



FUTURE REGULATORY FRAMEWORK REVIEW: FINANCE & LEASING ASSOCIATION RESPONSE

About the FLA

1. The Finance & Leasing Association (FLA) is the leading trade body for the UK asset, consumer and motor finance sectors. In the twelve months to November 2020, FLA members provided £115 billion of new finance to UK businesses and households. Over £87 billion was in the form of consumer credit, accounting for over a third of all new consumer credit written in the UK. Nearly £28 billion of finance was provided to businesses (including £16 billion to SMEs) and the public sector to support investment in new equipment, representing over a third of UK investment in machinery, equipment and purchased software.
2. Our members provide both regulated and exempt lending and are subject to regulatory oversight by the Financial Conduct Authority (FCA), Prudential Regulation Authority (PRA) and the Competition and Markets Authority (CMA). The Financial Ombudsman's Service (FOS) also plays a quasi-regulatory role in interpreting FCA rules and guidance. The FLA's Lending Code and Business Finance Code have also formed part of the overarching regulatory framework for over 25 years, providing additional protection for customers.

The Future Regulatory Framework

3. The removal of the EU layer from the policy framework offers an opportunity to simplify the financial services policy framework and make it more transparent.
4. Key to effectiveness will be ensuring that each of the key players – Parliament, Government, FCA and the other Financial Services and Markets Act (FSMA) bodies – have clearly defined roles and accountabilities and that their functions are exercised transparently.
 - Parliament should clearly retain for itself the function of determining the framework through primary legislation and calling all the players to account.
 - The FCA should, as now, have significant powers to set and enforce the detailed rules in a transparent, independent, evidence-based and agile way.
 - There is, however, an opportunity to redefine the role of Government in this framework, to address a perceived or real current democratic deficit – where society's expectations would be, for example, that significant decisions around strategic direction and scope of regulation should be the preserve of Government, as held to account by Parliament.
 - But it is essential that any enhanced role for Government be exercised in a transparent and consultative way in accordance with procedures set out in statute (such as an amended FSMA), for example through orders and instruments subject to parliamentary scrutiny. It is essential for market and

consumer confidence that significant government control should not be exercised behind closed doors.

RESPONSE TO QUESTIONS

The post-EU regulatory framework proposal

Q1. How do you view the operation of the FSMA model over the last 20 years? Do you agree that the model works well and provides a reliable approach which can be adapted to the UK's position outside of the EU?

5. The FSMA model has been effective. It enshrines the principle that Government and Parliament should set the purpose, objectives and boundaries of the regulatory framework, while an independent and evidence-based regulator sets, amends and enforces the rules. The FSMA model also allows the redress and compensation arrangements to be set within the overall framework, alongside the processes that ensure the accountability of the bodies that perform these regulatory functions. We believe that this remains the right model for the future.
6. The credit sector, however, is as much impacted by the Consumer Credit Act (CCA) as it is by FSMA. The sector is also impacted by the EU Consumer Credit Directive (CCD), whose provisions have been transposed variously into both the CCA and into rules set within the FSMA framework. There are, as well, 27 statutory instruments made under the CCA which add further to the complexity of the overall framework for credit.
7. Now the UK has left the EU and ceased to be bound by the CCD, we therefore see significant scope for simplification and modernisation of the regulatory framework for credit. The scope for such improvement would also be much enhanced if parliamentary time were secured for reform of the CCA too. Furthermore, we see no conflict between the need for simplification, modernisation and reform and the need to retain or enhance the level of consumer protection. Rather, we see all these needs as being best met by moving to the type of regulatory framework that is proposed: a limited core of primary legislation (restricted to those matters that only primary legislation can deal with, such as rights, liabilities and the terms of the framework) with the setting and enforcement of the rules delegated to the FCA.

Q2. What is your view of the proposed post-EU framework blueprint for adapting the FSMA model?

