RESPONSE TO DEBT PACKAGERS: PROPOSALS FOR NEW RULES

FINANCIAL CONDUCT AUTHORITY

Introduction

1 The Institute of Chartered Accountants of Scotland (ICAS) is the oldest professional body of accountants and represents over 22,000 members who advise and lead business across the UK and in almost 100 countries across the world. ICAS is a Recognised Professional Body (RPB) which regulates insolvency practitioners (IPs) who can take appointments throughout the UK. We have an in-depth knowledge and expertise of insolvency law and procedure.

2 ICAS's Charter requires it to primarily act in the public interest, and our responses to consultations are therefore intended to place the public interest first. Our Charter also requires ICAS to represent its members' views and protect their interests. On the rare occasion that these are at odds with the public interest, it is the public interest that must be paramount.

3 ICAS is interested in securing that any changes to legislation and procedure are made based on a comprehensive review of all the implications and that alleged failings within the process are supported by evidence.

4 ICAS is pleased to have the opportunity to submit its views in response to the Financial Conduct Authority (FCA) consultation on proposed new rules surrounding debt packagers (CP21/30). We shall be pleased to discuss in further detail with the FCA any of the matters raised within this response.

Our approach to the consultation

5 We have adopted the following approach in drafting our response, in the hope of producing a more accessible submission:

- While we are responding to each of the questions, we also include an executive summary below to highlight our key comments.
- We have made some additional comments relevant to the consultation covering areas not captured by our answers to the questions posed.

Executive summary

6 ICAS is supportive of both the sentiment and aim of this proposal. However, there are some areas of concern once the finer points of the proposals are considered in more detail and inter-connected issues are more widely considered. Further comments are set out in the detailed responses to the consultation questions.

7 Overall, this proposal is welcomed when viewed in isolation. We however note that it is not going to be a panacea for the harm identified and targeted by the proposals – consumers receiving non-compliant debt advice which is biased towards debt advise which may not meet the needs of the consumer. This market is one widely known to "adapt". Much wider and co-ordinated action by the FCA, Advertising Standards Authority, The Insolvency Service and the Recognised Professional Bodies (RPBs) is still required.

8 ICAS is extremely concerned that the proposals may lead to an increased emphasis and focus on lead generators whose activities are unregulated. There is significant concern from anecdotal evidence that lead generator firms stray, intentionally or unintentionally, into the regulated activity of debt-counselling. Without increased focus and resources allocated to the monitoring and pursuance of action against such entities where they are carrying on regulated activities without the appropriate authorisation, we are concerned that the potential for consumer harm will not be adequately addressed.

9 The anticipated outcome of the proposals is that debt packagers business model will no longer be viable. The (unstated) outcome of this of course would be that those requiring debt advice would have to find alternative sources to obtain that advice. The stated preference is that debt advice is provided by the not-for-profit sector. This sector is already struggling to cope with demand and lacks capacity to absorb further demand. We are therefore concerned that impact

of the proposals might be felt by those who are most vulnerable and unable to access the debt advice that they need.

10 The proposals for new rules present an opportune moment to revisit the ability of Insolvency Practitioners to provide consumer related debt advice. In particular, the limited insolvency exclusion provided for in paragraph 52(2) of the Schedule to The Financial Services and Markets Act 2000 (Exemption) Order 2001 has resulted in some peculiar outcomes, particularly when also viewed alongside the provisions of Part XX of the Financial Services and Markets Act 2000.

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Question 1: Do you agree with our assessment that the remuneration model for debt packager firms is driving consumer harm?

ICAS agrees that advice provided should have regard to the customer's best interests and not be biased towards debt solutions merely because they generate revenue.

The evidence presented in the consultation and the prior reports strongly supports the view that some firms within the 'debt packager' market are unable to resolve this inherent conflict of interest and leads to individuals being guided towards certain solutions.

An IVA/PTD will not always be the wrong solution. Indeed it is likely that an IVA/PTD may be one of several options available to an individual, each option having advantages and disadvantages to a greater or lesser extent. Given that individuals in problem debt are more likely to suffer anxiety, adverse effects on their feelings and emotions as well as difficulty in decision making, it is not unreasonable to assume that initial debt advice has a significant bearing on the choice that will end up being made. We therefore agree that the initial contact and communication during this initial contact needs to have a significant focus on it.

Question 2: Do you agree that the only effective remedy is to ban receipt of remuneration for referrals by debt packager firms?

Overall, this proposal is welcomed but it is not going to be a panacea. This market is one widely known to "adapt". Much wider and co-ordinated action by FCA, Advertising Standards Authority, The Insolvency Service and the Recognised Professional Bodies is still required.

The ICAS Insolvency Committee's views on this matter were sought and concerns were expressed that debt packagers will circumvent the ban by attaching themselves to an existing insolvency firm (whether at the instigation of the debt packager or the insolvency firm), or debt packagers recruiting an IP.

However, it is achieved, the consensus of the Committee is that the market will find a way to work around the new Rules.

We make further comment on the Rules in response to question 5.

Question 3: Do you agree that we should not include debt management firms or not-for-profit debt advice firms in our proposals?

Given the different business models of debt management firms and not-for-profit providers, as outlined in the consultation paper, ICAS agrees that these should not be included in the proposals.

Question 4: Do you have any comments on our proposed obligation on debt management firms who act as principals?

