appg

All-Party Parliamentary Group on

Alternative Lending

REPORT OF THE INQUIRY INTO 'LENDING AND BORROWING POST-COVID'

MAY-JUNE 2020

INTRODUCTION

THE INQUIRY

The Inquiry into 'Lending and Borrowing Post-Covid' ran from 20 May to 10 June 2020 and covered a wide range of credit-related issues from the availability of debt management services, to consumers' needs for ongoing forbearance and new borrowing, the impacts of the Financial Ombudsman Service (FOS), the future viability of credit files and the likely increase in illegal lending as a result of the pandemic.

It comprised three oral evidence sessions with three key stakeholder groups: money advisers, public policy experts and lenders and industry representatives. The evidence sessions were held via Zoom, with questioning from a panel of MPs and Lords chaired by APPG Chairman, Julian Knight MP. The Panel was fully cross-party with representatives from the main parties in each of the devolved nations.

The aim of the Inquiry was to get an early feel for the impact of the Covid crisis on consumer finances; and a sense of what would be needed in the rebuilding phase to help consumers get back on their feet.

SPECIFICALLY, THE INQUIRY LOOKED INTO:

- The scale and nature of anticipated debt problems post-Covid and their impacts on money advice provision;
- Consumers' short and longer-term forbearance and borrowing needs as they deal with the impacts of the crisis on their household finances;
- What the supply picture needs to look like in terms of new and ongoing lending; and
- What regulatory adjustments might be needed to ensure continuing consumer access to a fluid and functioning credit market, and adequate forbearance from lenders, in the recovery period.

EXECUTIVE SUMMARY

The main output from the Inquiry is the list of Conclusions and Recommendations at the end of this Report. The hope is the report and its recommendations will help to inform policy formulation in response to Covid, so that borrowers are better protected and adequately served, and able to play an active part in our economic recovery.

CONCLUSIONS IN SUMMARY:

- On **money advice**, the extra £38m announced by the Government in June is welcome and timely given the expected rise in debt cases in the aftermath of Covid. This will help to alleviate capacity problems, but agencies will also need to find ways to help new debtor groups they have not encountered before at scale, such as the self-employed and the formerly 'better-off'.
- On **forbearance**, the Financial Conduct Authority (FCA) responded quickly to alleviate borrowing-related problems by instructing lenders to offer 'payment deferrals'. This too was necessary, but lenders will need to be able to use a wider toolbox of forbearance measures to bring borrowers' accounts back under control, instead of just one remedy, the 'payment holiday'.
- Similarly, with regard to **access to credit**, , consumers will need safe, available sources of liquidity to help them to deal with disruption to their budgets and play an active role in the recovery. Alternative, not-for-profit lenders will only be able to meet a fraction of the demand; ministers and regulators need to ensure a viable mix of alternative and commercial providers to ensure the availability of credit at sufficient scale.
- Despite positive sounds from the Treasury at the time of the evidence sessions, ministers have since announced there will be no Bank of England **funding for Non-Bank Lenders**. This is an oversight: NBLs are the 'small boats' that provide working capital to millions of small and micro-sized businesses, plus individual borrowers who banks won't touch. Their inability to lend due to lack of funding would significantly hamper the recovery.
- Concerns about **public sector debt management** techniques have been widely aired. Therefore, the Cabinet Office's consultation on 'Fairness in government debt management' announced in June is welcome. A Government Debt Management Bill, plus a pre-action protocol to prevent any immediate bailiff action against debtors, are ideas well worthy of close ministerial consideration.
- On **consumers' credit files**, again, the FCA moved quickly to prevent the reporting of 'payment holidays' back to Credit Reference Agencies. This might have

helped in the short term, but it will leave 'black holes' in consumers' files for the long run. The FCA and the CRAs need to quickly find a way to restore the integrity of credit files, otherwise both lenders and borrowers will suffer.

- There was significant unease about the **Financial Ombudsman Service's** policies and procedures towards lenders, and more widely about possible statutory over-reach and a lack of accountability. The issues are complex but also fundamental to the future viability of sections of the credit industry. Therefore, ministers should consider a National Audit Office review of FOS's structures and processes, the first in a decade.
- The Panel heard a consistent message about the risk of increased **illegal lending** as a result of Covid: job losses and tighter underwriting policies create perfect conditions; lending business closures and new forms of online illegal lending greatly exacerbate the threat. The Government should address the risk as a priority through a combination of preventative and punitive measures, as detailed in the findings section.

