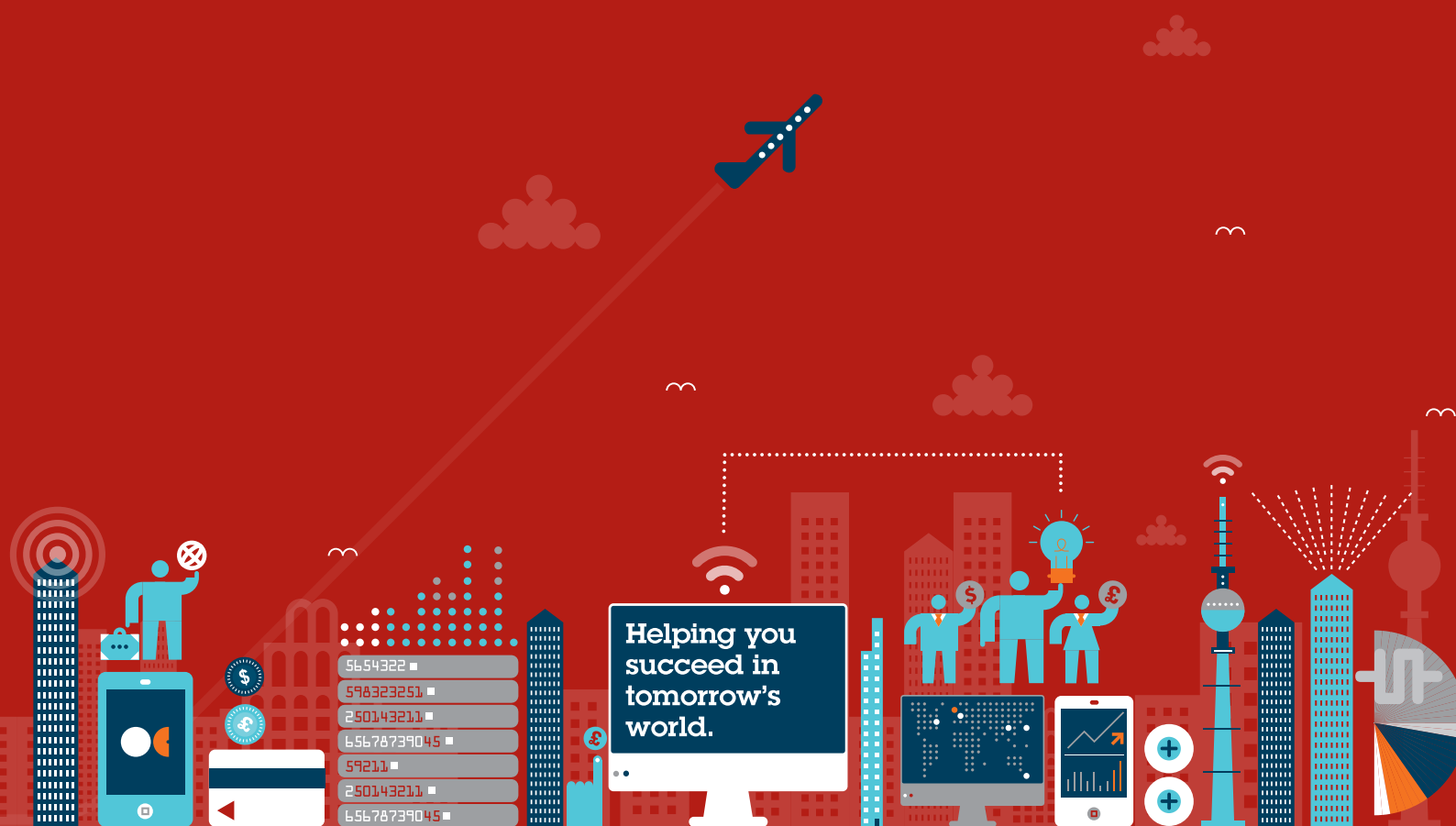


What's on the regulatory agenda for businesses?



Some might say that we are in the middle of a “perfect storm” when it comes to shaking-up consumer finance: we have had a long period of persistently low interest rates and we are witnessing a technological and digital revolution. In the meantime, since the Financial Conduct Authority (FCA) took over responsibility for regulating consumer credit from the Office of Fair Trading (OFT) in April 2014, we have experienced unprecedented levels of regulatory scrutiny and change. Despite this, as firms adapt to keep up, we find that credit is now available more widely, and in more different forms, than ever before.

In this article, we look at some of the key current issues in consumer finance regulation, and the developments that are coming up over the coming months.

FCA looks to post-Brexit future

Since its inception in 2014, the FCA has made efforts to lead on policy, publishing Occasional Papers, designed to stimulate debate on topics like behavioural economics theory, how to predict financial distress, consumer vulnerability and the ramifications of an ageing population. It is unapologetic in taking an approach that first identifies a theory of consumer harm before investigating whether harm does in fact exist. It is, therefore, perhaps unsurprising that in its November 2017 publication *FCA Mission: Our Future Approach to Consumers* it indicated that it is already thinking about policy developments post-Brexit.