8. As a result of our withdrawal from the EU, both the Government and regulators have more autonomy, more for regulators than at any time since their creation as they did not exist when the EU was established. It is more important than ever therefore that both conduct themselves with the highest degree of integrity. In the UK, integrity is defined through [Seven Principles of Public Life](#) which apply to regulators as well as other bodies. These include three which are particularly relevant to this consultation: objectivity, accountability and openness. The

Consultation Paper neglects to reference these important ethical standards and how they will be fostered in the future.

9. The 2016 [review](#) of these Principles points to the importance of regulators:
 - adopting evidence-based and risk-based approaches by regulators (objectivity);
 - being accountable to stakeholders and fulfilling this function in “an open and transparent manner”; and
 - consistently maintaining openness and honesty in their day-to-day operation.
10. Regulatory integrity and the above principles cannot be upheld successfully by regulators unless their independence from Government is assured, particularly in relation to operational and enforcement decisions. Achieving this requires regulators and other public bodies to have strong boards and strong governance and should be considered as part of the Government’s analysis. To this end, the interaction between the regulator and government must be clear and transparent (which has not always been apparent in consumer credit markets during the pandemic) and requires compliance with public appointments rules.

In particular:

- *What are your views on the proposed division of responsibilities between Parliament, HM Treasury and the financial services regulators?*
11. We agree with this division of responsibilities. We support giving regulators powers to act more flexibly to ensure a more modern and consistent approach to supervision. However, they must consult widely and give realistic timeframes for response. An example of bad practice during the Summer of 2020, was giving firms a two-day turnaround over a weekend to help shape the FCA’s guidance on payment deferrals for unsecured lending even if this work was time critical.
 12. We also support the view that the scope of the regulatory boundary should be set by government and Parliament (see specific example in para. 15). Again, we would encourage governments to abide by the [2018 Consultation Principles](#) which state that the process should not be rushed and should consult the “full range” of those affected. There have been examples of this not being the case in our markets so it is important that these Principles are respected.
 13. How the FCA accounts to Parliament for its statutory activities is a matter primarily for Parliament. The fact that some of FCA’s policy-making activities touch on, or overlap with, wider government policy-making is not new. Standard machinery of government liaison processes exist to deal with this, without affecting each body’s statutory powers or remit.
 - *What is your view of the proposal for high-level policy framework legislation for government and Parliament to set the overall policy approach in key areas of regulation?*
 14. The central premise of HMT’s proposal that government and Parliament set the policy approach in key areas makes sense. A core area – which is reflected by the

fact that 40,000 of the 60,000 of the FCA-regulated firms undertake consumer credit – is to reform the CCA, which is nearly 50 years old and contains provisions dating back to the 1960s.

15. The CCA's shortcomings have been severely exposed during the pandemic. Lenders have been supportive to their customers, for example, by offering payment deferrals (in line with the FCA's guidance) but the requirement to offer a modifying agreement (a lengthy process involving a fresh agreement together with a customer signature) when applications for forbearance were at a high level, was operationally challenging. FLA members processed over 1.7 million such requests. If lenders instead agreed informal arrangements with those in financial difficulty, this triggered the requirement to issue arrears and default notices, the latter, in particular, couched in aggressive and unsympathetic language when customers were at their most vulnerable. HMT has made helpful changes to the content of default notices via a statutory instrument, but was prevented from being more radical because this would have required primary legislation.
16. The CCA is also ill-suited to digital channels. 89% of new loans provided in 2017 by FLA members were fully or partially digital. We anticipate that today almost all new agreements contain a digital element. The cumbersome standard pre-contractual information – prescribed by the EU CCD – repeats information found in agreements and should be adapted to the online environment, for example via the use of links.
17. The Government recently announced plans to phase out the sale of new petrol and diesel cars by 2030. However, the CCA impedes finance companies' ability to more widely fund low emission vehicles (LEVs). Examples include the antiquated definition of a motor vehicle and the need for separate agreements for the vehicle and battery.
18. Other challenges to be addressed for the modern consumer are inconsistencies between the protections provided by different credit products, including Sharia-compliant finance.
19. The regulatory perimeter for the CCA poses difficulties for many SMEs seeking funding for their businesses. Over 1.5 million of the UK's smallest businesses are covered by the CCA and lending agreements with these businesses are subject to extensive regulation designed to protect individual consumers under the legislation. Whilst the FCA has previously acknowledged that businesses are generally better equipped to understand the risks and conditions of commercial finance agreements, the requirements imposed by the CCA do not reflect this. Providing the appropriate documentation is costly for funders and time consuming and as a result, some asset finance funders have withdrawn from the market or have avoided entering it entirely. This reduces competition and customer choice, leading to higher costs for businesses.
20. We have proposed to the Economic Secretary a simplified consumer credit regime, in which CCA's provisions would be replicated via a combination of powers contained in FSMA and the FCA's Consumer Credit sourcebook (CONC). In this