SESSION WITH MONEY ADVISERS

20 MAY 2020

WITNESSES

- **Matt Hartley**, Head of Public Affairs, Money Advice Trust
- **David Hawkes**, Policy and Campaigns Co-ordinator, AdviceUK
- **Peter Tutton**, Head of Policy, StepChange

PANEL

- **Julian Knight MP (Con)**, Chairman, APPG on Alternative Lending
- **Dr. Lisa Cameron MP (SNP)**
- **Chris Evans MP (Lab)**, Officer, APPG on Alternative Lending
- **Baroness Kramer (LD)**, Treasury Spokeswoman in the Lords
- **Lord Sharkey (LD)**, Officer, APPG on Alternative Lending
- **Alison Thewliss MP (SNP)**

The dual focus of this session was the volume and nature of enquires coming into money advice organisations since the Covid crisis started; and what might be expected in the aftermath in terms of debt problems in particular. In written briefings submitted ahead of the hearing, AdviceUK, MAT and StepChange shared some headline statistics and observations regarding enquiries related to Covid.

For AdviceUK members, the biggest increases in demand had related to employment and domestic abuse. The main challenges had been delivering a remote service, equipping staff to work from home and funding (additional IT costs and the loss of funding streams, e.g. Legal Aid). MAT saw keeping up with Council Tax and rent payments as big concerns for many people. Calls into MAT's Business Debtline showed that self-employed people were being hit particularly hard, having suffered a near total drop of income overnight. The debt problems StepChange were seeing were not, at the time of the inquiry, significantly different from the problems they were seeing before Covid. However, a higher proportion of clients gave unemployment as the main reason for their debt problems; and a higher proportion of enquiries were coming from men.

All of the agencies reported lower than expected demand for debt management (StepChange had seen only one third of the volume it saw in the same period in 2019), but a high volume of 'what if' type enquiries. The consensus view was that we are in the 'calm before the storm'. An explanation was the tendency for people to delay seeking debt advice while dealing with their immediate income shock. It is common for people to use credit as a coping strategy, if it is available, even though this may increase the risk of debt problems later on.

Baroness Kramer asked about the storm to come, and how well resourced the agencies were to deal with higher volumes. Peter Tutton said StepChange's experience in the aftermath of the 2008 financial crisis was indicative: a 50% increase in demand immediately after the crisis, which reduced over the following 3-4 years but remained above pre-crisis levels. On the resource question, the common view was agencies would struggle to scale to meet increased demand. David Hawkes said a supply-demand gap already existing before the crisis and would only get worse. Matt Hartley pointed out that scaling is not just a question of money, it's also the time and resource required to train and equip advisers. (Note: this oral session was held before the Government announced a further £38m for money advice on 9 June, taking the total Money Advice and Pensions Service annual budget for debt advice to over £100m.)

> *Between 23 March and 24 April 2020, 443,084 individual users accessed the StepChange Debt Charity website. This is an increase of 116,330 on the same time as last year (326,754) and included 162,818 individual users accessing our pages with information relating to Covid-19.*
>
> **Peter Tutton**, StepChange

Alison Thewliss MP asked about the likely nature of debt problems post-Covid. Matt Hartley flagged different impacts on different demographic groups. New groups are likely to be the self-employed, who have had less Government support, and the 'better-off' who have experienced an income shock. David Hawkes identified women (domestic violence), prisoners (who depend on letters for communication) and students (problems in relation to exams and ongoing liability for accommodation they cannot occupy). There was praise for the speed and scale of the Government's emergency relief packages for borrowers, but central to everything would be how the FCA manages the exit process from 'payment holidays'; consumers of every description will need on-going protections to avoid a cliff edge.

Julian Knight MP asked about consumers' future credit needs. Respondents noted that credit applications were down but would inevitably rise. There was acknowledgement that people would use high cost credit, including credit cards and overdrafts, if no other options exist; and that illegal lending would likely increase given the tighter economic conditions. The England Illegal Money Lending Team would need extra funds to address this problem, which was regarded as a hidden and under-estimated problem partly because money advice clients tended not to disclose the use of illegal lenders. The most vulnerable consumers on benefits would be likely to suffer the most.

Respondents agreed that 'alternatives' to high cost credit needed a boost, for instance the pilot No Interest Loans Scheme. The Social Fund also needed reinstating. StepChange was asked about its proposed 'temporary financial resilience fund' to provide no-interest loans to struggling households. Based on the size of the Hardship Fund for Council Tax (£500m), Peter Tutton suggested a sum in the region of £5bn would be required.