In an arguably radical move, it will look at whether there is a need to introduce a new “Duty of Care” for all regulated firms. In other words, it will look at whether its rules (which have the force of law) should impose an obligation on firms to exercise reasonable skill and care in the provision of services to consumers. There also appears to be an acceptance on the part of the FCA that many of the mandatory consumer disclosure requirements that are derived from European law actually hinder effective communication, have a negative impact on consumers and should be reviewed.

Rising consumer debt, vulnerability and breathing space

Interest rates have been consistently low since the 2008 financial crisis. This has reduced the costs of servicing debt and has disincentivised people from saving. According to the FCA, through the late 1980s to the early 2000s, household debt was roughly equally to disposable income, but during the financial crisis, the household debt-to-income (DTI) ratio reached a peak of 160%. It currently stands at around 140% and is forecast to reach 149% in early 2022. Perhaps unsurprisingly, this is an area of focus for both regulators and the government.

To date, however, the governmental and regulatory focus has been somewhat piecemeal. The FCA has considered how to help customers who are “in financial distress” (Occasional Paper 20, 2016), “in persistent debt” (Credit Card Market Study 2016) and “in difficulty” (Financial Lives Survey 2017), in each case using different parameters for the people about whom it is concerned.

This creates an uncertain platform for firms providing financial products to consumers across the product lifecycle, from creditworthiness assessments through account monitoring and on to forbearance and debt collection.

The Treasury is, until 16 January 2018, calling for evidence on whether it should legislate for people who are suffering with “problem debt”. Again, it has created an entirely new set of parameters to define who is affected. In the meantime, the Financial Guidance and Claims Bill has been amended to include provisions requiring the government to legislate. It is, therefore, now a question of when and how the Government will legislate for a debt respite scheme, rather than whether it will do so.

Focus on creditworthiness

During 2017, the FCA has consulted on new rules relating to assessing creditworthiness and affordability, under the guise of improving transparency for regulated firms. Concerns have been raised that the proposals go further than improving transparency and actually significantly change the current regulatory regime. For example, under the proposed rules, firms would not be able to take household income into account, potentially increasing financial exclusion. The FCA aims to publish a policy statement in the first half of 2018.

Overdrafts and high cost credit

As part of its work on consumer vulnerability and access issues, the FCA introduced a payday lending cap in 2015 and has, since then, continued to look at other forms of high-cost credit. The Competition and Markets Authority (CMA) retail banking market investigation concluded in 2016 that a third of bank revenues come from overdraft charges. The CMA recommended that the FCA implement measures to increase overdraft customers’ engagement with their overdraft usage and charges.

In July 2017, the FCA indicated that it is concerned about the long-term use of arranged overdrafts at levels which can be persistent and unsustainable. Its concerns about unarranged overdrafts are broader – that their use is often inadvertent, and charges appear high and complex. The FCA has even gone so far as to say that there is a case for considering the fundamental reform of unarranged overdrafts and whether they should have a place in any modern banking market at all. It plans to consult in Spring 2018 on proposals to change the regulatory regime applying to overdrafts. This may open up opportunities for alternative lenders to innovate and increase competition in this space. The FCA also aims to consult on proposed solutions to problems of financial distress and vulnerability it sees in the rent-to-own, home-collected credit and catalogue credit markets.

Exploratory work on the motor finance industry

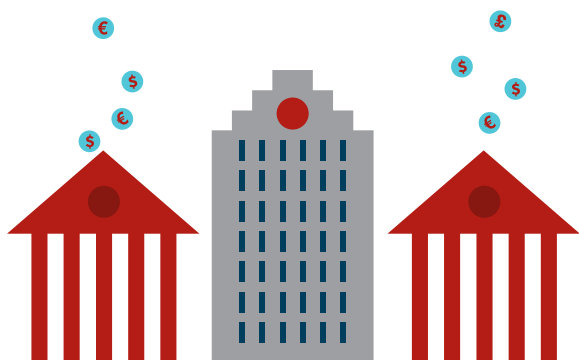
The FCA is currently looking at the motor finance sector, which has grown significantly in recent years. It is considering whether firms are taking the right steps to ensure that they lend responsibly; whether information about hire purchase and hire products is sufficiently clear and transparent; whether there are conflicts of interest arising from commission arrangements between lenders and dealers; and whether risk is being adequately priced. Following its review, the FCA will assess whether and how to intervene in the market. It plans to publish an update in the first quarter of 2018.

There is no doubt that the fundamental difference between a hire product (which does not involve ownership of the vehicle) and a hire purchase product (which can involve ownership of the vehicle but only after payment of a final balloon payment) is not always clear to consumers, and there is clearly potential for a conflict of interest between the dealer's drive to sell and the importance of the consumer being sold finance that is suitable for his or her needs. These issues are, however, highly sensitive, as any intervention by the FCA could have a significant impact on the motor industry as a whole.

