as the professional bodies would carry out the work directly on its regulated members, but there would be cost-savings for the professional bodies as they would combine their regulatory efforts in relation to all statutory provisions, and this would also result in cost-savings for the regulated members as they would only be accountable to one supervisor. The professional bodies would also be able to use the combined intelligence relating to each regulated member in order to apply an effective risk-based approach to regulation required by all these statutory provisions.

It is the IPA's opinion that the regime for regulating the IA86, MLR07, and FSMA in recognising named professional bodies, rather than considering and processing applications from these bodies for group licences as currently required by the CCA, has proven to be a successful way of maintaining a sound regulatory structure and better reflects the Hampton Principles of Better Regulation. In addition, we are not aware of any difficulties experienced by the Secretary of State or the Treasury in supervising these regimes; these supervisory bodies have successfully set down standards to which they require the recognised professional bodies to adhere and have continuously monitored the professional bodies' compliance with these standards. We consider a similar approach would be advantageous for regulating the CCA (or its successor).

IPA Secretariat
22 March 2011

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

22 March 2011

Dear Sirs,

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

On behalf of ILAG, I have pleasure in submitting the following comments on the above Review.

ILAG is a trade body representing members from the Life Assurance and Wealth Management industries. Our members share and develop their practical experiences and expertise, applying this practitioner knowledge to the development of their businesses, both individually and collectively, for the benefit of members and their customers.

We welcome the opportunity to comment on the proposals, which we consider useful and well written. We have concerns that the Government may be taking too much on. As a consequence, we have not responded directly to the specific consolidation questions but instead have some overarching comments which are noted below and we would be happy to discuss these in more detail if required.

Although Option 1 to create an FSA style regime to replace the existing Consumer Credit regime would appear to be the Government's preferred option, we do not feel that this would work in practice given the manner with which General Insurance has been administered following its regulation.

There are comparisons to be drawn with the debate on mortgage suitability, with the State making decisions which should properly be made by consumers themselves. There has been a number of well-publicised cases where credit has been offered to consumers manifestly incapable of servicing it, but we are unconvinced that the solution lies in a proscriptive, FSA style, regime.

Although the Paper suggests that such a regime must be flexible, regulation thus far has not reflected this aspiration. FSA originally offered assurance that the General Insurance Business regime was to be flexible. Subsequently, however, firms such as garages which offered introductions to motor insurance, and travel agents which offered introductions to

travel insurance were brought into scope. Unfortunately this resulted in many firms withdrawing in the face of the regulatory requirements and consumers losing easy access to insurance.

Yours faithfully

Mark Searle
Administration Team

Jackson Cohen Associates Limited are a compliance consultancy specialising in supporting short term lenders. As such, much of our response is based upon the impact of the consultation on the short term lending industry.

1. Do you agree with this assessment of the consumer credit market?	Yes we broadly agree with the assessment
2. Is this a fair assessment of the problems caused by the way in which consumer credit is currently regulated and issues that may arise as a result of the split in responsibility for consumer credit and other retail financial services?	Yes – particularly with the different formats and requirements for secured loans on residential property, the complexity of the CCA regime and the OFT's less intrusive regulatory methods.
<p>3. The Government would welcome further evidence relating to the consumer credit regime, including in particular:</p> <ul style="list-style-type: none"> • 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. 	<p>Short term lending, commonly known as bridging finance, is, by its very nature, generally required urgently.</p> <p>Much of this lending is exempt from CCA as it is for business purpose, to high net worth individuals or secured against an investment property but often requires firms to obtain the correct exemption certificate. An anomaly is that there is no exemption certificate required if the loan is secured on an investment property.</p> <p>It is quite typical of this type of lending for the amounts required to vary shortly before completion which does not allow time for a new pre-offer to be issued. Indeed, a lot of loans would typically be completed in less than a week.</p> <p>This makes CCA lending generally non-viable, thus restricting consumers access to urgent funds. This has often been a source of frustration to consumers and those seeking to advise them.</p> <p>The general inflexibility and complex rules of CCA carries significant risk for lenders and the investment required in compliant automated systems and expert staff makes it an unattractive proposition. Likewise intermediaries need to understand and have in place compliant systems to sell CCA loans. Many intermediaries find this too much of a burden and lenders are concerned that the actions of intermediaries can be binding on them, reducing the attractiveness of this type of lending.</p> <p>The paperwork required for CCA loans is typically less clear for consumers than that for FSA loans.</p>

	<p>More short term lenders would be more willing to offer secured lending under FSA regulation rules than CCA rules and there is no evidence that consumers would be worse off under FSA regulation than under CCA regulation.</p> <p>Some examples of inconsistencies include: The CCA generally focuses on the purpose of the loan, making business lending secured against a home as a second charge exempt. However if it was a first charge this would be regulated by the FSA. Why should one consumer have the protection of a regulated loan for business purposes just because he has no mortgage (and thus would be FSA regulated) and another consumer not have a regulated loan because he has a mortgage already?</p> <p>A loan secured on an investment property is exempt regardless of the purpose. A loan secured against a home to purchase an investment property would not be exempt unless it was a second charge and the borrower could demonstrate that this was his business. A loan secured on an investment property to buy a home would not be regulated.</p> <p>As loans of less than £25,000 for business purposes are not exempt from the CCA many firms set minimums above this which means customers may have to borrow more than they need. This also impacts further advances which are also often set with minimums above £25,000 in order to save the lender costs and the risks of writing CCA regulated loans. This is not beneficial to the borrower.</p>
4. Do you consider these objectives for reform of the consumer credit regime to be appropriate and attainable?	We believe that these would be both beneficial and appropriate even if only applied to second charge lending. We believe that the business purposes and high net worth exemption should be removed at the same time as the transfer.
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.	<p>We believe that unification should provide the consumer with a simpler and clearer regime. Only having one regulator should also lead to better oversight, especially for those firms currently dually regulated.</p> <p>A removal of the business purposes exemption and high net worth exemption would improve consistency and provide greater protection for consumers.</p>
6. The Government welcomes views on the role of institutions other than the OFT in the current consumer credit regime, and the benefits they may confer.	No comment on this topic

<p>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.</p>	<p>Removing the 7 day cooling off period for secured lending against property should occur when combining the two regimes. This will allow borrowers to access funds for traditional bridging finance.</p> <p>Introduction of the 7 day cooling off period to loans currently under the FSA regime would destroy the viability of the short term finance industry and have a significant negative impact on consumers.</p> <p>The removal of the business purposes and high net worth exemption should take place at the same time. It does not make sense that a second mortgage should not enjoy the same protection as the first. (Lenders do not give borrowers the option of not opting out).</p> <p>Some thought should be given to how to protect consumers against 'gaming'. It is thought that some lenders insist applicants form or use a limited company to borrow through in order to avoid regulation. It is even rumoured that one firm has a supply of ready made firms for applicants to buy.</p> <p>We would urge the CPMA to rely more on the current MCOB regulatory regime than the highly complex and costly CCA regime.</p>
<p>8. The Government would welcome further evidence relating to:</p> <ul style="list-style-type: none"> • the use of consumer credit by small and medium sized enterprises (SMEs); • whether the protections currently afforded by the CCA are appropriate and cover the right groups of businesses; and • the costs and benefits of considering extending FSMA-style conduct of business rules to a wider group of SMEs. 	<p>Generally short term lenders avoid loans to businesses of less than £25,000 due to the complexity and cost of running CCA regulated loans.</p> <p>This can cause a negative consequence for SME's who require a further advance. They may have to borrow over £25,000 to get it as the lender will not offer CCA loans. Even if they are willing to borrow the higher amount it may not be available to them due to lack of sufficient equity to secure the higher amount. This is to the detriment of the consumer.</p> <p>There does not appear to be any logic in applying protection to loans for business purposes based only the size of the loan or further advance being below the £25,000 limit.</p> <p>Consumers who put their home on the line should receive adequate protection.</p>
<p>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.</p>	<p>More short term lenders would be willing to offer secured loans that currently fall under CCA regulations if they were under MCOB based rules.</p> <p>More intermediaries would be capable of advising</p>

	<p>under an MCOB style regime than CCA regime thus providing greater choice and support for consumers.</p> <p>There would be more competition which should lead to better outcomes for consumers.</p> <p>Dually regulated firms could achieve significant cost savings by operating only one scheme.</p>
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 FSMA style supervision should enhance the current CCA regime leading to greater consumer protection
11. The Government welcomes views on the synergies afforded by the current regime in tackling problems associated with the sale of goods and services on credit, and how these might best be retained in the design of a new regime.	No comment on this matter
12. Do you agree that transferring consumer credit regulation to a FSMA-style regime to sit alongside other retail financial services regulation under the CPMA would support the Governments objectives (as outlined in paragraph 1.18 of Chapter 1)?	Yes
13. Are there other advantages or disadvantages that you consider could result from transferring consumer credit regulation to sit alongside that of other retail financial services?	<p>If the business and high net worth exemptions are removed then more lenders currently operating outside of both the CCA and FSA regulations would need to be regulated which would reduce the potential for consumer detriment.</p> <p>Likewise intermediaries operating in the non-regulated space would either have to become regulated if they were not already or see their business opportunities reduced. This would increase the level of consumer protection and help stamp out any bad practices. Regulated firms are likely to be more careful with their non-regulated activities.</p>
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?	<p>Removal of the cooling off period for secured loans would be beneficial in encouraging more lenders to provide short term loans under an MCOB style regime.</p> <p>The removal of the business purposes exemption and high net worth exemption should be made at the same time as the transfer. This would align the two regimes reducing the potential for confusion. It would also stop firms having the ability to 'game' the</p>

	process by advancing a first mortgage for a small amount and then a second 'unregulated' mortgage for business purposes or using the high net worth exemption.
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.	<p>There is a logic in requiring all firms offering secured loans to meet the same standards and comply with the same rules of business.</p> <p>Non-secured lending may require some additional checks and balances given the often vulnerable nature of the borrowers but this should be able to be built into the new regulations.</p>
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.	<p>Whilst the costs will be an important factor the bigger issue is likely to be how easily and quickly firms that are not already FSA authorised can transfer to the CPMA and what support may be offered to come to terms with FSA requirements.</p> <p>This is important given that firms in this position will not necessarily have all the background information on historic consultations and reports on topics such as TCF and may need some clear guidance and pointers.</p>
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	No comment

the implications an appointed representatives regime might have for firms and consumers.	
20. The Government welcomes: evidence relating to experiences of the current group licensing regime; and views on how the professional bodies regime might be adapted for different categories of consumer credit activities.	No comment on the current regime.
21. The Government welcomes views on the extent to which self-regulatory codes might continue to deal with aspects of lending to consumers and small and medium enterprises.	These could be incorporated into the treating Customers Fairly requirements
22. Do you consider that there would be a case for deregulation of certain categories of consumer credit activity in the event of a transfer? Please explain why.	Rather than de-regulation, we believe that the high net worth and business purposes exemption should be removed.
23. Are there other ways in which the design of a new consumer credit regime based on a FSMA-style framework might ensure a proportionate and effective approach?	No comment
24. The Government welcomes views on how the treatment of agreements already in existence could be approached.	<p>Short term lenders would find this aspect relatively easy to cope with given that agreements are for less than 12 months and could be run off of the books in existing format.</p> <p>We see the benefit of one regime being only having to run one system and logically loans should thus be transferred to the new basis. Running two systems side by side for a lengthy period would not be beneficial.</p> <p>The key is to ensure consumers do not lose any key rights, but repealing of the regulations could reduce administrative burdens.</p> <p>A 3 year transitional period should be long enough for firms to complete transfers. An option should exist for any firm not wishing to transfer or able to meet the new CPMA requirements to continue to run off their book but not write new business under CPMA supervision. It is worth noting that not all firms may be able to meet CPMA proposed requirements for capital adequacy.</p>
25. The Government welcomes views on: <ul style="list-style-type: none"> • how existing licensees could 	Those with current FSA permissions in this area should not be required to change their permissions to offer second charge loans.