The panel also asked about the ability of credit unions to weather the crisis, especially in light of multiple closures in the aftermath of the 2008-9 financial crisis. Respondents were emphatic about the role they can and should play. Robustness depends on the particular union: some are strong, some more vulnerable. The common view was that 'good credit' would inevitably contract post-Covid: if lenders are doing adequate affordability assessments, they simply wouldn't be able to lend. Hence, 'alternatives' such as credit unions would be crucial. However, Peter Tutton insisted credit provision needed to be 'socialised': credit unions will not be able to serve those in greatest need without government support for lending to this group.

> *There has been a decline in demand for debt advice, probably due to payment holidays and other measures the FCA has taken. Demand for debt advice is likely to rise significantly when these temporary reliefs come to an end.*
>
> **David Hawkes**, AdviceUK

PUBLIC POLICY SESSION
3 JUNE 2020

WITNESSES

- **Anna Ellison**, Director, Policis (think-tank and consultancy specialising in financial services)
- **Tony Quigley**, Head of the England Illegal Money Lending Team
- **Emma Revell**, Head of Communications, The Institute of Economic Affairs (standing in for Victoria Hewson, IEA's Head of Regulatory Affairs)
- **Joe Shalam**, Head of Financial Inclusion & Housing, The Centre for Social Justice

PANEL

- **Julian Knight MP (Con)**, Chairman, APPG on Alternative Lending
- **Dr. Lisa Cameron MP (SNP)**
- **Chris Evans MP (Lab)**, Officer, APPG on Alternative Lending
- **Baroness Kramer (LD)**, Treasury Spokeswoman in the Lords
- **Ben Lake MP (PC)**
- **Lord Sharkey (LD)**, Officer, APPG on Alternative Lending
- **Alison Thewliss MP (SNP)**
- **Sammy Wilson MP (DUP)**

The principle questions explored during this session were the fitness-for-purpose of the current regulatory framework to deal with the crisis and its aftermath; whether certain aspects of the regulatory framework serve to exacerbate consumer harms; and what adjustments might be necessary to ensure an accessible and fluid market for credit, and adequate forbearance from lenders, in the recovery period.

> *Digital channels have enabled the emergence of large and highly damaging online illegal lending markets in the US, Canada and Japan, closely associated with criminal enterprise including, in Japan, serious organised crime.*
>
> **Anna Ellison**, Policis

The Chairman invited short opening comments from witnesses:

Anna Ellison of Policis said access to credit would be the primary issue post-Covid. We would see a reduction in consumer resilience and a fall in the supply and availability of credit. This could lead to a disorderly market and opportunities for criminals to take advantage of the resulting vacuum unless preventative steps were taken by regulators and criminal agencies. She highlighted findings from Policis research in the US, Canada and Japan that illustrated the scale and nature of new forms of 'digital' illegal lending. From a consumer's perspective, illegal lender websites are indistinguishable from legal sites, and often just used to steal the consumer's identity data. Policis's research also revealed digital illegal lending as a major vector to serious organised crime.

Tony Quigley from the England Illegal Money Lending Team said his team had seen a reduction in people making contact during the Covid crisis: the lock-down had apparently impacted the operations of illegal lenders as well. He anticipated a spike in illegal lending post-Covid, with higher unemployment and greater loan delinquency creating the necessary conditions. His team was aware of newer online forms of illegal lending, as well as the extorting of upfront fees, identity theft and the link to organised crime. Illegal lending used to be a face-to-face business; it still is, but it is also becoming digital with some ‘illegals’ even using Facebook and WhatsApp groups.

> *The chief concerns with FOS appear to be a lack of awareness of its processes and certainly its impacts, and a lack of accountability for the predictability and consistency of its decisions.*
>
> **Emma Revell**, IEA

Emma Revell described the IEA’s regulatory affairs programme and its focus on the Information Commissioner’s Office and the Financial Ombudsman Service (FOS) in 2020. She felt there was a general lack of awareness of the constantly expanding role and impacts of FOS amongst the public and even the politicians. This is causing concerns about the accountability of decision-making processes, the fairness and consistency of decisions themselves, and ultimately competition and the availability of products in the marketplace (with a succession of businesses going bust on account claims volumes stacking up in FOS). There are also fairness concerns owing to the absence of an appeals mechanism: businesses are bound by decisions and simply have to pay, without any recourse to appeal. In the consumer credit sector, the effect of FOS’s actions is insolvency for some regulated credit businesses that would otherwise survive; and market exit for many others due the uncertainty surrounding future decisions on ‘affordability’ claims.