Open banking initiative

The CMA retail banking market investigation concluded that older and larger banks do not have to compete hard enough for customers' business, and smaller and newer banks find it difficult to grow. One of the remedies to improve competition has been the open banking initiative. Open banking enables personal customers and small businesses to share their data securely with other banks and with third parties, allowing them to compare products on the basis of their own requirements and to manage their accounts without having to use their bank.

To deliver open banking, a new organisation was created that is working with nine large banks mandated by the CMA, as well as some challenger banks and fintechs to define and develop the required Application Programme Interfaces (APIs), security and messaging standards that underpin open banking. Open banking is tasked with delivering the APIs, data structures and security architectures that will make it easy and safe for customers to share their financial records by the end of January 2018. This date is aligned to the implementation of the Payment Services Regulations 2017 on 13 January 2018, which in turn implement the second European Payment Services Directive. These new regulations will allow authorised third parties to be given consent by the account holder to access their bank accounts to extract statement information and to initiate payments, without having to use their bank's online services. It is envisaged that this capability will then lead to far reaching innovative services being created by new entrants and technology companies, including, of course, lenders.



Extension of the Senior Managers and Certification Regime (SMCR)

In the light of the financial crisis in 2008, the Parliamentary Commission on Banking Standards recommended that the FCA develop a new accountability system that was more focused on senior managers and individual responsibility. In response to the recommendations, the FCA created the SMCR, which replaced the approved persons regime for individuals in banks, PRA investment firms and some insurers in March 2016. The Government announced in 2015 that all regulated firms would be subject to SMCR from 2018. This extension means that all 47,000 FCA regulated firms will now be caught, although, given the diverse range of firms that will be within the extended regime, the FCA has proposed to take a proportionate and flexible approach; splitting SMCR requirements into 'limited', 'core' and 'enhanced' categories. The applicable category will depend on a firm's size, complexity and on the potential impact on consumers. HM Treasury has not yet announced the implementation date for the extension of the SMCR. Originally, it had intended to implement the extension by March 2018, but given that this consultation was only published in July 2017, many believe implementation will now not be until summer 2018. It is also expected that the FCA will take a phased approach to implementing the SMCR.

Review of retained provisions of the Consumer Credit Act 1974 (CCA)

When the FCA took over responsibility for regulating consumer credit in April 2014, some provisions of the CCA were repealed, some were replaced by FCA rules and other provisions were retained. The FCA is required by law to review remaining retained CCA provisions and report to HM Treasury by 1 April 2019 on whether their repeal (in whole or in part) would adversely affect consumer protection. In particular, it must consider which provisions could be replaced by FCA rules or guidance, whilst also considering the principle that a burden or restriction that is imposed on the carrying on of an activity should be proportionate to the benefits.

Between February and May 2016, the FCA asked firms to provide input on the planning phase of its review. It sought initial views from stakeholders on a number of issues, in particular whether the FCA should prioritise particular provisions for review, the timescales for review, and the conduct of the review, including engagement with stakeholders. The report to HM Treasury must be preceded by at least one interim report on which the FCA has consulted. The FCA has since been considering the responses to the call for input. It has, however not yet published a summary of the responses (which it promised in the first half of 2017); nor has it yet outlined the scope for the review, and the approximate timelines through to 1 April 2019. A contributing factor to the delay could be Brexit, as some of the retained provisions implement the European Consumer Credit Directive. We do, however, anticipate further regulatory activity in this space over the course of 2018.

Please see overleaf for the important dates for your diary.

Dates for the diary

Overdue

FCA to publish a summary of the responses to the Call for Input on the retained provisions of the Consumer Credit Act and scope for the review

Q4 2017

FCA due to publish policy statement on new rules to address persistent credit card debt

January 2018

Payment Services Regulations 2017 in force and APIs, data structures and security architectures for open banking in place

Q1 2018

FCA due to publish update on motor finance exploratory work

Spring 2018

FCA due to consult on proposed new rules for overdrafts, rent-to-own, home-collected credit and catalogue credit products

May 2018

GDPR in force

H1 2018

FCA due to publish a policy statement on creditworthiness rules

Summer 2018

Extension of SMCR to all FCA-regulated firms

Osborne Clarke in numbers

725+

talented lawyers

working with

240+

expert Partners

in

25

international locations

advising across

8

core sectors

with

1

client-centric culture

Key contacts



Nikki Worden

Partner

T +44 20 7105 7290

nikki.worden@osborneclarke.com



Charlotte Harris

Associate Director

T +44 20 7105 7585

charlotte.harris@osborneclarke.com

Our locations around the world

Europe

Belgium: Brussels

France: Paris

Germany: Berlin, Cologne, Hamburg, Munich

Italy: Brescia, Busto Arsizio, Milan, Padua, Rome

The Netherlands: Amsterdam

Spain: Barcelona, Madrid, Zaragoza

Sweden: Stockholm

UK: Bristol, London, Reading

USA

New York, San Francisco, Silicon Valley

Asia

China: Shanghai

Hong Kong

India: Mumbai*

Singapore

Osborne Clarke is the business name for an international legal practice and its associated businesses. Full details here: osborneclarke.com/verein/

* Relationship firm

osborneclarke.com