<p>be dealt with; and</p> <ul style="list-style-type: none"> • factors that should be considered in determining whether a modified approach could be adopted for particular categories of licensed firms. 	<p>Those who only have CCA licensing will need to prove they meet the standards applied for Home Finance Arranging so must apply.</p> <p>We believe careful consideration will need to be given to how to cope with and assist firms, particularly small lenders, in getting authorised under an FSA style approach. It seems unlikely that any shortcuts could be offered if firms given the current FSA view on lenders as being high impact.</p> <p>If the Government removes the high net worth and business purposes exemption there will be a significant number of lenders who are not currently FSA or CCA authorised who will need to apply for authorisation. (There are currently over 70 short term lenders operating in the market).</p>
<p>26. The Government welcomes views on key factors that would need to be considered in transitioning from the current to a new fee structure.</p>	<p>No comment</p>
<p>27. Are there other factors the Government should take account of in considering transitional arrangements?</p>	<p>There is a need to find a basis for firms to run off their loan books if they do not want to sell new business under the new regime.</p> <p>Some form of limited licensing should be available at reduced cost and simpler process although supervision will still be required.</p>
<p>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.</p>	<p>The original application process was far more simpler than the current process for home finance providers.</p> <p>Many small firms would struggle to cope with the intensity and minutia of detail required in the current process. Small firms running successful businesses for many years may not have the experience and ability to write the extensive scenario modelling and business planning currently required. This could result in firms having to spend a lot of money on external consultancy.</p> <p>It would be beneficial if existing firms only had to provide accounts, basic projections (no modelling) and details of systems and procedures to meet the CPMA requirements.</p>



Registered in England
No. 561912

JAMES SMITH & SON (Music Sellers) LTD.

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Fax: 01704 579019

Registered Office: 42-46 STATION ROAD . AINSDALE . SOUTHPORT . MERSEYSIDE . PR8 3HW

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: James Smith & Son(Music Sellers)Ltd

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

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114 MANCHESTER ROAD
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PR9 9BJ
Tel. 01704 531854

also incorporating SuperVision, 101 Shakespeare Street, Southport . 01704 514744

Consultation response from James Smith & Son (Music Sellers) Ltd on “a new approach to financial regulation: consultation on reforming the consumer credit regime”.

James Smith & Son (Music Sellers) 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 retail, hire, and offer credit terms on Electrical Goods to consumers through six retail premises. We employ 24 staff in the operation and have traded for over 30 years in the local communities we serve.

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

A handwritten signature in dark ink, appearing to be 'R G S Wright', written over a light blue circular stamp.

R G S Wright
Managing Director

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: Kingsway Finance & Leasing plc

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 Kingsway Finance & Leasing plc on “a new approach to financial regulation: consultation on reforming the consumer credit regime”.

Kingsway Finance & Leasing 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 Government's 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 as we have 11 employees and we are engaged in the supply of credit and hire to other SME’s throughout the mainland UK to assist them in acquiring business essential assets such as IT Equipment.

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
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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

A J ANTHON
MANAGING DIRECTOR

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

21 March 2011

By first class post and email: financial.reform@hmtreasury.gsi.gov.uk

Tel No: 0113 225 7796
Fax No: 0113 216 7289

Dear Sirs

Leeds Building Society's response to the consultation on reforming the consumer credit regime

This letter sets out Leeds Building Society's response to the consultation on reforming the consumer credit regime.

Leeds Building Society is the fifth largest in the UK with assets of circa £10 billion, with over 680,000 members and employs 900 staff in 68 branches in the UK and 2 in Europe.

1. General Comments and Key Points

The Society has had the opportunity to consider the Building Societies Association's (BSA) response to this consultation, which we support. We would, therefore, invite HM Treasury to consider the BSA response and we refer HM Treasury to the BSA response in relation to the specific questions raised by the consultation, rather than repeat the points made by the BSA in their entirety.

2. Key Observations

- The Society agrees that there may be inefficiencies and overlap between the roles of the OFT and the FSA and therefore, it would, in principle, appear to make sense to transfer responsibility from the OFT to the FSA. However, the fact that consumer credit legislation has been the subject of much reform in the last few years is an important consideration and the consumer credit industry, consumers and regulators would benefit from a period of consolidation, rather than further disruption.

- The proposal to move responsibility to the OFT also comes at a time when the FSA's responsibilities are also the subject of change and reform. Therefore, it may not be prudent to expect a new regulator, during its initial period of consolidation, to take on such a major, complicated piece of work. Firms are also likely to be affected by the changes brought about by the changes to the FSA and therefore, it would not be appropriate to expect firms to deal with any further changes to consumer credit legislation at the same time.
- We also note that the Regulatory Policy Committee has described the analysis of potential costs and benefits of the proposed change as "incomplete". For that reason, we consider that it would make sense to install the regime that will replace the FSA and allow a reasonable opportunity to consolidate before addressing the possibility of repealing the existing consumer credit legislation. This should also enable a clearer picture to be obtained of costs and benefits.

Yours faithfully

Jennifer Young

Jennifer Young
Solicitor
Legal Services

CONSUMER PROTECTION & MARKETS AUTHORITY
[Financial Conduct Authority]

From: Leisure Finance Plc
16 Davy Avenue
Knowlhill
Milton Keynes
MK5 8PL

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

18th March 2011

Consultation response from Leisure Finance Plc on “a new approach to financial regulation: consultation on reforming the consumer credit regime”.

Leisure Finance 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 Government's 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 provide small regulated loans of up to £1,000, but more typically around £350-£500, to finance annual Health and Fitness Club membership. These loans are often free to the borrower with the service provider paying a small monthly fee instead. We employ 28 staff and have been conducting this type of business since 1976.

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

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22 March 2011

Dear Sir

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

The Lending Standards Board (LSB) welcomes the opportunity to respond to the Treasury and Department for Business, Innovation and Skills' consultation document - 'A new approach to financial regulation: consultation on reforming the consumer credit regime.'

The LSB is the successor body to the Banking Code Standards Board (BCSB) and is the independent, not-for-profit company that monitors compliance with and enforces the provisions of the Lending Code. This is a self-regulatory code of practice, sponsored by the British Bankers' Association, the Building Societies Association and The UK Cards Association, covering conduct of business in respect of personal customer current account overdrafts, unsecured loans, credit and charge cards and lending to micro-enterprises and charities. All major providers of these products subscribe to the Code. A majority of the directors of the LSB are public interest representatives. The LSB is not a trade association or representative body.

The credit provisions of the former Banking and Business Banking Codes were transposed to and reinforced in the Lending Code which was launched in November 2009 and this Code is subject to essentially the same monitoring disciplines as conducted by the BCSB. The Code does not regulate commercial matters such as rates of interest or the level of charges, and does not cover store cards.

Our response is attached and we would be pleased to meet with you to expand upon this if it would be of assistance. Further background information on the Lending Code and the LSB is included as an appendix to our submission.

Yours faithfully



Robert Skinner
Chief Executive

**A new approach to financial regulation: consultation reforming the consumer credit regime.
Response of the Lending Standards Board**

Summary

The LSB considers that the interests of consumers would be better served if there were a single statutory regulator for all retail financial services, including consumer credit. The current split in regulation between the FSA and the OFT has led, as the consultation document notes, to a lack of coherence in consumer protection and a degree of regulatory overlap, resulting in confusion for both consumers and firms.

Whichever regime is chosen as the preferred route to regulatory reform, and we recognise that there could be variants on the two options outlined in the consultation document, the LSB strongly believes that the target regime must be at least as strong as the sum of the current constituent parts. The regime must also be capable of covering all financial credit, so that there is consistency of approach and all borrowers receive similar levels of protection. Following from this, we feel that there is a potential role for a continuation of industry codes in the regulation of consumer credit. We believe that complementary self-regulation, underpinning the statutory regime, should not be dismissed until there is confidence that other solutions will achieve a better outcome.

1. A single statutory regulator

The LSB believes that there should be a single regulator providing statutory oversight for all retail banking products across the full product life-cycle including debt collection and debt sale. The existing split between the FSA and the OFT can lead to a blurring of responsibilities leading to regulatory overlaps and in some cases underlaps or gaps, inconsistencies in approach to different retail banking products and a lack of clarity for consumers over ultimate regulatory responsibility.

In addition to the regulatory inconsistencies mentioned in the consultation document, which include the treatment of current accounts which are regulated by the FSA if in credit but the OFT if overdrawn, the LSB would draw attention to the following instance of apparent duplication or inconsistency of regulatory approach:

- the operation of the banker's right of set-off (ROSO) is subject to regulation by both the FSA, which has responsibility for accounts in credit, and the OFT which, via the CCA, regulates the loan or credit card to which any credit balance will be applied. The LSB issued guidance to firms on the fair use of set-off early in 2010 (see below).

The current split in regulation between the FSA and the OFT arguably increases the costs of regulation for firms, because of the need to satisfy two different sets of requirements and risks gaps and inconsistencies in regulatory coverage. Those costs and overheads will be passed on to consumers in the form of increased charges and higher or lower interest rates (for borrowers and savers respectively).

From the consumer's perspective, the extension of the compulsory jurisdiction of the FOS to encompass consumer credit has already provided the significant advantage that the consumer does not have to worry about which body is responsible for regulating the financial product in respect of which they have a complaint, as most retail financial services are now within the FOS's remit and there is a one-stop shop for consumer complaints.

2. Consistency of approach

The LSB would be concerned if the new regulatory structure provided a lesser standard of consumer protection than the sum of the current parts of the regulatory regime. It would not, in the LSB's view, be appropriate for example, for the move to a single regulator for retail financial services to be accompanied by any diminution in the level of compliance monitoring of credit providers or reduction in the level of business standards expected of firms. Additionally the LSB believes that consumers should receive similar levels of protection regardless of the nature of the loan product, be it a credit card or a payday loan. There is currently a fragmented and inconsistent approach to the regulation of retail lending products. Whilst all are subject to the statutory provisions of the CCA, depending upon the product, there are varying degrees of additional protection afforded to consumers by industry codes, some but not all of which are subject to independent monitoring and enforcement.

3. The role of industry codes

The LSB believes that, depending upon the target regime that is agreed upon and the scope and level of prescription in the statutory rules, there could be benefits for both the consumer and industry in maintaining industry codes of practice. They would allow the industry to set business standards above those required by legislation, provide detailed guidance on conduct of business beyond the level prescribed in any statutory rules, and retain the ability to address emerging issues of consumer detriment speedily and effectively, without the delay often associated with statutory changes.

Whilst it is certainly the case that the FSA is able to promulgate changes to its rules and guidance more quickly than changes can be made to the CCA and its associated regulations, it can nevertheless take some time for changes to the FSA Handbook to be made.

The changes made to BCOBS to address concerns in relation to the operation of the right of set-off were first consulted on in July 2010 (having been the subject of discussion with the LSB for at least nine months before this) and were finally published at the end of February 2011. The LSB has also addressed the issue of set-off and issued minimum standards for firms on 2 February 2010 with an implementation date of 1 May 2010. During the period of September to November 2010, the LSB undertook a themed review to assess the degree of industry compliance with the minimum standards. The results of that review were published on the LSB's website on 27 January 2011.

One risk inherent in moving to a single regulator is the danger of creating a vast monolith that is too large and cumbersome – and therefore incapable of reacting swiftly to issues of consumer detriment as they arise.

Codes of practice can be tailored to cover particular products or markets and could help to avoid the need for the very substantial and detailed rule book that might be necessary to cover all consumer credit products, ranging from those currently covered by the Lending Code to payday loans and home credit, and the full product life cycle, including debt collection and debt sale.

The LSB believes that the interests of consumer protection can be, and are now, well served by ensuring that any industry code is subject to independent monitoring and enforcement in order to ensure the integrity and credibility of the code. Recognising the problem of differential standards referred to in 2. above, the LSB believes that if the benefits of complementary self-regulation are accepted, it could, perhaps through some rationalisation of the various current industry codes and their governance, operate in a way that ensures all customers receive appropriate levels of protection, regardless of the nature of the financial product they hold.