Joe Shalam highlighted public sector debt as a major cause of consumer detriment. The Centre for Social Justice had conducted focus groups and analysed Citizens Advice records before lock-down which revealed that 42% of problem debt cases were government related, whereas the equivalent figure for commercial lending had declined from 57% to 32%. A core problem was collections. While the private sector had made real progress with collections techniques, the public sector had not (with the exception of a few central government departments and councils). The CSJ had gathered evidence of outmoded practices, such as councils’ ‘in-year’ collection targets and 2.6m referrals to bailiffs in 2019, as well as blunt debt recovery methods in the welfare system. In response, the CSJ was calling for a Government Debt Management Bill to bring cross-government debt collection practices into line with private sector best practice. CSJ was also starting new research looking more closely into ‘hidden debt’, and specifically illegal and informal lending in the UK.

> *While we have seen huge advances in private sector debt collection practices, the public sector continues to use antiquated and inefficient methods.*
>
> **Joe Shalam**, CSJ

Chris Evans MP asked what illegal online lending looked like in practice. Anna Ellison and Tony Quigley described copy-cat websites indistinguishable from legal, regulated ones; and scam sites with UK-based URLs that actually reside in Eastern Europe or West Africa. A follow up question concerned policing: how could the law be enforced against international operators? Tony Quigley said international coordination of enforcement activity actually worked very well: fake sites can be taken down within 24 hours. Anna Ellison observed that illegal lending, once established, was very difficult to eliminate: the best approach was a regulatory strategy that headed off the growth of illegal markets by balancing market access with consumer protection.

Dr. Lisa Cameron MP probed on local authority debt collection practices. Joe Shalam acknowledged the difficult balance authorities have to strike, given budgetary pressures and in-year targets. Nevertheless, a move towards individualised plans would be better than slavishly following the sequential steps set out in Council Tax collections regulations.

Lord Sharkey asked about the size of illegal lending operations, and what collections practices illegals employ. Tony Quigley said there were few data points on size in the UK: the FCA's 2017 Financial Lives estimates 100,000 borrowers from illegal lenders at any one time; and a further 300,000 using 'friends and family' (for many, a euphemism for unregulated lenders). Tony Quigley put the number of illegal borrowers at 310,000. Anna Ellison quoted Policis findings that 6 out of every 10 small-sum loans in some US states were made by illegals; and one in every 10 in Japan. On collections, she referenced the US Government's 2013 Operation Chokepoint initiative, which had attempted to cut off illegals' access to the payments system. This proved successful for a while, but by 2015-16 illegal lending was back to the same scale.

Baroness Kramer asked what Government can do to shore up legitimate, regulated lending. Joe Shalam suggested demand side measures, such as capping debt repayments from benefits awards: as much as 30% of Universal Credit (UC) standard allowances were being swallowed up by debt repayments before a limit was introduced. There could also be a signposting role for UC Work Coaches. Emma Revell pointed to the deleterious effects of FOS's ex post facto adjudications on the 'affordability' of historic loans, judgements being made in some instances 7-8 years after the loan was originally made. This is driving into administration businesses whose lending practices had been approved by the FCA, and some which had even undergone in-depth Section 166 'skilled person' reviews initiated by the FCA. The uncertainty this causes in the marketplace is having a chilling effect on lenders' appetite to lend, leaving a vacuum for 'second best' choices to fill.

Julian Knight MP asked for views on regulatory adjustments. Anna Ellison observed that regulators had

purposefully and understandably prioritised consumer protection, but might have done so at the expense of credit exclusion. International examples show that excessive regulatory interventions cause a contraction in the alternative lending sector. Demand is suppressed to some extent, but only temporarily. Consumers might initially 'go without' or resort to friends and family, but eventually a black market emerges when these options are exhausted. Typically, this process took 7 years in Japan and US; digital channels had accelerated and scaled the effect.

> *In the US, states which require high consumer protection standards, but also allow large commercial providers to operate profitably at scale, have been far more successful at preventing illegal operations than states with restrictive credit regimes.*
>
> **Anna Ellison**, Policis

To close the session, the Chair asked for one recommendation that witnesses would give to Treasury ministers as they formulate their approach to consumer credit market regulation post-Covid. For Joe Shalam, it was a new Debt Management Bill to deal with problems with public sector debt collection; for Emma Revell, safeguards to ensure regulators strike the optimum balance between protection and access; for Anna Ellison, it was moving the regulatory focus to prevention while regulators still can; and for Tony Quigley, raising the exemption limit in the Consumer Credit Act from £25,000 to £50,000 and raising the maximum prison term for illegal lending to five years from the current two.

