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HM Treasury

A new approach to financial regulation: transferring consumer credit regulation to the Financial Conduct Authority

A Response by Credit Action

Background

Credit Action is a national financial capability charity (registered Charity in England & Wales No. 1106941) established in 1994.

Credit Action empowers people across the UK to build the skills, knowledge, attitudes and behaviours, to make the most of their money throughout their lives. It develops and delivers products and services which provide education, information and advice on money matters, in an appropriate way for young people and adults. Through its work Credit Action reaches approximately 500,000 UK citizens every year.

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Introduction

As an organisation, Credit Action is committed to helping people build their financial capability, and develop the skills necessary to manage their money effectively. In our view, fair and well-functioning markets are crucial to enabling consumers to make the best use of these skills, and to ensuring that they are able to make financial decisions in an informed and objective manner. We therefore maintain a keen interest in regulatory developments, particularly with respect to the conduct regime.

The transfer of consumer credit regulation from the Office of Fair Trading (OFT) to the Financial Conduct Authority (FCA) is a hugely significant change to the regulatory landscape, and will have an enormous impact for consumers and firms alike. However, it is a shift that we very much welcome, and we would like to make clear at the outset of this response that we believe the introduction of a stronger, rules-based regime has the potential to provide greater protection for consumers than has been possible under the OFT's licensing system, and therefore drive real benefits in the consumer credit market.

There are, though, certain areas in which we feel there is a need for much greater clarity around the FCA's approach. One particularly significant issue is the way in which not-for-profit "debt advice" will be defined. At present, we are concerned that a very broad range of activities, including even the provision of generic budgeting advice, could fall within the FCA's definition as it currently stands and therefore be subject to regulation. This would have considerable implications for a large number of organisations and services. We discuss this in detail in our answer to Question 3.

In responding to this consultation, we have focused in particular on addressing Questions 1, 2, 3, 8, 9, 10 and 11, and set out both where we feel the proposals for reform of the consumer credit regime are particularly strong, as well as those issues that we believe still need to be addressed.

Question 1: What are your views on the Government's proposal to carry forward CCA conduct requirements which cannot easily be replicated in FCA rules? Do you agree with the Government's intention to require the FCA to review these retained CCA provisions, with a view to moving to rules-based alternatives wherever possible?

In general, the proposed approach of carrying forward CCA conduct requirements which cannot be easily replicated in FCA rules seems to us to be sensible, and enables the FCA to get the new regime up and running in the short-term. Moving forward, we also agree with the suggested review of the retained CCA provisions by 2019 with a view to moving to rules-based alternatives. As outlined in the Introduction, we believe a rules-based regime is stronger and will offer greater protection to consumers, and therefore feel that in the longer-term this approach should form the basis of regulation as far as possible.

<u>Question 2:</u> How, if at all, do you think industry codes can complement FCA conduct regulation?

In principle we believe that there is a place for industry codes, where these push firms to go beyond the basic requirements of regulation. In this context, we would envisage codes as effectively representing a sort of "gold standard" for conduct. Were codes to be employed in this way, we feel that they would help to drive better outcomes for consumers, and genuinely promote best practice within the credit industry. However, we would stress that where codes largely require signatories to simply comply with existing regulation, they add very little value, and will not complement the FCA's work in any meaningful way.

In practical terms, we would also note that industry codes may be particularly useful in the short-term, as the regulatory transition takes place and the FCA develops its institutional expertise in consumer credit. The consumer credit "bloc" is an incredibly diverse one, encompassing the likes of payday lenders, home credit firms, debt advice providers and peer to peer platforms. It will, understandably, take the FCA a certain amount of time to get to grips with the unique features of the various different aspects of this market, and while it does so the industry codes which apply in each of these spheres could potentially help plug the gap. However, we would reiterate that, looking forward, it will be crucial for industry codes to push firms to go above and beyond the FCA's regulatory requirements in order for them to have utility in the long-term.

<u>Question 3:</u> What are your views on the Government's proposals for a two-tier authorisation regime? Is the scope of the limited permission regime right?

As suggested in the Introduction, our central concern with regard to the scope of the limited permission regime is the way in which the FCA will define not-for-profit debt advice, and whether this could ultimately be drawn too broadly.

Paragraph 3.24 notes that as part of the proposed changes to consumer credit regulation, "debt advice, even where it is provided by a body that operates on a not-for-profit basis, should be regulated by the FCA" and that this is facilitated by an amendment to the "by way of business" test in Part 5 article 16 of the draft RAO order. Paragraph 3.25 then makes clear that not-for-profit debt advice providers will be subject to a bespoke regulatory model and included in the lower cost limited permission regime. While we have little problem with the general principle of these provisions, we also believe there is a lack of clarity around precisely what sorts of activities will qualify as "debt advice", and therefore require a limited permission if performed by a not-for-profit body.