If the current monitoring levels and/or business standards cannot or will not be carried forward to the new regulatory regime, the LSB believes that provision should be made to ensure that these elements continue to be addressed via the medium of independently monitored industry codes of practice.

4. Transition

The LSB believes that it is imperative that during the transition to the new regulatory regime there is no diminution in the level of consumer protection afforded by the elements operating under the current regime, including the Lending Code. Of equal importance in the view of the LSB is the need to ensure that in the period in the run up to the introduction of the new regulatory regime there is no 'regulatory planning blight' and that where issues are identified that are not adequately dealt with under the current regime, they are addressed promptly.

The Lending Code self-regulatory regime

The Lending Code contains detailed minimum standards in relation to the provision and operation of current account overdrafts, personal loans and credit cards, with particular reference to credit assessment and the treatment of customers in financial difficulties. These standards supplement the statutory provisions of the CCA and benefit from the compliance monitoring and enforcement regime of the LSB. These standards are capable of being updated quickly when necessary to address emerging issues of consumer detriment, in contradistinction to the time taken to amend statutory rules.

The LSB's monitoring regime includes themed reviews, specific investigations and the review of annual statements of compliance submitted by each Code subscriber. Where instances of non-compliance are found, the LSB ensures that appropriate remedial action is taken in a timely manner. In the case of material breaches of the Code, principally where there is actual or potential consumer detriment, formal enforcement action, including the issue of public censure, is taken.

Recent themed reviews have been undertaken on firms approach to supporting customers in financial difficulties, credit assessment, use of the right of set-off and unauthorised credit card transactions. Summaries of all of these reviews, including areas of actual or potential consumer detriment identified, are available on the LSB website.

Where issues of potential consumer detriment are identified which are not covered by either statute or the Code, the LSB in conjunction with the Code Sponsors can act quickly to address the matter by issuing guidance to firms which in turn will be monitored by the LSB, as part of its ongoing work.

A number of recent improvements in consumer protection resulting from discussion between the LSB and Code Sponsors with BIS/HMT have been or are in the course of being implemented via the Lending Code and accordingly subject to our monitoring and enforcement regime. They include the extension of the breathing space provisions for customers in financial difficulties, new rights for credit card users, new principles for lending to small business customers and rules covering the ability of customers to 'opt-out' from unarranged overdrafts.

These changes, together with new protections resulting from the independent review of the Lending Code which has recently been undertaken, will be incorporated into a new edition of the Code to be launched at the end of March 2011. Subject to agreement with the industry, any new conduct of business standards that may be appropriate as a result of the recent consultation 'Managing borrowing and dealing with debt' could also be implemented via the Lending Code.

The Lending Code, and before it the Banking and Business Banking Codes, has established itself as an important element of the current consumer credit regulatory regime. By working with the industry and Government agencies, the LSB has played an important role in developing new and enhanced business standards to address emerging issues of potential consumer detriment.

Such changes have been developed and implemented in a timely, efficient and effective manner, in consultation with the industry, Government agencies and the consumer bodies, and without the need for recourse to the lengthy Parliamentary process generally required for changes to the statutory regime.

Consultation Response

Response to HM Treasury / BIS consultation on reforming the consumer credit regime

22 March 2011

Introduction

Local Government Regulation is part of the Local Government Group. We promote quality regulation to councils in the areas of trading standards, environmental protection, streetscene, licensing and gambling, food hygiene & standards, animal health & welfare, animal feed, health & safety and private sector housing. We offer comprehensive advice and guidance to councils and their partners, disseminating good practice and providing up-to-date information on policies and initiatives that affect local people and local services. We lobby on behalf of councils to ensure that legislation and government policy can be practically implemented. We contribute, with our colleagues in the Local Government Group, to sector-led improvement.

www.local.gov.uk/regulation

For the purposes of this consultation response, LG Regulation is representing all local authorities across Great Britain in relation to trading standards.

Response:

LG Regulation notes the Government's wish to ensure that the consumer credit regime is "fit for the future, flexible and able to keep up with a fast-paced, innovative market", however has a number of concerns about the drive for further major reform before considering whether the changes brought about by the Consumer Credit Act 2006 and the implementation of the Consumer Credit Directive have achieved the improvements which were intended.

Both measures have resulted in substantial changes to the consumer credit landscape in the UK, the first following the consultation "Tackling Loan Sharks – And More!" and the White Paper "Fair, Clear and Competitive", and the second resulting from years of negotiations in Europe to reach agreement on a maximum harmonisation Directive. LG Regulation believes that both have had substantial cost implications for the credit industry and regulators, and questions the rationale for further major reform without evidence of the effects of these recent developments.

Chapter 1

At paragraph 1.16, it is stated that an estimated 16,000 of "96,000 firms regulated by the OFT" are also FSA-authorised. From local knowledge, it is believed that many of these "firms" may be self-employed financial advisers working for some of the larger

life assurance companies who were required by the companies to hold a consumer credit licence authorising them to act as credit brokers for any mortgage introductions. The companies did regard the issue of a licence as a “satisfactory reference” as to an employee’s fitness. These have seldom given rise to consumer complaints, and the majority of their work is likely to be FSA-supervised as the resulting mortgage itself would normally be an exempt agreement under the CCA.

In Box 1.A, under the heading “Supervision of firms”, it is stated that FSA authorised firms have a regular supervisory relationship with the regulator. There is a risk that this relationship becomes too close, and the regulator looks to “tick boxes” rather than take early action when an intelligence-based approach might indicate that is appropriate. It is unlikely that a central regulator could ever exercise the same level of supervision over the larger number of consumer credit licensees compared with those currently supervised by the FSA.

In relation to “Business applications”, it is worth noting that the CCA considers the fitness of the applicant to carry on a relevant business, rather than his capital structure and indemnities etc. In many ways this is more appropriate for a business providing credit to consumers, while the FSA approach is more suited to businesses accepting money from consumers for investment, pensions etc. The OFT is now considering competence as part of the fitness process under the changes brought about under the CCA 2006, and again this appears to be based on a more intelligence-led approach. The introduction of „lifetime licences” also imposes less of a regulatory burden and cost on licensees.

LG Regulation is unclear what the “objectives relating to retail financial services” and “statutory objectives” at paragraph 1.17 refer to. The wide range of businesses covered by the CCA regime does not lend this sector to a “one size fits all” approach to regulation. Equally, in relation to the “Lack of coherence”, is there any evidence that consumers do regard credit and other retail financial services to be a “single product or service”?

It is unclear what relevance the example of “set-off” is, and how this would be different under another regime; if self-regulation in the form of the Lending Code is not working, the regulator may give guidance or take action. If a problem issue is identified, the OFT could issue guidance that it considers it to be an unfair business practice in the same way as it has for “irresponsible lending”.

In respect of “duplication”, LG Regulation is aware of the issue of “dual regulation” where the advertising of some secured loans may fall within both the CCA and FSMA regimes, and therefore obliged to meet the statutory requirements of the Consumer Credit (Advertisements) Regulations 2004 and the FSA’s MCOB rules, however there is little evidence of confusion, and joint advice has been issued by OFT and FSA. Joint guidance has also been issued on “sponsored links”, where self-regulation by the ASA also has a role to play. LG Regulation is unaware of duplication in the form of “overlapping data requests or investigations”.

The fact that the CCA has remained unchanged for 32 years may reflect its success as a regulatory framework with subsidiary orders and regulations, rather than grounds for criticism. A body of case law has been established which helps to provide some certainty for businesses, consumers and regulators. The recent implementation of the Consumer Credit Directive has brought a number of changes

and given greater flexibility in some areas, such as in the form and content of credit agreements, but less in others, such as the detailed pre-contract requirements. The Directive's requirements are unlikely to change in the immediate future, which should allow business a period of stability. In addition, the original Credit Directive was modelled to a considerable extent on the CCA and many of the same protections have been continued and updated in the current Directive.

LG Regulation is not aware of any evaluation of the changes to the licensing regime introduced by the 2006 Act, to judge how effective they may have been. Revocation or refusal of a licence was previously the only measure available to the regulator, which in the case of a national company might be disproportionate to deal with a problem at a local branch. The ability to seek information and impose requirements under sections 36B and 33A provide the regulator with a more flexible and measured „toolkit“.

LG Regulation does not dispute that the legislative process is cumbersome, but wonders what deregulation is anticipated to benefit both business and consumers.

Box 1.B Consultation Questions

Q1. LG Regulation considers the assessment of the consumer credit market is very generalised, and does not take account of the wide range of credit products, ancillary activities such as debt collection, debt adjusting, credit brokerage, credit information services, or problems experienced at local level by consumers. The assessment concentrates on the regulatory aspect which is not at the heart of the regime. This is the protection of the individual consumer in their transactions involving credit. The assessment of the consumer credit market in 1.8 contains points which could be in need of clarification. Reference is made to secured lending being only mortgages and this is not the case. CCA has references to loans being secured on property but is the assumption being made that secured means houses? Hire purchase and conditional sale agreements are secured on the goods being bought.

The consumer credit products listed have all been about from a number of years and the changes may have been the increase in some or all of these in monetary terms as apposed to the credit products themselves. However cheque cashing cannot in any way be considered a consumer credit product in terms of the CCA regime. It is a service offered to those who may receive payments by cheque but do not have a bank account to pay in to. There are no loans involved only a charge, sometimes considerable, for the service.

Reference in 1.9 to the increase in pawnbrokers. The report referred to gives the figure as a best estimate and it is questionable how many of these actually engage in the main in pawnbroking. A check of "pawnbrokers" in Norfolk in 2009 found despite claiming to be pawnbrokers the vast majority of such businesses operated sale and buy back agreements which are outside the remit of CCA. It would be acknowledged that this could be an indication of an increase in sub-prime lending.

It was noted in the comments in the report about the methodology used that many telephone contacts were not possible due to unobtainable numbers. Whilst there is no real evidence such problems may be a symptom of people not wanting their real identify know such as in the pawning of stolen goods.

In 1.14 reference is made to Trading Standards Services (TSS) and their role. For the vast majority of consumers this is the face of Consumer Credit and their work has helped many thousands of consumers.

Few TSS have had the need to resort to prosecutions under CCA and it would be fair to say Consumer Credit issues have not generated the level of enforcement/awareness as some other issues within some TSS. This is partly due to the national context/policy issues discussed above and, particularly, in the area granting of and revoking of Consumer Credit Licenses (OFT). The ability to regulate a trade sector via licensing conditions is potentially a powerful weapon but concerns about the effectiveness of this system has resulted in many cases to more costly and time consuming ways of dealing with a problem trader by TSS.

Q2. LG Regulation considers the assessment of the regulatory landscape to be reasonably fair, but does not necessarily believe that the split in responsibility is detrimental to either business or consumers. Both regimes provide consumers with information as to where they need to go for help. The split does mean some businesses may have to work under two regimes but the regimes deal with fundamentally different financial products and to some extent customers. The strength or not of self-regulation come down to the individual organisations and how they deal with their members. Consumer protection remedies may be lacking.

Q3. The CCA has eliminated many of the risks that consumers could face. However one area which does continue to cause problems is the mis-selling of insurances to cover credit agreements. These can be often not required and there are often questionable verbal claims which the consumer can be hard put to prove.

Also the deferring of the credit agreement over a period of time which allows the consumer to pay the cash price (sometime with a small fee) by a certain date, often a year from acquiring the goods and thus getting in effect an interest free loan. The time period is such that consumers may forget to pay and find themselves having to pay considerable interest.

Key elements of CCA are the provision of copies of agreements, limiting automatic repossession of goods, steps a creditor is required to take in the case of default, equal liability for creditors for suppliers breaches of contract, and fundamentally the fact that if the provisions are not fully followed it is a creditor who has to take court action to enforce the agreement which may well not be successful.