> *The FCA's 2017 Financial Lives survey shows that 7% of people in the UK (3.6 million) have a loan from 'friends or family', we want to know how this is affecting family relationships.*
>
> **Joe Shalam**, CSJ

INDUSTRY/ LENDER SESSION

10 JUNE 2020

WITNESSES

- **John Cronin**, Head Analyst, UK Financials, Goodbody Stockbrokers
- **Stephen Haddrill**, Director General, Finance & Leasing Association
- **Peter Reynolds**, Director of Communications, Non-Standard Finance PLC (leading provider of non-prime consumer lending)
- **Graham Wheeler**, CEO, Advantage Finance Ltd (leading provider of finance to independent motor dealers)

PANEL

- **Julian Knight MP (Con)**, Chairman, APPG on Alternative Lending
- **Dr. Lisa Cameron MP (SNP)**
- **Chris Evans MP (Lab)**, Officer, APPG on Alternative Lending
- **Baroness Kramer (LD)**, Treasury Spokeswoman in the Lords
- **Ben Lake MP (PC)**
- **Lord Sharkey (LD)**, Officer, APPG on Alternative Lending
- **Alison Thewliss MP (SNP)**
- **Sammy Wilson MP (DUP)**

The focus of this session was the impact of Covid on lenders' lending and collections performance; the impact of the FCA's 'temporary reliefs' (payment holidays) on customers, collections and future business viability; likely / anticipated demand for new borrowing from consumers post-Covid; the availability of wholesale funding from the money markets to be able to fund new lending; and regulatory adjustments required to ensure a functioning market, and adequate ongoing forbearance for borrowers, in the recovery period.

The Chairman invited short opening comments from witnesses:

John Cronin said the consumer's needs had to come first, and access to credit was critical, therefore. Less affluent households in particular depend on a regular flow of credit for essential and seasonal spending. This is the market served by alternative lenders in the main, and this is where the constriction is taking place. We are seeing a tightening in underwriting which is causing reduced access to products at reasonable cost. Funding for this type of lending is vital to ensure the availability of credit to end-users. This is currently a problem with closed or restricted wholesale markets and no Treasury / Bank of England 'Term Funding' or equivalent in place. How to make the funding available is a technical issue; there should be no question about the principle of providing support.

Stephen Haddrill supported John Cronin's comments on making BoE funding available to alternative, non-bank lenders. FLA members had granted 1.4m requests for forbearance; the Government needed to provide equivalent assistance on the other side of the balance sheet. The other key question is what the FCA does at the end of the 3 month payment holiday period. A further extension would not necessarily be in consumers' best interests; lenders need a full toolbox of forbearance measures to decide what's best for each individual borrower, rather than being constrained to one single response. The other issue is credit performance data: how will lenders be able to calculate affordability accurately post-Covid if there are black holes in borrowers' credit files? It is in the borrower's and the lender's interests for the regulator and industry to find a way to record payment performance.

Peter Reynolds echoed the same points on funding. Collections were down but stabilising, and payment holidays had been granted to c. 20% of customers which risked having a squeezing effect on businesses in the absence of appropriate funding support. But the main problem is how poorly understood the alternative lending sector is. It is a large, vital industry serving a market that banks and credit unions will not or cannot serve. Despite this, it is under siege from a Financial Ombudsman Service that is applying its own interpretation of FCA rules, and one increasingly at odds with that of the wider industry. This is harming consumers by driving up costs, encouraging claims management companies, and driving otherwise sustainable businesses to the wall. The net effect is tighter lender underwriting to limit any increase in FOS-related claims.

Graham Wheeler shared the latest performance data from Advantage Finance. 21% of customers had taken up payment holidays, equating to £8.5m in delayed payments. There had been an 85% year-on-year reduction in sales in March-April, a 50% reduction in May, and a return to parity in June. With regard to payment holidays, a key problem was the fact that customers' financial accounts were standing still while their cars were depreciating, an imbalance that would only be exacerbated by an extended period of payment holidays. Lenders should have a full range of forbearance measures at their disposal, and be trusted to deploy the right solutions to get customers back on track. Also, the 'black holes' in customers' credit files caused by the FCA's instruction not to report payment holidays would erode trust in credit reference agency data and drive a move to Open Banking solutions as a better alternative for assessing affordability.

> *Alternative lenders need access to funding on economic terms – no government support of meaningful significance has been provided, in contrast to the position of the high street banks.*
>
> **John Cronin**, Goodbody

Lord Sharkey picked up the point on credit files and Open Banking: how can the industry get back to accurate judgements of affordability? Graham Wheeler anticipated further use of Open Banking. The obstacles are consumer reluctance and lack of awareness. Peter Reynolds agreed that Open Banking was a positive development but flagged the inadvertent risk of increased exclusion for some groups. On creditworthiness assessments, John Cronin observed that lenders have followed and will continue to follow FCA guidance, but consumers' eligibility for credit will

> *The key question is what follows the FCA's temporary reliefs? What is in the customer's best interests? The answer isn't always additional payment holidays. Lenders need a full toolbox of forbearance remedies.*
>
> **Stephen Haddrill**, FLA

have deteriorated because of Covid and related job losses and income reduction.