manner, some of the challenges outlined above could be addressed in a more streamlined and efficient manner without reducing consumer protection – indeed, it would be possible to enhance it without the need for secondary legislation.

- *Do you have views on how the regulators should be obliged to explain how they have had regard to activity-specific regulatory principles when making policy or rule proposals?*

21. We believe the existing accountability mechanisms (e.g. reports and evidence sessions to government and Parliament) should be applied to these new principles.

Q3. Do you have views on whether and how the existing general regulatory principles in FSMA should be updated?

22. There have been recent calls for the Government to introduce a general Duty of Care on lenders. We believe that the FCA already has an extensive regulatory toolkit for ensuring that customers are well protected and able to seek redress where poor practice arises. The introduction of a general Duty of Care would create another layer of regulation which is likely to generate further uncertainty since its remit is unlikely to be clear for either customers or firms. If there are gaps in consumer protection, these should be plugged by enhancements to the current principles and rules, rather than introducing an additional limb of regulation which requires a costly court-based resolution process, which customers may be reluctant to use and the scope of which would take time and cost to establish with any certainty.

23. The FOS is an important part of the FSMA framework in delivering consumer redress. Consistency in decision-taking is central to promoting preventative action by firms. FCA members are concerned about decisions that are inconsistent and do not seem to align with FCA rules. This underlines the need for greater transparency to promote understanding of how decisions are reached. The time taken to reach some decisions is also a factor in facilitating prevention and some complaints take several years to determine. Also, the valuable free availability of FOS services to consumers is now being exploited by professional claims management companies who often bring unmeritorious and sloppily prepared cases to FOS, for which the lender pays fees even if the case is thrown out by FOS at the first opportunity. FOS and the FCA have both tried to bring these firms into line and the challenge remains. Some thought should be given to more directly penalising this conduct, perhaps by requiring professional complainants to pay a security fee when lodging a claim which goes to offset the lender's fees if the complaint is not substantially upheld. The fee should not be recoverable by the CMC from its client.

Q4. Do you have views on whether the existing statutory objectives for the regulators should be changed or added to? What do you see as the benefits and risks of changing the existing objectives? How would changing the objectives compare with the proposal for new activity-specific regulatory principles?

24. We believe the existing statutory objectives are appropriate, balanced and fit for the future, striking the right balance between consumer protection, competition and market integrity. And we do not see these objectives as inconsistent with the proposal for new activity-specific regulatory principles. Rather, we see Government and Parliament having significant scope to set the framework and strategic direction for each financial activity, subject only to the constraint that this should itself be consistent with the statutory objectives.

25. The FCA needs to be clear on the outcomes it wants to achieve across its regulated markets. This will ensure any change is properly focused on its statutory objectives. The respective responsibilities of consumers and firms should be balanced appropriately. While firms must always be trustworthy and treat customers fairly, consumers should also take some responsibility for their actions, as a zero-risk approach would be disproportionate. Just as the FCA does not operate a 'zero-failure' regime for firms, there should also be some element of this in relation to consumers.