With regards to rogue traders, civil law is only productive way for consumers to enforce individual cases. Traders may be out of business. Consumers may lack evidence. The average consumer can be easily confused by the credit regulations and methods of enforcement.

Advice and enforcement often come from separate bodies, for example, the OFT will issue consumer credit licences and publish a leaflet on whether you need one or not but will not answer individual queries from businesses as to whether they need one. The financial ombudsman is a good service however only in terms of redress not enforcement.

A quick analysis of complaints received by one Trading Standards Service since 1 January 2009 shows that they received 88 complaints coded „hire and unsecured credit“ and 159 coded „ancillary credit business“. These include complaints about selling methods and misleading information, debt collection activities, e.g. harassment and repossession, credit refusal, PPI, early settlement, loan scams e.g. fee paid but no loan, withdrawal from agreements, guarantor issues, failure to return deposits, brokerage fees, default disputes, failure to settle finance on trade-ins, unsolicited credit cards, identity fraud, debt management and credit repair scams.

Some specific examples from another TSS illustrate the types of risks faced by consumers:

Example 1: Debt Management firm and the need for local enforcement

Trading standards received complaints from local debt advisers about the activities of a local debt management firm. Officers investigated the complaints and visited the business. There was evidence of misleading activities and an apparent lack of competence by the individuals involved. Trading standards made it clear that a failure to meet the OFT's Debt Management Guidance could lead to action by the OFT under the consumer credit licensing regime. The outcome was that the business ceased to operate as a debt management business, and local consumers were protected from misleading claims and poor service from this firm. This was a small local firm and best dealt with by local enforcers. OFT were prepared to take action if necessary but needed the evidence from the local investigations "on the ground" by Trading standards.

Example 2: Debt Collection: Scottish dimension (DAS) and effective work by home and enforcing authority

A debt counsellor complained to a Scottish Trading Standards Service that the debt collecting arm of a large national finance company was contacting one of his clients by phone and by letter, despite that client being subject to a "Debt Arrangement Scheme" (DAS) order. The DAS is a formal procedure for Scottish debtors which prohibits such contacts from the debt collectors and the company had been informed of this in writing. These activities were deemed to breach the OFT's Debt Collection Guidance, and there were further breaches of the guidance in terms of the inapplicability of terminology and procedures used in letters and the bypassing of "appointed representatives". The Scottish TSO investigating contacted the home authority TSO for the company and provided the information (including an explanation of the operation of the Scottish DAS system) for the home authority officer to approach the company. After the home authority officer visited the company, it agreed to change the way it dealt with this debtor and review its procedures vis a vis Scottish debtors to take account of the possible involvement of DAS requirements. Had the company not responded positively, the matter would have been referred to the OFT for possible formal action under the credit licensing regime.

Example 3: Debt Collection: bad practices by local debt collection agents; importance of credit licensing system

Ongoing case in Scottish city where two local agents of a medium-sized debt collection firm have been the subject of several complaints to Trading Standards.

The agents were repeatedly accused of making overly-frequent phone calls and visits to debtors who also felt intimidated and harassed by their aggressive attitude during these calls and visits. The agents also repeatedly contacted the debtors' employers and former employers. The case is being treated as a potentially serious breach of debt collection guidance which brings into question the fitness and appropriateness of these individuals to be involved in debt collection. On conclusion of the investigation a report will be sent to the OFT.

Example 4: "Log Book" style Loans: Scottish dimension and need for local enforcement; effective joint working with OFT; need for "unfair relationships" provisions

National company offering so-called "log book loans", which are effectively based on security on the debtors' cars. This security is unlawful in Scotland. The company targeted individuals with poor credit ratings and as it was seen to be "taking advantage" of consumers in vulnerable situations, it was deemed to be contravening the "unfair relationships" provisions in the credit licensing regime. After receiving a number of complaints, Trading Standards conducted a thorough investigation and took a number of statements from consumers. Regular contact was maintained with OFT and the completed investigation was passed to the OFT. OFT took action to revoke the credit licence and a tribunal hearing is pending.

Example 5: Section 75 and apparently established and reputable firms

There are many examples of s75 providing useful protection to consumers. One "angle" is to particularly point to situations where a reputable and well-established retailer of large and expensive items goes out of business, e.g. Landmark Furniture Co. The point being that whereas there may be an element of "buyer beware" regarding consumers buying from e.g. on-line ticket sellers of unknown probity, customers of Landmark could have had no reason to predict what happened and particularly "deserved" the protection of s75 if they bought on credit.

Example 6: Section 75 Examples

The following refunds are a small sample of recent examples of refunds made by credit card companies under Section 75 after the trader had refused to refund the consumer. These refunds were only made following intervention by Angus Council Trading Standards on behalf of the consumer.

- £1500 refund for quad bike that was never delivered.
- £2800 refund for an alarm system. Misrepresentations had been made during sales visits.
- £510 refund for faulty washing machine.

Examples of debts written off or loans cancelled following investigation and intervention by Trading Standards (within last 2 years)

All of the following refunds/write-offs were made following interventions by Angus Council Trading Standards. In each case the trader had initially refused to offer a remedy to the consumer's complaint. It was only once Trading Standards

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become involved and wrote to the trader and/or lender that the complaint was resolved. There is no doubt that a trader will often be forced into offering a remedy when Trading Standards become involved. This can result in the lender putting pressure on the trader who will take action they might not otherwise have taken to preserve their relationship with the lender.

- £4477 loan for double glazing written off for a Polish couple who had been misled into borrowing to have new windows fitted to their Council House.
- £1500 loan for a door canopy cancelled after it was found a vulnerable adult with learning difficulties and adverse credit history had been subjected to inappropriate sales visits.
- £10,000 loan for a training course written off after it was shown the agreement was not enforceable.
- £2,750 loan cancelled after the agreement was found to be improperly executed and unenforceable.

Example 7: Enterprise Act

The Consumer Credit Act 1974 as amended is specified legislation for the Enterprise Act 2002 and civil and criminal infringements of the 1974 Act are actionable by the OFT and Trading Standards who are designated enforcers under the 2002 Act.

This is an important enforcement tool that improves consumer protection by giving enforcers powers to obtain court orders against businesses that do not comply with their legal obligations to consumers. The consultation process also allows traders to be brought into line without the need to resort to court action.

The Enterprise Act 2002 has provisions that allow swift action to be taken against individuals and businesses that move location or change their name in an effort to evade enforcement action.

The Consultation does not explain how this important area of consumer protection would be maintained under Option 1.

Example 8: licensing

Licensing is a useful consumer protection measure as it excludes those from the market who are found to be unfit or lack competence; the fitness test in section 25 may deter those who know they are unlikely to be granted a licence and also encourages existing licensees to act fairly towards their customers. The fact that agreements with an unlicensed lender or broker may be unenforceable without validation by the OFT also helps protect consumers.

Example 9: advertising

The controls on advertising help to ensure „truth in lending“ and that consumers are given the information they require to decide on different credit offers; the regulations also help to maintain fair competition between advertisers.

Example 10: formalities

The pre-contract and contract formalities are largely dictated by the Credit Directive, and seek to ensure that the consumer is given an opportunity to consider their commitment before and at the time of entry into the agreement.

In many cases where vulnerable consumers have been targeted by high-pressure sales techniques, the consumer has been persuaded to sign a credit agreement for the product or service; often, the trader is reluctant to leave much paperwork to enable the consumer or his/her relatives to consider the contract or exercise their cancellation rights. Where this has been brought to TSS attention, particularly at an early stage, TSS have been able to provide appropriate advice or contact the trader or creditor to have the contract cancelled or amended. In one particular incident, a couple were helped to cancel a double-glazing contract which they had been pressured into signing and could ill-afford, when it was found that the finance company's documents did not include the correct cancellation notice.

Example 11: cancellation rights

The cancellation provisions, now superseded by the Directive's right to withdraw from the credit agreement allow the consumer an opportunity to reconsider after signature.

Example 12: Crowther Committee recommendations

Section 75 is one of the most important consumer protection measures in the Act, and brought into law the policy recommendation of the Crowther Committee that creditor and supplier should have joint liability for any misrepresentation or breach of contract on the part of the supplier. As Lord Hope of Craighead observed in the House of Lords judgement in the OFT case against Lloyds TSB and other banks "Transactions of that kind are to the commercial advantage of the supplier and the creditor. The creditor is in a better position than the debtor, in a question with a foreign supplier, to obtain redress. It is not to be assumed that the creditor will always get his money back. But, if he does not, the loss must lie with him as he has the broader back. He is in a better position, if redress is not readily obtainable, to spread the cost. He is in a better position to argue for sanctions against a supplier who is not reliable. For his part, the debtor is entitled to assume that he can trust suppliers who are authorised to accept his credit card."

TSS find that involvement of the creditor can often assist with the resolution of a consumer complaint where the supplier has previously refused any redress. This avoids the need to commence potentially costly and time-consuming court proceedings.

Example 13: copy agreement provisions

While the right to information and a copy of the agreement under sections 77 and 78 have been abused by some debtors and claims management companies, they nevertheless provide an important element of consumer protection in providing consumers with essential information.

Example 14: default procedures

Default procedures and those relating to the protection of goods supplied under hire purchase agreements ensure that the consumer is given information and an opportunity to remedy the default within the time allowed without a detrimental effect on his credit rating, which can have severe implications for his ability to obtain mortgage or other credit.

Example 15: early settlement rights

The rights to a rebate on early settlement, and the provisions relating to termination of hire purchase and hire agreements have proved valuable to consumers in allowing them to end contracts on reasonable terms.

Example 16: time orders

Time orders offer a consumer an opportunity to apply to the courts for a breathing space in times of temporary financial difficulty.

Example 17: unfair relationships

the new „unfair relationships“ sections introduced by the 2006 Act allow the court to review the terms and circumstances surrounding the making of an agreement, and apply a number of remedies. The previous „extortionate credit“ provisions had imposed too high a burden on consumers.

Example 18: recovery of brokerage fees

Section 155 entitling consumers to recover brokerage fees is also a useful consumer protection measure. Consumers unable to obtain credit from „mainstream“ lenders are vulnerable to approaches from brokers suggesting that they can arrange a loan for them with a minimum of formalities.

Example 19: criminal offence of unlicensed trading

The criminal offence provisions relating to unlicensed trading have proved to be vital in combating „loan sharks“. In many cases, unlicensed credit activity tends to be through ignorance, if for example a business changes from a partnership to a limited company. Normally, if the partnership was licensed under the Act, the company would be advised to apply for a licence and no further enforcement action would be taken, although if consumers were to complain, they and the business would be informed that the agreements might be unenforceable without validation by the OFT. Any evidence of unlicensed money-lending would be investigated or passed to the Illegal Money-lending Unit with a view to prosecution.

Prosecution would also be considered if a licence applicant were to deliberately conceal information or give false information to the OFT in connection with a

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licence application, if the locus of the offence were considered to be in the local authority's area. Unlicensed debt-collection activities have previously resulted in prosecution, particularly where combined with other offences.

Policy Objectives and Box 1.C Consultation Question

LG Regulation would make the point that the inconsistency in regulatory treatment has in part been due to the differing degrees of perceived risk, for example the possibility that someone might lose their home as opposed to having a court judgement awarded against them in relation to a small unpaid debt.

LG Regulation accepts that there may be a small element of dual regulation, but does not consider that there is real evidence of burdens on business caused by unnecessary duplications.

LG Regulation welcomes reform where it can be shown to benefit consumers and business.

Chapter 2

Objective 1

Any wholesale changes to the CCA regime would be unnecessary and counter productive. Equally there is little evidence that the suggested replacement (CPMA) would present any distinct advantages to business or consumers alike; in fact the proposal as currently stands appears to increase the risks involved.

As indicated above, LG Regulation believes that the inconsistency in regulatory treatment has in part been due to the differing degrees of perceived risk. It is also worth pointing out that the Credit Directive applies to overdrafts, but not to mortgages or secured lending, and therefore the different treatment of these products may persist.