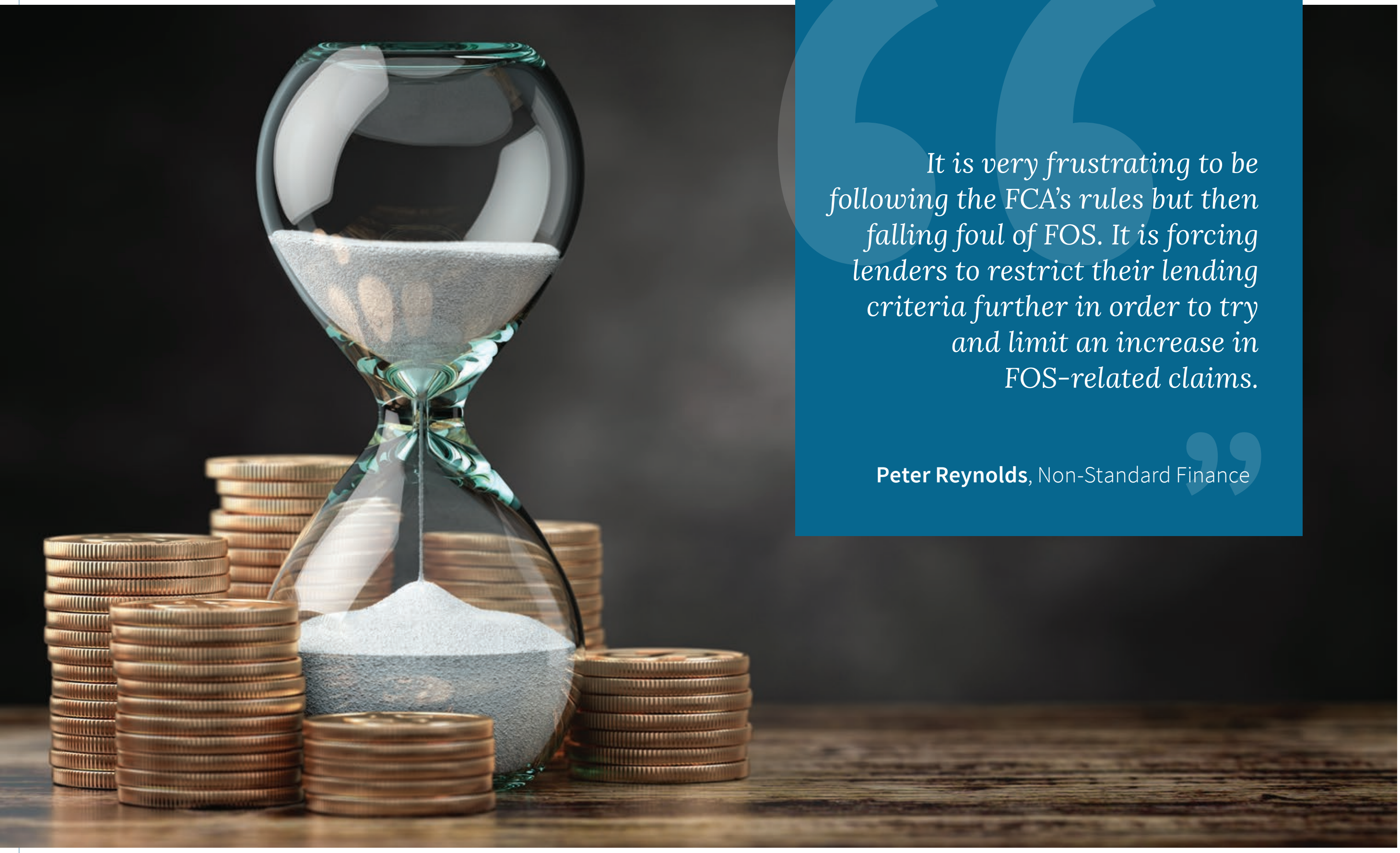
Lord Sharkey also raised FOS and asked what could be done? Peter Reynolds described the frustration of following FCA rules but falling foul of FOS's expectations retrospectively. Lenders are being confronted with erratic, inconsistent decisions but have no recourse to appeal. Judicial Review is an option but limited to one case only, with no read across to wider cases. The risk is credit exclusion because, faced with such uncertainty, lenders will stop lending. Stephen Haddrill said that all his members had the same concerns. There were two sets of rules: the FCA's official rules and then how FOS interprets them. The uncertainty this causes overhangs the market. FOS has not shown itself to be capable of adjudicating in an even-handed way.