The Financial Services Authority's parallel consultation on reforming the consumer credit regime (*FSA CP13/7: High level proposals for an FCA regime for consumer credit*) includes the following passages which imply quite a broad interpretation of the activities which will require a limited permission:

> [Paragraph 8.4] While we expect all regulated debt advice to be high quality, we propose to apply different rules to different types of advice, reflecting the different nature of the advice and associated risk.

> [Paragraph 8.5] Where advice is given to the borrower on the liquidation of a debt that is specific to the borrower, but the advice provider does not identify and/or recommend a particular 'debt solution' for the borrower to enter into, we propose that it should be sufficient for the advice provider to ensure that they observe the FCA's high level Principles for Business. *For example, advising a borrower on their weekly budget in order to better enable them to meet repayments of the money they owe under their credit agreement(s) as they fall due.* [Italics added]

The italicised section appears to suggest that the provision of budgeting support to clients could potentially be subject to FCA regulation, if such an activity is intended "to better enable them to meet repayments of the money they owe under their credit agreement(s)". In practice however, given that almost every UK consumer will have some form of credit obligation, it is likely that most budgeting advice will ultimately encompass the repayment of money owed under a credit agreement. Therefore, we believe that in most circumstances this definition will prospectively capture the provision of even the most generic budgeting advice.

Consequently, we are concerned that within the FCA's approach, a wide range of actors that do not offer what has traditionally been understood as debt advice could ultimately require a limited permission. For example, any organisations offering face-to-face or telephone-based budgeting services are potentially drawn into the scope of this, even where no debt solution is recommended or facilitated, while online tools offered by the likes of the Money Advice Service which allow users to construct personalised budgets could also fall into this category. Indeed, such services are taking on particular significance right now, given the Coalition Government's wider reform of the welfare system and the introduction of Universal Credit. In this context, it has been recognised that support will be necessary to help benefit claimants to budget on a monthly rather than a weekly basis (this is highlighted in the Department for Work and Pensions' *Universal Credit Local Support Services Framework*, for example), and it is possible that all such services could require a limited permission under the above definition.

Meanwhile, the approach taken by HM Treasury is set out in the draft RAO order in Annex C of this consultation. Part 5 article 16 of the draft order amends the "by way of business" test to the effect that not-for-profit bodies undertaking "debt-adjusting", "debt-counselling" and "providing credit information services" will require a limited permission. With respect to *debt adjusting*, article 39D of the draft order states that:

> *(1) When carried on in relation to debts due under a credit agreement –*
>
> > *(a) negotiating with a lender, on behalf of the borrower, terms for the discharge of a debt,*
> >
> > *(b) taking over, in return for payments by the borrower, that person's obligation to discharge a debt, or*
> >
> > *(c) any similar activity concerned with the liquidation of a debt,*
>
> *is a specified kind of activity. [i.e. an activity subject to regulation]*

(2) When carried on in relation to debts due under a consumer hire agreement –

> *(a) negotiating with the owner, on behalf of the hirer, terms for the discharge of a debt,*
>
> *(b) taking over, in return for payments by the hirer, that person's obligation to discharge a debt, or*
>
> *(c) any similar activity concerned with the liquidation of a debt. It is a specified kind of activity,*

is a specified kind of activity.

Equally, with respect to *debt counselling*, article 39E of the draft order states:

(1) Giving advice to a borrower about the liquidation of a debt due under a credit agreement is a specified kind of activity.

(2) Giving advice to a hirer about the liquidation of debts due under a consumer hire agreement is a specified kind of activity.

Meanwhile, article 89A of the draft order states with respect to the *provision of credit information services* that:

(1) Taking any of the steps in paragraph (3) on behalf of an individual or relevant recipient of credit is a specified kind of activity.

(2) Giving advice to an individual or relevant recipient of credit in relation to the taking of any steps in paragraph (3) is a specified kind of activity.

(3) Subject to paragraph (4), the steps in this paragraph are steps taken with a view to –

> *(a) ascertaining whether a credit information agency holds information relevant to the financial standing of an individual or relevant recipient of credit;*
>
> *(b) ascertaining the contents of such information;*
>
> *(c) securing the correction of, the omission of anything from, or the making of any other kind of modification of, such information; or*
>
> *(d) securing that a credit information agency which holds such information –*
>
> > *(i) stops holding the information; or*
> >
> > *(ii) does not provide it to any other person.*

(4) Steps taken by a credit information agency in relation to information held by that agency are not steps in paragraph (3). [The article then includes a final provision which defines a "credit information agency" which is not replicated here]

Within these legislative provisions, advising borrowers on "the liquidation of a debt due under a credit agreement" constitutes a specified activity. While this could, in theory, extend to the provision of budgeting advice where this encompasses repayments on a credit agreement, this would represent an exceptionally broad interpretation of the legislation, and one that may not reflect the framers' original intent.