LG Regulation is concerned to note that there is little account taken of the existing role of Trading Standards Services and DETINI and the Illegal Moneylending Units in consumer credit regulation. While the licensing regime and policy at a national level are the remit of the OFT, much work is carried out at a local level, for example to ensure businesses are licensed, and advertisements are compliant, as well as providing advice to consumers and businesses.

Box 2.A & B Consultation Questions

Q5 LG Regulation believes that the first three identified benefits are overstated, but recognises that one regulatory regime might improve market oversight and contribute to financial stability in the way outlined.

Retail Financial services cover such a wide and diverse area and have differing needs and pressures that it would be difficult to see how this could be simply achieved by one regime. There would clearly need to be areas of operation to cover all aspect which could lead to conflicting interests within the one organisation. Markets in relation credit and say investments are so diverse as not to really benefit for a single market oversight.

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LG Regulation accepts that a single regulator could improve clarity and coherence but there are benefits in credit enforcement being dealt with at a local level by local authorities (LAs). The officers concerned have a good knowledge of local businesses, are often contacted for advice by those businesses and already have a profile on the high street and business community due to their other regulatory functions. Trading Standards officers are in contact with businesses and consumers on a very wide range of transactional issues. If there is consideration of a local authority enforcement role ending or transforming into a "notified body" regime, then LG Regulation believes either the LA enforcement role should be retained or there should be a positive obligation on the new markets authority to seek notified bodies among local authorities or CAB. Otherwise while a new regime might deal with some aspects of credit provision effectively, it may not deal with all consumer facing practices. LG Regulation believes there is much to be gained by keeping credit enforcement with a specialist consumer law regulator at a local level.

For example, a recent large case that one council took to court against a problem company under the CPRs is a case in point, where alleged misrepresentations by brokerage companies affect the civil rights of consumers. Any non-council enforcer in this situation would be unaware of these practices which were only uncovered because of the larger investigation on mostly non-credit related matters.

Q6

Whichever organisation gets the role of regulating and enforcing credit needs to have the skills and resources to carry out investigations. They also need to be responsive to the consumer credit market and to individual consumers. We believe the public would like a regulator that can deal with individual complaints and businesses would want a local contact for reliable advice and information.

Trading Standards services play an important role in the regulation of the consumer credit market. First, they provide something that the Office of Fair Trading cannot, namely, local knowledge of trading conditions and of traders' records. This is essential in deciding the best course of action when an enforcement decision has to be made and the easiest way of ensuring that the benefits of this knowledge are not lost would be to retain the role of Trading Standards under any new regime. Secondly, Trading Standards services are more readily available to provide trader advice than a central body such as the OFT or CPMA would be. Consistency of advice is achieved by means of LG Regulation and this could potentially continue but would involve negotiation with the LG Group as LG Regulation ceases trading around April 2011. Thirdly, enforcement against illegal moneylenders is primarily carried out by local Trading Standards Services. To transfer this function to a central body would involve that body in recruiting large numbers of staff who would lack the local knowledge that is so useful in this kind of enforcement. In addition, effective engagement with the problem of illegal lending requires a joined up approach that addresses the problems of poverty that drive people into the arms of loan sharks. Local authorities are far better placed to deliver this than a central regulatory body would be.

Another issue arises in this area. Trading Standards has always had more than one option in pursuing misleading descriptions of credit facilities. Normally, consumer credit legislation would be used but, if there were any advantages in doing so, it has always been possible to use the Trade Descriptions Act 1968, before its repeal, and now, the Consumer Protection from Unfair Trading Regulations 2008. Consideration would have to be given to whether this state of affairs should continue as it could lead to a dual enforcement regime and potential inconsistencies of approach.

As noted above, LG Regulation is concerned to note that there is little account taken of the existing role of Trading Standards Services and DETINI and the Illegal Moneylending Units in consumer credit regulation. A flavour of the work this involves may be gained from the following examples:

a) A few years ago East Ayrshire successfully prosecuted a local trader who was operating under his wife's credit licence supplying mortgages. The trader was found to be charging fees of several hundred pounds for his service and also an indemnity fee of several hundred pounds which he claimed would be refunded after a year but in actual fact was never refunded. In addition, the mortgages supplied by the trader were at a very high interest rate or sometimes not supplied at all. The OFT eventually revoked his wife's licence.

b) A case investigated by Midlothian TS some years ago resulted in a conviction against a company who were carrying on business under an unlicensed name, but whose dubious practices as a mortgage broker were well known in the trade. He would offer to secure a mortgage on good terms for sub-prime borrowers, who had to pay hundreds of pounds in fees, but return with a poor value loan. The fees were not returned. The OFT had an active interest in the case and revoked his personal licence following conviction.

c) The Scottish Illegal Moneylending Unit is greatly concerned that the consultation on the Consumer Credit Regime considers the removal of the licensing regime. This would be particularly problematic for their work given that in general the only offence available is the Section 39 offence of operating without a licence. Although they would welcome some kind of offence for aggravated illegal lending, the straightforward offence of operating without a licence is a matter of fact and much easier to prove for the purposes of a prosecution.

TSS currently work with the OFT to carry out licensing competency visits after appropriate training, and therefore might be considered competent to undertake a similar role under any CPMA regime. The risk of no TSS involvement in consumer credit is the loss of enforcement of the law / rules at local level, and loss of relevant knowledge for the provision of consumer advice. The majority of credit problems tend not to arise at head office level, but with local staff, or ancillary credit businesses including debt collectors and credit brokers such as motor traders.

The current regime where OFT are responsible for licensing functions and some enforcement, trading standards for enforcement and advice, and FSA for certain products is fragmented and has not achieved the desired level of consumer

protection in the consumer credit arena. In particular the current system is not that helpful for consumers trying to seek redress.

The current role of trading standards is predominantly that of supporting businesses by way of advice and guidance with a view to achieving compliance. Trading standards are used to providing advice and interpretation in a definite manner and in a timely fashion. A frequent complaint from businesses is that OFT are not prepared to provide advice or assistance. Whilst businesses have a responsibility to comply with the law, supporting them in order to achieve compliance is normally much more cost effective than needing to take enforcement action.

Consumer credit is a specialist area of law and often businesses that have paid for advice from solicitors have been given incorrect advice, particularly on matters such as the content of adverts or agreements, and unfair terms.

It is easier for the business to seek guidance on the legislation from just one source such as trading standards, but at present if they have some products which are FSA regulated they will already need to be mindful of complying with two sets of requirements which are confusing and at times contradictory, particularly in terms of advertising requirements and warnings.

Enforcement action is something Trading Standards are used to because of their duty to enforce many other pieces of legislation, and the Consumer Credit Act is just one of these and dovetails well with other activities.

In some areas of business, consumer credit is an integral part of the contract with consumers, an example being the new and used car market. Any Trading Standards involvement with business will take a „complete view“ of the relevant legislation. Trading standards will deal with the whole issue, whether providing advice and seeking compliance, taking criminal action or seeking orders under the Enterprise Act. If consumer credit enforcement were taken out of their remit completely this could lead to an equally fragmented approach.

The advice services also provide consumers with assistance in regard to more complex credit complaints and assessment of whether the business has fulfilled its legal obligations in order to enable consumers to seek redress or take further action.

The information trading standards receive from OFT in terms of licence notifications etc can be useful intelligence to enable us to target work generally. Trading standards would want this information exchange to continue.

LG Regulation believes that it would be sensible if there were scope, for trading standards to continue to play an active role and liaise with, and support the relevant supervisory agency in order to achieve the best result for consumers and businesses.

Local trading standards services often in partnership with Consumer Direct is in effect „the face“ of the CCA to the general public, including business. By advice and assistance they can ensure businesses comply with the requirements including the adopting of best practices as well as assisting consumers in

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problems they may have. A vast amount of experience is held with regard to the practical application of the legislation. They offer a local presence to the community and work well with partners locally such as Citizens Advice, and are therefore often a preferred point of contact for the OFT or FSA. Through regional and national groups, they can provide consistency in approach/enforcement of consumer credit issues.

If a better and more effective overall body could be established under the CCA regime this would further enhance the effectiveness of TSS and the contributions they make.

Objective 2

Box 2.C Consultation Question

Q7 LG Regulation considers that it is essential that the consumer protection elements identified in answer to Q3 in Box 1.B above are retained. As many of these have derived from the law and court decisions, LG Regulation is unclear on how this might be achieved in the event of the CCA being replaced by a „rules-based“ regime. As a particular example, section 75 provides for equal liability, but only in the case of misrepresentation or breach of contract which may require to be decided in a court of law.

Unenforceability of improperly executed agreements, and to a lesser extent the existence of criminal sanctions have proved to be valuable elements for the protection of consumers.

The proposals to include powers to impose significant fines, and require consumer redress schemes to compensate consumers would be an enhancement.

Currently If a problem occurs with a CCA regulated loan this can involve large sums of money, normally way over the small claims action limit, and for consumers who may already be in financial difficulty, the prohibitive cost of seeking redress through the court leaves them unable to take further action.

Whilst there is an argument that local-based enforcement and involvement with business will produce the best results, this could also be achieved through a consistent approach from one overall body.

The current licence regime has not been that effective in preventing rogue businesses obtaining licences. The change by OFT to introduce licences and scrutiny which is proportionate to the risk is a move in the right direction. This should be continued and incorporated into any new licensing regime.

It is particularly important that the regulatory authority keep up with changes to services offered in the marketplace and the risks those may present to consumers collectively in regard to their financial wellbeing.

The points made in 1.9 are very relevant in regard to the explosion in the marketplace of products such as payday loans, subprime loans, log book loans, pawn broking, and debt management plans and IVA"s. These are areas which

target those most financially vulnerable. It would be a benefit if any regulatory authority were able to respond and implement new rules quickly in response to changes in the market to provide enhanced consumer protection.

Currently section 56 and Section 75 of CCA provide significant protection to consumers in terms of seeking redress. If CCA were scrapped then there should be an equivalent protection put in place.

Overall, it is difficult for LG Regulation to see how the overall level of consumer protection could be retained. There is already reference to the potential for breaching the new rules as not leading to any enforceability issues with credit matters. However in our view this represents a backward step for consumer protection and effectively a green light for any unscrupulous businesses who wish to take advantage of consumers within such a regime. „Enforceability“ is a key aspect of control in this market and its potential removal suggests that the need for consumer protection has been overlooked. Consumer Protection can of course be achieved in a number of ways, and part of this will include action, in various forms, taken by regulatory bodies against those businesses which are not compliant with requirements. However if there is no equally robust protection for individuals, then the aim will have in part failed. CCA has managed to a great extent to achieve this by putting the onus on the business (professionals and experts in the field) rather than the customer. The CPMA approach changes this emphasis, and past experience has shown that many consumers will not be confident/able to take legal action, and thus will be much more likely to suffer detriment.

LG Regulation feels that consumer protection is best retained and enhanced by ensuring local authority enforcers (i.e. Trading Standards Services) are sufficiently resourced, retain the enforcement function and exercise it at a local level. This brings synergy as trading standards enforcers already deal with a wide range of consumer and business transactional processes, are a trusted and well known presence in local communities and business communities and can more easily deal with credit in the context of the larger marketplace in goods and services.

Section 75 is an incredibly useful tool for the consumer especially in circumstances where traders go into liquidation or where rogue traders take the money and run. This protection should be retained in any new consumer credit regime.

LG Regulation believes the consumer should have the right to a cooling off period on credit agreements. This is necessary due to high pressure tactics used by sales people and also due to the fact that many consumers sign agreements without taking the time to fully read them. By giving seven days cooling off period the consumer is able to give adequate consideration to signing up for agreements for large sums. For simplicity LG Regulation think it would be sensible for this cooling off period to apply where-ever the credit agreement is signed as opposed to the current complicated system where it can vary.

c. LG Regulation believes consumer credit agreements should be as simple and as easy to read as possible. Most consumers are not credit experts. All credit agreements should prominently feature the amount of credit, the interest rate and the total amount of to be paid at the end of the agreement. It should also contain

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what the credit is for, broken down. Most credit agreements do contain this information but it is drowned out by the mass of small print which the consumer doesn't want to read. A simple version with just this information should be provided to consumers and require their signature.