Baroness Kramer came back to the issue of funding: are lenders leaving the market or putting up prices? John Cronin said the main impact was a tightening in underwriting and reduced lending. The availability of low cost funding facilities would address lenders' reduced appetite for lending and put alternatives on a level playing field with the banks. If this doesn't happen, problems of illegal lending will increase. Stephen Haddrill described a solution to free up the flow of funds through the banks, where it was tending to get stuck. This involved a BoE guarantee to incentivise through-flow.

Julian Knight MP asked whether the size of the non-prime borrowing population would grow as a result of Covid. Respondents predicted it would. John Cronin said it was an inevitable consequence of banks being more risk averse. This would push more borrowers into the sub-prime net. As a consequence it was essential to ensure good competition in the sector. Stephen Haddrill flagged impaired credit data as an exacerbating factor: Open Banking could have an ameliorating effect but the full benefits remain some way off.

It is very frustrating to be following the FCA's rules but then falling foul of FOS. It is forcing lenders to restrict their lending criteria further in order to try and limit an increase in FOS-related claims.

Peter Reynolds, Non-Standard Finance



CONCLUSIONS AND RECOMMENDATIONS

A number of common themes and conclusions can be drawn from the three evidence sessions. Based on these, it is possible to draw some preliminary policy recommendations to address shortcomings in the markets for credit and debt management. Some of these proposed solutions are already under consideration, or have been announced since the hearings took place in May and June.

1

Money Advice. It is highly likely there will be a marked increase in demand for money advice and debt management in the aftermath of the Covid crisis. It is reasonable to assume a pattern similar to that seen by StepChange in the aftermath of the Global Financial Crisis in 2008-9, when applications for debt advice rose by 50% in a year before gradually falling back to a new level 10-15% higher than the pre-crisis level. In light of this, the extra £38m awarded to the Money Advice and Pensions Service in June is welcome (taking the total annual amount to £100m). In addition to extra financial support, MaPS and individual agencies will need to find ways to assist new debtor groups they might not have encountered at scale before, such as the self-employed and formerly 'better-off' consumers who are reasonably savvy and possibly able to self-serve, but otherwise unfamiliar with debt advice.

2

Ongoing forbearance. A major driver of traffic to money advice will be debt problems arising from job losses and income reduction. The withdrawal of furlough in particular will cause job losses to mount from Q3 2020 onwards. The FCA acted quickly to alleviate debt problems by requesting lenders to provide 'payment holidays' (initially 3 months, extended to 6 months). Payment friezes have undoubtedly brought relief to consumers in the short term, which is what the FCA intended, but they are a blunt tool which could lead to worse outcomes in the longer term. We heard a plea from lenders to be allowed to use the 'full toolbox' of forbearance remedies in order to be able to bring borrowers' accounts under control and avoid imbalances arising (for instance in credit contracts linked to a depreciating asset like a car). Further forbearance support will undoubtedly be required for large numbers of borrowers during the recovery period. The FCA should allow a broader range of lender-led forbearance options instead of restricting assistance to just one solution, payment holidays.

3

Access to Credit. Similarly, consumers will need a full array of financial tools to help them deal with the disruption caused by Covid, so that they can rebalance their budgets and also play an active role in getting the economy back on its feet. Access to new credit needs to be part of the solution, both as a mechanism for bridging income-expenditure gaps, and as a stimulus for renewed spending on the high-street. Alternative providers such as credit unions will need continuing government support so they can play a part. But given the large disparities in size, the commercial lending sector will need to do the heavy lifting. This calls for a shift in mindset amongst regulators and officials, and a deeper appreciation of the role specialist lenders play, particularly in lower income and 'poor credit file' households where banks choose not to tread.

The FCA should continue to address residual concerns with commercial lending models. But ministers and regulators also need to be clear-eyed about the potential for 'alternative' suppliers of credit to supplant commercial providers: it is not going to happen any time soon. Consumers will need access to credit during the recovery; we will need regulated, viable lenders to provide it at the requisite scale.

4 **Funding for Non-Bank Lenders.** The wider alternative lending sector has pushed hard for access to Term Funding or equivalent on the same generous terms as the banks. The mood music from Treasury ministers at the time of the hearings was encouraging, but ministers have since declined to extend access to Bank of England funding for NBLs. The Finance & Leasing Association had produced its own blueprint for bypassing the blockages in the banks and getting funds into the hands of lending businesses that can provide liquidity to SMEs and consumers, and this looked promising. There was universal consensus from panellists that it needed to happen. As one witness put it, the philosophical case is established, the Treasury just needed to find the technical means. Non-bank lenders to SMEs and consumers are dutifully offering extended payment holidays to borrowers. But lenders that are reliant on the wholesale money markets for funding cannot do this endlessly. The lack of funding support could threaten the viability of specialist NBLs, and the Government should keep the situation under close review.