Consequently, we believe there is an urgent need for clarification about precisely what activities will be subject to FCA regulation. As suggested, we fear that if generic budgeting advice is ultimately covered, it will prospectively mean that a wide range of not-for-profit actors who have not previously been within the scope of regulation will require a limited permission. In our view, this would create a significant risk that many organisations will withdraw this sort of basic (but nonetheless essential) support as they seek to pull back from the regulatory perimeter. Indeed, we feel that in a situation where changes to the advice landscape (including the introduction of the Retail Distribution Review and other developments) have raised fears over the emergence of a possible "advice gap", the regulatory issues discussed here have the potential to aggravate such problems even further.

As a final point, we would also briefly raise a separate issue surrounding the terminology that surrounds the "limited permission" regime. There are concerns within the not-for-profit debt advice sector that using the term "limited permission" to describe the FCA's regulatory approach could imply that not-for-profit services are somehow of an inferior standard compared to commercial firms who require "core" credit authorisation, rather than simply being lower risk. We believe that such concerns are warranted, and the term "limited permission" may ultimately send inappropriate messages to consumers. We would therefore encourage HM Treasury and the FCA to develop an alternative term to describe the regime that applies to not-for-profits in order to address this.

Question 8: What are your views on the proposed new activity to capture the activities of peer to peer platforms?

We are very much in favour of greater regulation of peer-to-peer platforms. These have the potential to become a significant part of the consumer credit landscape over the next few years, and it is therefore crucial that those consumers and businesses that make use them are afforded appropriate levels of protection. Paragraph 4.8 highlights important gaps in the Consumer Credit Act with respect to peer-to-peer platforms which clearly need to be addressed.

We are therefore supportive of the creation of the new bespoke activity of "operating an electronic system in connection to lending" to cover peer-to-peer platforms, and hope that this will provide the greater legislative cover necessary. Ultimately, we would emphasise the need for an effective and robust regime for peer-to-peer platforms to be put in place when, as mentioned in paragraph 4.11, the FCA sets out its plans for introducing new rules for the sector later this year.

<u>Question 9:</u> Do consultation respondents have any data on the activity of lead generators in the debt management sector? What detriment is being caused by these firms? And what are your views on a suitable regulatory response?

With respect to regulating lead generation within the debt management sector, we feel that it is important to raise the issue of possible implications for not-for-profit bodies. We note that, as outlined in paragraphs 4.40 to 4.43, the Government is considering whether or not to take regulatory action in this area, subject to the provision of the market data necessary to make a decision. However, while we have no real issue with the principle of regulating organisations which sell leads to commercial debt management businesses (and, indeed, believe that doing so could ultimately benefit consumers), we would stress that it would be crucial for any regulatory interventions to be designed carefully in order to avoid unintended consequences.

In particular, we are concerned that if any such provisions are drawn too broadly, then the simple activity of referring someone to a not-for-profit debt advice body such as Citizens Advice, StepChange Debt Charity of the Money Advice Trust could ultimately constitute a regulated activity. This, in our view, would be heavily disproportionate, and affect not only those who regularly refer clients on to not-for-profits for debt advice (such as ourselves or the Money Advice Service), but potentially any organisation who includes a link to such providers on their website (which might, for example, encompass the likes of the BBC).

We do not believe that it is the FCA's intention to include this kind of general signposting within the scope of regulation, but at this stage simply wish to emphasise the importance of calibrating any regulatory response to commercial lead generation carefully, to ensure that it does not inadvertently capture the sorts of activities described here.

<u>Question 10:</u> What are your views on the Government's proposal to repeal many of the criminal offenses in the CCA and make breaches of these requirements, once in rules, subject to the FCA's enforcement toolkit?

We recognise that in order to create a consistent system of regulation under the FCA, it will be necessary for the Government to repeal criminal offenses in the Consumer Credit Act and make breaches of the requirements subject to the FCA's enforcement toolkit. In principle we take little issue with this proposal, provided that it facilitates a coherent regime. However, we would add that once the FCA's toolkit is in place, it will be vital that it makes full use of those tools in order to deliver improved outcomes for consumers, and pursue strong and effective enforcement action wherever this is required.

<u>Question 11:</u> What are your views on the proposed interim permissions regime?

In general, we believe that the proposed interim permission regime represents a sensible approach to the challenges of transition. We recognise the need for this to be managed in a way that balances

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the needs of consumers and firms, and agree with the sentiments of paragraph 6.10 that in principle it achieves this by delivering enhanced protection and oversight on one hand (by providing the regulator with the full range of powers available under the Part 4A permission system) while ensuring a proportionate burden on firms on the other (as they will not need to meet the higher test of becoming fully authorised before April 2014, allowing them time to adjust). We would, however, reiterate the need for the FCA to make effective use of its enforcement powers where necessary during the interim permission period, and ensure that transition is not used as an excuse by negligent firms for poor conduct.

Contact

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