LG Regulation believes that all credit providers should have to fully consider a person's creditworthiness before providing them with credit.

LG Regulation believes a positive licensing system should be retained

LG Regulation believes there should be simpler and speedier mechanisms to suspend or remove transgressing individuals and businesses from the credit market and control practices not in consumers interests.

LG Regulation believes a free market in credit interest rates does not offer adequate protection, particularly for consumers on low incomes or with poor credit ratings. The issue of extortionate credit needs to be reviewed and we would suggest a statutory code of practice could be introduced to set enforceable guidelines/limits for interest rates applicable to particular groups, based on risk e.g. The advertising of loans on TV for relatively small amounts at interest rates of 1000's %, preys on those with low income and the vulnerable, who don't have ready access currently to cheaper credit, and discredits any credit regulation regime and the lending sector generally.

Consumer credit legislation confers a number of rights that are directly enforceable by the debtor in the courts. It would detract from the current level of consumer protection to deprive consumers of these rights and put enforcement in the hands of CPMA. If CPMA decided not to act on a certain issue the consumer would have difficulty in proceeding any further whereas now he or she can choose to take their chances in court. It is a salutary incentive to lenders to get it right to provide that certain errors will render an agreement unenforceable. The incentive would be less if the only consequence were an expression of displeasure from CPMA.

The protection afforded by section 75 of the Consumer Credit Act 1974 is useful but, if the regime is being reviewed, the opportunity should be taken to clarify exactly what is supposed to be covered and to deal with anomalies such as the lack of protection for authorised users on credit cards.

Box 2.D Consultation Question

Q8 Reference is made in paragraph 2.12 to the protection afforded to small businesses under the regulatory regime. TSS have consistently argued that small businesses are just as vulnerable as individual consumers, and have examples of them being „conned“ by salesmen into agreements for computer or telephony systems, photocopiers etc. Because many of these agreements are leasing agreements, they do not benefit from the protection which might be afforded to consumers under a credit agreement by section 56(2), which makes the creditor liable for the negotiations conducted by a credit broker in similar circumstances.

Box 2.E Consultation Question

Q9 LG Regulation recognises the advantages of flexibility, however believes that the framework of the principal Act with subordinate regulations has allowed changes to be made relatively quickly and with the same degree of consultation as might be undertaken under a FSMA-style regime. LG Regulation believes that a level of certainty has been built up since the CCA was effectively brought into full effect in 1985, backed up by case law and that this is welcomed by business and consumers.

A rules- based regime will depend on a number of factors as to its success, not least the extent to which the rules actually cover the day to day activities. High level (generic) rules generally do not assist consumers but instead provide some businesses with room to „exploit“ loopholes. It is the detailed requirements under CCA which have ensured businesses have provided the protections which consumers benefit from, and indeed provide businesses with clarity as to the actions they need to take. They provide consistency. An example is the total charge for credit and the resulting APR calculation. Without detailed rules different business would produce different methods of calculation which would impair consumer choice and lead to consumer detriment. Rules must be detailed to provide both protection and consistency which will benefit both consumers and business.

The ways the rules are enforced or are of benefit to consumers are vital factors. The consultation document does not appear to address this in any detail. Reference is made to the current FSA rule book preventing consumers from taking action, which some may find rather confusing given the need to convey confidence in protecting consumers. It is difficult to believe that a „self-declaration“ type of annual report, sent in by a business, will ensure consumers and particularly vulnerable consumers are protected.

LG Regulation believes that there have to be clear basic rules that all credit providers have to abide by and there needs to be a body who have the power to enforce when these rules are not met, however there is no requirement for the regulation to be as complicated as it currently is. But simplification should not be at the expense of reduced protection for consumers or competitor businesses.

Box 2.F Consultation Question

Q10 LG Regulation is aware of significant fines imposed by the FSA for a failure to comply with its existing rules, and in some widely-reported cases these involve „high street names“, who might be expected to have invested substantial sums in compliance measures. LG Regulation experience shows that many of the problems causing detriment to consumers are caused at local level by credit brokers, such as garages and retailers failing to follow company procedures, or by the actions of debt collectors and other ancillary credit businesses. An FSA-registered mortgage broker was very scathing about the amount of paperwork necessary to demonstrate compliance, but questioned its usefulness when there was little likelihood of an inspection visit. This suggests that compliance may be regarded by some as nothing more than a „tick box“ exercise.

LG Regulation believes that the success or failure of any regulatory body comes down to its attitude to actions which cause consumer detriment. An organisation which is tough with rogue traders and those who breach regulations will help

ensure consumer confidence in the credit market. It must be prepared to act much more quickly than under the current regime to deal with transgressors and practices not in the public interest and suspend and if necessary remove offending businesses and individuals ability to offer credit, engage in the credit market.

The impact of an FMSA approach to regulation on assuring consumer protection has to be looked at in the light of how much power would remain in the hands of local agencies and consumers. For the reasons already set out, an over centralised approach would detract from consumer protection. Conversely, the greater flexibility of the FMSA approach has the potential to increase consumer protection by making it easier to react to new trading malpractices in a rapidly evolving market. What is essential is that an FMSA approach must operate in conjunction with robust joint working arrangements with local agencies such as Trading Standards services to tackle issues such as illegal moneylending.

Box 2.G Consultation Question

Q11 LG Regulation considers that good communication links exist between TSS and OFT, at the stage of licence applications and for consideration of fitness and other issues during the currency of a licence. LG Regulation believes that the local knowledge of TSS about traders in their area is essential for the successful implementation of any regulatory regime, and has no doubt that such relationships would continue in the future.

The simple answer is to leave the protections as they are. The equal liability provisions protect consumers from traders who refuse to help, have gone out of business or are involved in some form of fraudulent activity. The lower financial limit of this liability does prevent abuse of the provision in relation to minor purchases. This should go to ensuring creditors deal with only reasonable traders and provide them with justification to stop business with them.

The databases kept by trading standards and by consumer direct contain a huge volume of information about consumer complaints. This information would inform the regulator as to problem areas and problem traders. A regulatory authority has to react quickly when new issues arise.

Box 2.H Consultation Questions

Q12 While some elements may seem attractive, LG Regulation does not agree that a FSMA-style regime would deliver better regulatory outcomes while maintaining or enhancing consumer protection and dealing with the issues which affect consumers on a day to day basis at the local level. There is a requirement that any new body should regularly communicates with and be responsive to trading standards or else directly receives complaints from the general public.

The objectives could be more easily and less expensively achieved by actions which are contained in the response to item 15 below.

Q13 The advantages and disadvantages are fairly well set out in the consultation. One disadvantage of removing Consumer Credit advice and

enforcement from Trading Standards completely is that there will be a loss of local knowledge and experience.

The success of any new scheme will be affected by how pro-active the regulator is. Will they have resources to take on multiple cases against both small and large companies? Will they have the culture and enforcement skills necessary to intervene to protect consumers and ensure a level playing field for businesses.

Q14 Box 2H Question14

Vulnerable consumers

Trading Standards have a long history of helping vulnerable and marginalised people, providing local advice and support, often visiting people in their own homes.

Trading standards see regular examples of vulnerable people being “befriended” by unscrupulous sales staff who see them as an easy target for repeat business. One example is of a man whose vulnerability was exploited and he was coerced into taking out loans repeatedly for products he did not need. The sales visits were stopped after the intervention of Trading Standards. Without this local action the consumer would be at risk of further sales visits and seen as an easy target for repeat business.

How could this level of support be maintained and developed under Option 1?

Further example of current work with the vulnerable

Angus Council Trading Standards has recently started working in partnership with colleagues in their Social Work Department to assist adults who have been deemed to be at risk from harm under the Adult Support and Protection (Scotland) Act 1987. Risk of harm under these regulations includes financial harm in addition to physical harm.

Angus Council Trading Standards are currently assisting social work with three cases. The cases involve home collected credit and non-status cash loans. There are doubts about each of the client’s capacity to contract or to understand credit terms.

Angus Council Trading Standards believes that the few cases they have seen since being approached by Social Work Department are representative of a nationwide problem and this is an example of an area where only local involvement by Trading Standards staff can help vulnerable adults.

The costings shown are vague at present. If option 1 is adopted then the cost of any new regime to small and medium size businesses should be assessed properly. These are often the businesses where the credit aspect is not their primary function. The current FSA application fees (detailed in 3.25) for sole traders are significantly more than the current credit licence regime. There is a risk that making it too expensive and burdensome for small businesses to be part of the new supervisory regime would potentially reduce consumer choice.

Whilst most credit activities could probably be properly dealt with under a rulebook regime, provided the powers to impose penalty were adequate. The current work done by the illegal money lending team in relation to loan sharks would not be something for which a rulebook approach would be appropriate.

This area of work is aimed at protecting the most financially vulnerable. It requires criminal legislation to deal with hardened criminal activity, and to enable proceeds of crime action to be taken. This should be considered, and if necessary either separate legislation brought in to deal with these activities or parts of CCA should be retained to enable effective enforcement.

Q15 LG Regulation is not averse to change, where it can be shown to improve regulation for the benefit of consumers and business, and would cooperate with whichever body is responsible for the regulatory regime. However LG Regulation believes it is crucial that TSS and the DETINI continue to have a role in consumer credit regulation to address problems and provide advice to consumers at the local level. LG Regulation considers this would be best achieved by the CCA rather than a FSMA-style rulebook.

There is no doubt that some reform of the current position is needed. However for most who are involved in the Consumer Credit sector the real focus should be on issues surrounding national enforcement/policy within the current control of the OFT. Therefore broad support is given to reform or moving the overall responsibility under CCA. However the levels of protection, consistency and certainly provided by the CCA merits retention.

A detailed look at the CCA requirements and the consolidation of its provisions in to one new Act with associated SIs and provisions to react to changes would also be welcomed. It is accepted that there would have to be some form of Ministerial involvement with this but this would increase the accountability to Parliament and UK legislature.

The differences between consumer credit and other financial products would set them apart in terms of their differing requirements but the two regimes can easily dovetail in areas where there is a mutual need. Authorisation could easily cover a number of aspects including consumer credit. Thus in part the licensing provision of the CCA could be encompassed by a CPMA authorisation.

In keeping the CCA regime then there would be the potential of cooperation between the CPMA and local TSS which would mean the CPMA could tap into resources which arguably have been under utilized under current arrangements.

Chapter 3

Box 3.A Consultation Question

Q16 As the consultation recognises, many of the businesses currently licensed under the CCA, particularly motor dealers and retailers licensed as credit brokers, do not consider credit to be their core business. For them, the licensing process as amended by the CCA 2006 is viewed as a „necessary evil“ every 5 years, however the FSMA-style requirements such as that for minimum capital, reporting and the likely level of fees may be viewed as excessive interference.

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For other „high risk“ businesses the competence requirements introduced by the CCA 2006 are considered to have led to a raising of standards.

The approach may well work in relation to larger businesses and much of the focus of this consultation appears to be in relation to such businesses. However many current consumer credit business are small and the approach would increase the burden on these business in terms of time and money. The current CCA regime, with perhaps the exception of the license fee, minimizes costs for smaller business in terms of ensuring compliance. Any wholesale change could add to their costs with little perceived benefit.

Credit Reference Agencies are, for practical purposes, subject to the Office of the Information Commissioner. This seems to work well and to make sense. They are, however, still licensed by the Office of Fair Trading. It would seem logical that they should be subject to whatever licensing regime is decided as best for the rest of the consumer credit market.

Consumer credit, in the sense of actually advancing credit, is the category that, most obviously, could be regulated by an FMSA approach. What has been said earlier in this response is of direct relevance to this.