Q5. Do you think there are alternative models that the government should consider? Are there international examples of alternative models that should be examined?

26. The FSMA model is an international exemplar of a proportionate, contemporary, evidence-based and independent regulatory model, and we believe these proposals would both preserve and enhance this. The same cannot, however, be said of the CCA model, which by international standards is disproportionate, inflexible and outdated.

Accountability, scrutiny and stakeholder participation

Q6. Do you think the focus for review and adaptation of key accountability, scrutiny and public engagement mechanisms for the regulators, as set out in the consultation, is the right one? Are there other issues that should be reviewed?

27. We agree with the proposal's premise. Parliament acts as an important check on Government policy, particularly through Bill committees or select committees. They should continue to invite ministers and regulators to give evidence and be accountable for their actions.

Q7. How do you think the role of Parliament in scrutinising financial services policy and regulation might be adapted?

28. Parliament should explore an active role in scrutinising activity-specific policy development and scrutiny of regulators including their supervisory approach. This could be achieved through the existing infrastructure but it may be necessary to establish joint committees with the House of Lords, who not only tend to have more

expertise on technical issues, but also have more time to consider these matters (as they don't have constituency responsibilities). They also have longer tenures thereby ensuring a more consistent approach to scrutiny. A dedicated team of clerks for any new committee is a pre-requisite for enhanced scrutiny. They should be encouraged to engage with stakeholders, including regulators, outside the formal confines of evidence sessions and make recommendations to parliamentarians.

Q8. What are your views on how the policy work of HM Treasury and the regulators should be coordinated, particularly in the early stages of policy making?

29. We support close collaboration between HMT and regulators throughout the policy process. We would emphasise the need to be transparent with stakeholders when formulating policy.

30. We recognise, however, that the HMT / FCA relationship is a critical one and the basis for consultation set out in para 3.31 is sensible. We would recommend that the mechanism be set out in a public memorandum of understanding (similar to those that exist between the FCA and FOS), whereby the outcomes are minuted and disclosable under the Freedom of Information Act.

31. We would also support the standard practice of five-yearly reviews of policies.

Q9 Do you think there are ways of further improving the regulators' policy-making processes, and in particular, ensuring that stakeholders are sufficiently involved in those processes?

32. Recent events on the FCA's forbearance guidance must be the exception that proves the rule. While we accept the need to act urgently to support consumers during the pandemic, four aspects of the FCA's policy-making process were hard to justify: (a) extremely short consultation timeframes, (b) lack of cost-benefit analysis, (c) describing as 'guidance' measures which were clearly intended to have the effect of rules, and (d) giving greater prominence to one statutory objective over the other two. The FSMA model was not designed to operate in this way, in particular when the compliance costs are likely to run into the billions of pounds. Had proper, if accelerated, FSMA processes been followed, it is likely that key aspects of the measures would have been better thought-through and more nuanced – such as on blanket entitlements to payment deferrals, masking of credit file data and bans on terminations and repossession.

33. It is essential that government and Parliament abide by better regulation principles and consultation best practice guidance. An example of this would be roundtable events (prior to issuing a consultation paper) with stakeholders, which were commonplace when UK Government Departments consulted on European legislation.

34. We would encourage government to make use of sector expertise by seconding experts into HMT and FCA when developing new policy frameworks. This has

worked to good effect when the Department for Business (BIS) introduced the CCD between 2008 and 2010. It made use of lawyers working in the private sector. The Working Party approach, where BIS held regular meetings during 2007-8 with experienced industry lawyers when developing the regulations implementing the CCA 2006 was a good sounding board. It is worth highlighting that the more expensive problems with CCA 2006 derive from the Act itself, which benefitted from very little consultation, rather than from the regulations.

Finance & Leasing Association
19 January 2021