5 **Public sector debt collection.** There is already widespread acknowledgment of the consumer harms being caused by public sector debt collection techniques. Nonetheless, the statistics are stark. Many councils are over-reliant on bailiffs: as many as 2.6m debts were referred to them last year, even though they only recovered 27p of every £1 referred. Additionally, huge amounts of debt are deducted automatically every month from benefits payments. The impacts of Covid will undoubtedly weigh heavily on government creditors, just as they will on commercial lenders. The CSJ's proposals for, firstly, a pre-action protocol to prevent any immediate bailiff action, and, secondly, a Government Debt Management Bill to raise the quality of cross-government debt collection practices, would alleviate a lot of short and medium-term difficulties and are worthy of ministerial consideration. Therefore, the Cabinet Office's consultation on 'Fairness in government debt management', announced since the evidence sessions took place, is timely and welcome.

6 **Borrowers' credit files.** The FCA acted decisively to bring in a range of emergency measures to alleviate the immediate impacts of Covid on borrowers. These included payment holidays but also a halt on the reporting of payment holidays to the credit reference agencies. This is likely to end up helping consumers in the short-term but damaging their interests in the long run. Witnesses in the session with lenders warned about the 'black hole' that any lender would encounter when they came to consult the credit file of an applicant for credit. And faced with stringent affordability rules and the prospect of future claims, it would be brave of any lender to lend in these circumstances, even to a borrower whose finances were demonstrably stable. Witnesses highlighted the opportunity for Open Banking-enabled bank transaction analysis to plug the gaps in borrowers' credit reference files, but lenders using Open Banking solutions would face the same risk of adverse future judgements on their affordability decisions. Hence, the FCA and the credit reference agencies need to find a way re-establish the integrity of credit files without disadvantaging consumers who have taken payment holidays.

7 **Financial Ombudsman Service.** FOS featured prominently in the public policy and lender sessions. It is clear there is significant disquiet with FOS's policies and procedures amongst lenders. At the heart of these concerns are questions about statutory over-reach and a lack of accountability, questions which the IEA has committed to explore. There is no question that a streamlined, easy-to-access dispute mechanism is needed for the huge number of consumer complaints that arise in retail financial services markets; nor that there is a legitimate role for a claims industry that can help consumers get compensation they would not otherwise get. But there is also a risk of the Ombudsman system being abused; and of volume and capacity pressures (i.e. mass produced claims) creating an impetus for process refinements that lead to inconsistent decisions and unfair outcomes. Certainly if FOS were to be usurping the rule-making responsibility of the FCA, that would be a cause for further inquiry by ministers. The issues with FOS are varied and complex and beyond the scope of detailed parliamentary scrutiny. It is an organisation that has undergone rapid and regular change: as the role of the FCA has expanded so has the jurisdiction of FOS. We would therefore encourage ministers to instruct a National Audit Office review of FOS's structures, processes and costs base, the first since 2011, to ensure fitness-for-purpose and value for money.

8 **Illegal Lending.** The Panel heard a consistent message in all three sessions about the risks of increased illegal lending as a result of Covid. As the English Illegal Money Lending Team pointed out, economic conditions are ripe, with job losses, increased loan delinquency and tighter underwriting policies. Policis's research findings from the US and Japan also presage the arrival in the UK of worrying 'new variants' of digital illegal lending, in the form of fake lending sites and scam broking and identity theft operations — all online, all difficult to distinguish from legitimate, legal sites. On top of this, the recent closure of many regulated lenders threatens a perfect storm of increasing demand for credit from consumers, shrinking provision from regulated lenders, and a criminal sanctions regime that fails to disincentivise illegal operators. To head off the worst of this, we suggest three actions. One, more in-depth research to establish the scale and nature of illegal operations in the UK. Two, a review of both the thresholds for regulated lending in the Consumer Credit Act and prison tariffs for illegal lending. And three, consideration of the impacts of the affordability regime and FOS on the viability of regulated suppliers. While Covid inevitably means there is limited bandwidth in Government for wider policy initiatives, we would argue that these are priority requirements in view of the potential for acute consumer harm and the threat of organised crime taking route.

Report of the Inquiry into 'Lending and Borrowing Post-Covid'

May-June 2020

appg

All-Party Parliamentary Group on

Alternative Lending