There is no obvious reason why consumer hire should continue to be regulated in the same way as consumer credit. The supply of goods under bailment is a quite different kind of contract to the advancing of credit, whether or not the credit is to finance the purchase of goods. The terms of hire contracts typically have to account for depreciation in the value of the goods, options to change the goods during the lifetime of the contract and terms on which the contract can renew at the end of its term. Problems with contracts of hire are most often found where the “consumer” is a small business rather than a private individual. The possible advantages of an FMSA approach to regulating credit are not really applicable to hire. There is a good case for a review of how supply by bailment agreements should be regulated. This should involve not just such matters as the supply of photocopiers to small businesses but also the mobile phone market where, typically, goods are supplied by one business but the service with which they are used is supplied by another.

Credit Brokerage covers different kinds of business practice and some seem more suitable for an FMSA approach than others. The kind of business that offers to find loans for consumers and acts as an intermediary between them and the finance companies could be very suitable to be regulated in the same way as the creditors themselves. Conversely, a used car dealer who may deal with a single creditor and has little or no involvement in the credit side of the transaction would be better remaining subject to inspection and regulation by Trading Standards services. If such a trader misdescribed the credit facilities to which he or she was introducing a consumer, this would be a good example of the circumstances where an issue that was nominally “consumer credit” would be best approached using the Consumer Protection from Unfair Trading Regulations 2008. In short, introductions to cash loans would be suitable for an FMSA approach to regulation while other forms of credit brokerage probably would not be.

Such problems as are associated with Debt Collecting tend to relate to harassment and unfair practices. If an FMSA approach to this were adopted, it

would need to be implemented using the resources of Trading Standards. In addition, some debt collecting malpractices are associated with the problem of illegal moneylending where a more traditional enforcement regime is probably necessary.

Debt Adjusting, Debt Administration and Debt Counselling could be suitable for an FMSA approach but account would need to be taken of the varied nature of those engaging in these activities. A one size fits all approach might not work well in these areas.

The provision of Credit Information Services probably would be suitable for an FMSA approach. There would be some interaction with the regulation of Credit Reference Agencies and it may be that the CPMA would need to work in conjunction with the Office of the Information Commissioner in this area.

Box 3.C Consultation Questions

Q17 LG Regulation is concerned that the level of fees should not deter entry to the credit market, and believes that the level of fees currently applied by the FSA could lead to significant extra financial and administrative burdens on small businesses, and an overall increase in regulation costs. LG Regulation is also concerned at the cost of a FSMA-style regime to businesses, such as credit brokers for whom credit may be a necessary but very much secondary aspect of their business. This cost will ultimately be passed on to consumers.

A risk based system always has the potential to penalise those businesses perceived as „high risk“ but which may actually be broadly compliant, in that they inevitably need to spend resources in providing regulators with evidence of compliance. This wastes both the business and regulators resources which would be much better utilised in dealing with non compliant businesses. It would also seem in conflict with the policy direction of recent years, focusing on „intelligence-led“ enforcement, the corner-stone of the Hampton report. An intelligence led approach as adopted by TSS to deal with matters under CCA, provides a much more cost effective approach to enforcement.

A flexible fee arrangement which would depend on business size would be a welcome move, although it will potentially add burden to the large business rather than assist smaller **ones**.

LG Regulation agrees with the idea of a proportionate based approach however the question comes down to what is considered proportionate. We believe that consumer complaints should play a central role in determining where enforcement is carried out. Bear in mind that each individual consumer is likely to only be concerned about their case and if action is not taken on their case they will consider the regime to be a failure – especially if a clear beach of consumer law has taken place. See Q18 for our views on fees.

Q18 LG Regulation believes that the Government should take account of the responses to the OFT review of consumer credit licensing fees carried out in 2010 in assessing the appropriate fee arrangements for consumer credit firms.

A key factor in fee arrangements is to ensure the regulator is not solely dependant on fees; there is clearly a need to ensure that any decision making process involving licensing decisions are not influenced by the need to maintain income via this means.

Fees should be linked to business size, turnover etc and not their legal status as they currently are. There are large business where there is a sole proprietor and small business which are limited liability company"s. Current such a small business pays more than the larger business due to legal status.

In the event of an overarching body with responsibility for CCA and other financial services there may be two license regimes which could be used. Firstly an overall license which covers all activities. Secondly an element based license where a fee is paid for each element of activity the business wishes to cover. This latter has the advantage of not overburdening business with a license fee which covers areas they will not need. Thus a small charity offering debt advice may only require one or two elements as apposed to the full fee.

LG Regulation suggests fees should be flexible and if there appears to be an issue arising in a particular area then the fees may need amending.

Box 3.D Consultation Questions

Q19 LG Regulation believes that there is a significant difference between the appointed representatives regime as it applies to financial advisors working for one principal, and that which might apply to other credit brokers who introduce consumers to a number of lenders. In the experience of TSS and LG Regulation the majority of credit problems encountered by consumers are the responsibility of credit brokers and other ancillary credit businesses.

One TSS investigated the activities of a debt collector who acted as an agent for four separate debt collection companies, but had previously been prosecuted for multiple car clocking offences under the Trade Descriptions Act, and was considered unfit to hold a licence under the CCA. None of the companies was aware of his convictions.

Another ongoing case relates to a Scottish city where two local agents of a medium-sized debt collection firm have been the subject of several complaints to Trading Standards. The agents were repeatedly accused of making overly-frequent phone calls and visits to debtors who also felt intimidated and harassed by their aggressive attitude during these calls and visits. The agents also repeatedly contacted the debtors" employers and former employers. The case is being treated as a potentially serious breach of debt collection guidance which brings into question the fitness and appropriateness of these individuals to be involved in debt collection. On conclusion of the investigation a report will be sent to the OFT.

In some ways finance companies already influence the activities of their supporting brokers by, for example ensuring that agreements are properly executed, and assisting in the resolution of complaints, but this is self-interest to a certain extent as the consequences of non-compliance are potentially unenforceable agreements or section 75 liability. In reality, a national finance

company would be unable to „police“ the activities of its network of supporting dealers.

LG Regulation would agree that the creditor who ultimately benefits from the credit should be responsible for the activities of their representatives and ensuring that they have complied with credit regulations, however, as credit brokers are a common source of complaints and they work for many different clients we would believe that they also should still be regulated.

Box 3.E Consultation Questions

Q20 Most TSS have little experience in relation to group licenses and they cover a number of activities were the licensable activity does not involve high commercial and financial stakes.

Box 3.F Consultation Questions

Q21 LG Regulation believes that self-regulation already exists to the extent of finance companies influencing supporting brokers as outlined above, but does not consider this a substitute for the legal requirements contained in the CCA. Membership of a trade body or adherence to a voluntary code of practice is not compulsory or universal in the credit industry, and there is no effective sanction for non-member firms.

Home Collected Credit and Payday loans

In their study *„Keeping the Plates Spinning“* Consumer Focus estimates that the number of people using payday loans has increased fourfold since 2006 to 1.2 million people, borrowing a combined £1.2 billion. Charges typically range from £13-£18 interest for every £100 borrowed, but can be as high as £30 per £100 for some online providers. This can generate APRs in the region of 1000% to 2000% given the short-term nature of these loans.

The number of businesses offering online payday loans is ever increasing. The difficulty in regulating online businesses is well known and it is important that existing enforcement tools, such as the offence for unlicensed trading, are not weakened.

The home collected credit market is dominated by one or two lenders. Any move to increase competition in this market should not be made without preserving the enforcement provisions that currently exist. These provisions include the offences for canvassing off trade premises and trading without a credit licence. Any move to lighten the burden on reputable lenders should not result in the erosion of the enforcement tools that allow enforcement agencies to tackle rogues and loan sharks.

Box 3.G Consultation Question

Q22 LG Regulation notes that the categories of ancillary credit businesses subject to the licensing and other provisions of the CCA have been extended under the CCA 2006, and believes that this has been essential for the proper

regulation of such activities. Any move to deregulate these would be detrimental to the aim of consumer protection.

Box 3.H Consultation Question

Q23 LG Regulation remains convinced that the CCA should remain in place to ensure a period of reasonable stability following the implementation of the Directive and the changes introduced by the CCA 2006. LG Regulation is also convinced that the criminal sanctions and local enforcement by TSS is crucial to the overall regulatory regime.

If the consultation does result in a move to a FSMA-style regulatory regime, LG Regulation would hope that the local enforcement role of TSS and DETINI would be continued.

It is not considered that the proposed regime would necessarily be any more proportionate or effective than the current regime, except in relation to the creation of a competent, flexible and responsive supervising body under CCA. The incorporation of the current (and if needed amended) CCA regime under a new more dynamic and active body using existing partners and resources would have great merit.

LG Regulation believes that the regulations should be intelligence led and concentrate on areas with a high volume of consumer complaints. The regulator should be able to promptly act to protect the consumer from detrimental trading activity in whatever form it may take. LG Regulation also believes regulators should consider other social factors when determining enforcement priorities, including protecting vulnerable groups, dealing with aggressive selling practices and protecting those groups who are economically disadvantaged.

Chapter 4

Box 4. A Consultation Question

Q24 LG Regulation would be concerned if there were any loss of protection for consumers entering agreements under the existing legislation once the scope and detail of future regulation is made clear. The remedies and protections provided by CCA should remain across all aspects of business. Any transfer should be quick and seamless. It should be the case that consumers and business do not notice any major change. This is one reason why there is support for the retention of CCA albeit under a different overarching control body.

When people entered into their credit agreements under the old regime they did so under the belief that they would have the protections of that regime. This is true for both consumers and traders. Therefore LG Regulation is concerned that there may be a dual regime of old versus new provisions, with increased complexity for enforcers.

Box 4.B Consultation Question

Q25 If there are significant changes to the requirements needed to obtain a credit licence then all existing licence holders would have to abide by this

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however if there are no significant changes then group relicensing would be possible providing this is financially possible.

Box 4.C Consultation Question

Q26 LG Regulation has no comments at this stage, other than to refer to its answer to Q18 above where the results of the OFT consultation may have some relevance.

Box 4.D Consultation Questions

LG Regulation has no comments.

Annexes

LG Regulation would also make the point that consumer credit licensing is a core consumer protection provision of the CCA, which should be included in Annex A. Licensing helps to ensure that those who are involved in consumer credit are fit and competent, which is an essential prerequisite.

In the list of key features of the CCA regime in Annex B, it should be pointed out that the regulator can consider the fitness of associates of the licensee or applicant. Additionally the information-gathering powers of the OFT, referred to under „CCA regime fitness standards and supervision“, were only introduced under the CCA 2006.

LG Regulation also suggests that the „Conditions“ applicable to the CCA in Annex C should also include consumer hire agreements, and the wider definition of credit ie “any other form of financial accommodation” to clarify that the Act applies to agreements under which time is allowed for the payment of the price for goods or services.

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RESPONSE TO:

A NEW APPROACH TO FINANCIAL REGULATION: CONSULTATION ON REFORMING THE CONSUMER CREDIT REGIME

CIVIL SANCTIONS AND REMEDIES UNDER OPTION 1

GENERAL

1. I respond in a personal capacity as a legal academic researching consumer credit and financial services regulation law¹ and as a practising barrister in the area.² This response primarily addresses Consultation Question 14 and considers how Option 1 needs to address the differences in civil sanctions and remedies between the present consumer credit regulatory regime and the FSMA regime. Thus whilst Annex A of the Consultation Paper lists the 'core consumer protections enshrined under the CCA' it does not follow through how these protections are achieved and how they might be achieved under the FSMA. Whilst the alignment of disciplinary sanctions will (in my view) not be difficult, more thought needs to be given to the alignment of legal liabilities.

ACTIONABILITY FOR BREACH OF REGULATORY RULES

2. FSMA 2000, s.150³ renders a breach of most conduct of business rules actionable (as a quasi breach of statutory duty action) by 'private persons' who can establish loss. This has proved a very useful additional cause of action for consumers harmed by misconduct.⁴

3. Apart from a few isolated cases,⁵ the CCA explicitly excludes such actions.⁶ Whilst the CCA does not provide for a 'conduct of business' rule book as such,⁷ it does impose a

¹ At King's College London Law School; I edit (a) *The Encyclopedia of Consumer Credit Law* (Thomson; Sweet & Maxwell; Looseleaf) and the relevant Chapter (38) in *Chitty on Contracts* (30th Ed); (b) *The Encyclopedia of Financial Services Law* (Thomson; Sweet & Maxwell; Looseleaf)

² At 4 New Square, Lincoln's Inn.

³ This breach of statutory duty action is available for other breaches of the FSMA regime, see for example, ss.20(3), 71, 202(2), 241. It is also a common feature of related regulatory regimes, e.g. Payment Services Regulations 2009, SI 2009/209, reg.120.

⁴ See eg. (some case law on the predecessor FS Act 1986, s.62): Morgan Stanley UK Group v Puglisi Consentino [1998] CLC 481; Martin v Britannia Life Ltd [2000] Lloyd's Rep. PN 412; Loosemore v Financial Concepts [2001] Lloyd's Rep (PN) 235; Seymour v Ockwell [2005] EWHC 1137; [2005] PNLR 39; Shore v Sedgwick FS [2008] EWCA Civ 863; Spreadex Ltd v Sekhon [2008] EWHC 1136. I understand s.150 is also useful to the FSCS in seeking easily to establish an insolvent firm's liability to customers and see Re Global Trader Europe Ltd. [2009] EWHC 602.

⁵ Breach of CCA, s.55C (draft copy on request), CCA, s.78A (see n.24, below), CCA, s.92 (entry onto premises to recover possession of goods or land), s.103 (duty to provide termination statement).

⁶ CCA, s.170(1)

significant number of obligations on creditors that would belong in a FSMA COBS-type rule-book. Annex A of the Consultation Paper lists these. It is notable that the sanctions that the CCA presently provides for breach of its protections are either (a) criminal⁸ or (b) purely disciplinary⁹ or (c) rendering the agreement unenforceable (the 'unenforceability sanction').¹⁰

4. There are criminal sanctions for:

- credit advertising breaches: s.45, 47 (and see s.167(2))
- canvassing off trade premises: s.49
- sending circulars to minors: s.50
- sending unsolicited credit tokens: s.51
- sending unsolicited credit card cheques: s.51A
- breaches of pawn-broking regime: s.115
- breaches of credit reference agencies' obligations: ss.157-9
- breaches of credit intermediaries' obligations: s.160A
- breaches of various regulations under s.26 (conduct of business), s.44 (advertising), s.52 (quotations), s.54 (conduct of business):167(2)

5. There are purely disciplinary sanctions for breaches of the two new obligations imposed as a result of the Consumer Credit Directive: (i) to provide 'adequate explanation' of agreement (s.55A) and (ii) to assess credit worthiness (s.55B).

6. The obligations listed above in paragraphs 4 and 5¹¹ would (presumably) be collected in a FSMA COBS-type rule-book. It would follow that FSMA, s.150 would prima facie¹² apply and hence breach would give rise to a breach of statutory duty action. I suggest below¹³ that this would be desirable. Further, consideration needs to be given to removing some of these criminal sanctions which are out of line with the FSMA approach of only

⁷ Although there is power to make conduct of business rules under CCA, ss.26, 54 - these powers have hardly been exercised.

⁸ See para.4, below. Note that, in particular, breaches of conduct of business regulations made under CCA, ss.26, 54 are criminal offences: s.167(2).

⁹ See para.5, below.

¹⁰ See paras.10-12, below.

¹¹ As well as those in n.5, above, that already give rise to a breach of statutory duty action.

¹² The FSA may disapply s.150 to any of its rules: FSMA, s.150(2),

¹³ See para.14, below

criminalising very serious breaches¹⁴ and not criminalising breaches of rules by authorised persons.¹⁵ (Indeed, a more imaginative and potent sanction for breaches of CCA, ss.49-51A would be to absolve the debtor from liability under any consequent agreements made.)

UNENFORCEABILITY OF AGREEMENTS:

UNDER FSMA

7. FSMA reserves the 'unenforceability sanction' for transactions effected 'outside the perimeter', that is agreements made by firms that are unauthorised or through intermediaries that are unauthorised¹⁶ or transactions in breach of the financial promotion restriction that applies to unauthorised persons.¹⁷ Such agreements are unenforceable against and voidable at the instance of the customer, unless the court orders otherwise. This 'unenforceability sanction' is clearly an effective incentive to become authorised (and to check intermediaries are authorised), otherwise the firm's agreements are not only *prima facie* unenforceable but the customer can (in theory) recover their money back.

8. But once a firm becomes authorised, FSMA makes it clear that, whilst breach of statutory duty liability may arise,¹⁸ any contravention of the FSA rule-book does not render the agreement 'void or unenforceable'.¹⁹ (However, there is a suggestion, in the February 2010 Consultation, that breach of the proposed 'product banning rules' should render resulting contracts 'void/unenforceable'.²⁰)

9. Hence (presently) FSMA (as did the Financial Services Act 1986 before it) draws a bright line between activity 'outside the perimeter' (which does give rise to the unenforceability sanction) and activity within the perimeter (which does not). The rationale

¹⁴ See esp. FSMA, s.23 (breach of general prohibition), 25 (breach of financial promotion restriction), s.398 (market misconduct).

¹⁵ FSMA, s.151(1) cf. CCA, ss.26, 54 and s.167(2) (and see n.7, above).

¹⁶ FSMA, ss.26-28. See CR Sugar Trading Ltd (In Administration) v China National Sugar Corp & Alcohol Group [2003] EWHC 79 [2003] (decided under the predecessor provision in FS Act 1986); Re Whitely Insurance Consultants [2008] EWHC 1782 (Ch); Helden v Strathmore [2010] EWHC 2012 (Ch).

There is also criminal liability: FSMA s.23

¹⁷ FSMA, s.30

¹⁸ FSMA, s.150, see para.2, above

¹⁹ FSMA s.151(2).

²⁰ See *A new approach to financial regulation: building a stronger system*, Cm8012 (February 2011), para.4.65. First there is reference to making provision for 'the unenforceability of contracts made in breach of ..product intervention rules' and then there is reference to the contract being 'void'. I would suggest the term should be 'voidable' so as to give the consumer the choice whether to avoid the contract or not (if s/he wants to keep the product).

appears to be to reserve the drastic sanction of invalidating transactions to limited circumstances. This is because (unless the court exercises its discretion to uphold the agreement), it causes transactional insecurity/uncertainty and can be used unmeritoriously to try and avoid liability.

UNDER CCA

10 In contrast to FSMA, the CCA uses the 'unenforceability sanction' extensively. In particular, non-compliance with the detailed copy and documentation requirements renders agreements unenforceable,²¹ unless the court orders otherwise, having regard to prejudice caused and the degree of culpability for breach (as well as the court's discretion to reschedule payments and vary the agreement).²² Similarly, any security provided is unenforceable (unless the court orders otherwise) if certain documentation and other requirements are not complied with.²³ Non-compliance with the numerous 'information' obligations whilst the agreement subsists also renders the agreement unenforceable whilst the non-compliance lasts.²⁴

11. In the consumer credit context, as the debtor from the outset is under a repayment liability, the statute merely renders the agreement 'unenforceable'. Unlike the corresponding FSMA provision,²⁵ it does not entitle the debtor to 'unravel' the agreement as presumably no debtor would want to do this and incur the liability immediately to repay the credit; much better for the debtor just to rely on the unenforceability of his liability to repay.

12 As is well-known, these provisions have been extensively invoked (aided and abetted by claims management companies) to try and 'write-off' debt liabilities. Many such claims have been unmeritorious.²⁶

²¹ CCA, ss.55(2), 65

²² CCA, s.127(1)

²³ See CCA, ss.105(7)(a), (b), 111(2), 124(1), (2).

²⁴ CCA, ss. 77, 77A, 78, 79, 86D. But breach of s.78A (inserted recently as a result of the Consumer Credit Directive requiring amortisation information) gives rise to a breach of statutory duty action. See also ss.107-9 (notices to security provider: security unenforceable) and 110 (notice of security to debtor: again security unenforceable). This time the court has no discretion to enforce (but on compliance, the agreement becomes enforceable again).

²⁵ FSMA, ss.26-28, 30 - see para.7, above

²⁶ Eg. the notorious Rankine litigation

13 To complete the picture, again in contrast to FSMA, agreements 'outside the perimeter' (by unlicensed creditors), although unenforceable²⁷ can be enforced by the OFT (not the court).

THE FUTURE

14 The tidy solution under Option 1 would be to sweep the 'conduct of business' obligations of creditors (i.e. those listed in paragraphs 4 and 5 above and including the documentation obligations that presently give rise to the 'unenforceability' sanction noted in paragraph 10) into an FSMA COBS-type rule-book and render breach actionable under FSMA, s.150. This would have the merit of increasing the protection in some areas where the sanction is presently only disciplinary or criminal (see above²⁸).

15 The question then arises whether to retain (in addition or instead) the CCA 'unenforceability sanction'. Adopting the present FSMA dichotomy (reserving unenforceability for activities outside the perimeter and not making it available for breaches by authorised/licensed creditors) would reduce debtor protection in that (i) s/he would have to raise the s.150 claim when sued for the debt to reduce liability (rather than the creditor having to invoke the discretion of the court to enforce the agreement) and (ii) the court, in deciding the s.150 issue, could only take account of the 'loss' caused to the debtor whereas presently the court must also²⁹ look to the degree of culpability for breach and has a discretion to reschedule payments and vary the agreement.³⁰ Normally, where the debtor is prejudiced by some error in the documentation, the result under either system (CCA unenforceability or FSMA action for breach) would be much the same: his liability will be reduced by the extent of the 'prejudice' (the CCA term) or 'loss' (the FSMA term). However, the point remains that the CCA 'unenforceability sanction' is a potent consumer protection measure in incentivising creditors to comply with their documentation and information obligation, so that they do not risk a portfolio of agreements that are (i) prima facie unenforceable and (ii) whose enforcement (and/or variation) is at the courts (wide(r)) discretion. Against this is the fact that unenforceability does cause considerable commercial uncertainty (a significant issue if

²⁷ CCA, ss.40, 149. Again, there is no entitlement to 'unravel' the agreement, for the obvious reason given in para.11, above.

²⁸ Paras. 4 and 5 - although I suggest that the criminal sanction may not be appropriate in some cases.

²⁹ The 'prejudice caused' (CCA, s.127(1)) would normally correspond to the 'loss' (FSMA s.150(1))

³⁰ See CCA s.127(1)

the agreements are to be sold on in factoring or securitisation transactions) and does encourage unmeritorious shirking of liability.

16 In my view, the FSMA, s.150 breach of duty action is a sufficient sanction for breaches of conduct of business rules (including documentation etc. requirements) but it must be admitted (see previous paragraph) that in cases where the CCA presently provides for the 'unenforceability sanction', this would result in some dilution of consumer protection. However, such a breach of duty action would increase consumer protection in those cases where at the moment it is not available (see paragraphs 4 and 5).

17 As for transactions outside the perimeter, the FSMA approach of giving the court (rather than a regulator) the discretion to uphold agreements is (in my view) preferable to that under the CCA³¹ and hence rationalisation would seem to be appropriate here.

OTHER PROTECTIONS.

18 Otherwise, I would support the retention of the other 'special' CCA civil liability protections listed in Annex A, in particular:

- S.91: entitlement to repayment of all instalments when hire-purchased goods repossessed in breach of s.90.
- Ss.75 and 75A: connected lender liability (required by Consumer Credit Directive, Art.15(2)).
- Ss.140A-140D: re-opening of credit agreements if 'unfair relationship'.

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³¹ Compare paras. 7 and 13, above