The paper outlines the risk that debt packager firms could look to become appointed representatives of a debt management firm and thus circumvent the ban. As a result, the proposals include an obligation on debt management firms who act as a principal to ensure that none of their appointed representatives receive any remuneration from debt solution providers unless the appointed representative is genuinely acting as a debt management firm itself.

This has been identified as an area open to abuse and therefore the proposed solution makes sense. However, this perhaps demonstrates that there are likely to be weaknesses with the new rules that the market will adapt to and exploit.

The paper goes on to say, *"We will be monitoring this actively".* Additionally, at Paragraph 1.10 the paper states "*Consumers who seek debt advice are more vulnerable to harm due to being in financial difficulties. They need protection from non-compliant, biased advice which could cause them to enter debt solutions which are not in their best interests. Our existing rules, when complied with, should help provide this protection".*

This perhaps alludes to a significant barrier to the new rules having the desired effect. The consultation paper acknowledges that the current rules would offer the appropriate protection if complied with. The

fact that further action is required to be taken must then be because they are not being complied with and because there is insufficient effective enforcement taken to ensure compliance with the rules.

It does not matter how effective the new rules are in theory, if the FCA is not resourced and able to adequately enforce them then they will not achieve their intention.

We highlight again the risk that unregulated lead generator firms may end up providing regulated activity and that as a result of insufficient and ineffective enforcement action being taken the objective of the new rules will be eroded.

Question 5: Do you have any comments on the draft rules?

We consider that the wording used within the proposed addition to the CONC sourcebook at 8.3.9 R (2) lacks sufficiency to achieve the desired objective.

The reference to '[receiving only] an insignificant amount of its total annual revenue from providing *debt solutions." w*ill allow existing debt packagers to potentially restructure their business in a manner which could allow circumvention of the intended outcomes. In particular, the way this is drafted would mean that a firm receives more than what would be considered to be an insignificant amount of total revenue from the provision of debt solutions then the new rules are not applicable.

It is not clear what is meant by an 'insignificant amount' and is a highly subjective term. Does this mean less than 1%, less than 10%, or some other value?

We appreciate the difficulties that exist in setting out parameters. It is often difficult to do so in such a way as to take account of a variety of entity types and mix of services which may or may not be undertaken by business organisations. The proposed wording does have the advantage that it perhaps is less restrictive and capable of being used in a wider variety of business situations, however the consequence is that is it open to wider potential abuse.

To avoid the possibility of entity and operational restructuring to work within the boundaries of what is permitted and to achieve the desired outcome, we believe that the rules would require a much higher threshold to be established. In other words, for a firm to be considered as providing debt solutions itself, then the total revenue from debt solutions should be substantive.

Unless hard cut-off thresholds are to be established, irrespective of the approach adopted additional guidance should be incorporated to assist with the interpretation of subjective terms.

Question 6: Do you have any comments on the planned implementation period?

The proposed implementation period (subject to the outcome of the consultation) is 1 month. That is clearly a very short period, notwithstanding the reasoning set out in the consultation paper. We make no comment on whether such a short implementation period would cause particular concerns or issues.

We would however note that it is unclear from the draft instrument and draft rules how these would apply to existing arrangements and how any transition would be managed or applied. For example, a pre-existing contractual arrangement may exist where a debt packager had provided services prior to the new arrangements coming into force but had not yet received payment. Would the outstanding payment become prohibited?

Transitional and saving provisions should be clearly set out in the instrument.

Question 7: Do you have any comments on, or relevant additional data for, our draft cost benefit analysis?

The draft cost benefit analysis does not appear to recognise the costs likely to be incurred from the movement of data gathering and analysis in relation to consumers assets, liabilities, income and expenditure from debt packagers to debt solution providers (paragraphs 64-70). Assuming debt packagers are removed from the market then the requirement to ingather and analyse data relating to the consumers position will still require to be undertaken prior to debt advice being provided. Where this will now require to be undertaken by debt solution providers such as IPs the costs of doing so may

be higher than if such work was carried out by debt packagers. This is due to the variance in staff costs and operational overheads from debt packagers to professional service firms.

As noted elsewhere, there is a risk that as a result of the policy adopted lead generators participation in the wider market may become more prevalent. We have highlighted the risk that lead generators may stray, intentionally or unintentionally, into areas of regulated activity. The draft cost benefit analysis does not consider the impact of this and the potential for increased supervisory/regulatory action costs for the FCA in this respect.

If the changes achieve the desired result then the focus in a regulatory sense will switch from debt packagers to IPs, and the due diligence they are undertaking in respect of leads. The monitoring aspect of debt advice will consequently shift from the FCA to the RPBs, which will have implications for ICAS and the other RPBs. ICAS does not currently regulate IPs who utilise debt packagers in sufficient numbers to provide any meaningful estimate of the additional cost on RPB regulatory activities.

See below comments relating to provision of debt advice.

Additional comments

Provision of debt advice

Paragraph 1.12 of the consultation concludes that the proposed new rules "*will end the debt packager business model*". If that is the case, then it can reasonably be expected that debt packagers will largely cease to exist. The most obvious concern arising because of this is where does the displaced debt advice demand end up? The clear indications from the consultation are that the FCA preference is for debt advice to be provided by the free debt advice sector. However, that sector is already short of resources, struggling to meet demand and has called clearly and loudly on repeated occasions for additional funding.

The estimate within the consultation paper, based on an FCA survey and Money and Pensions Service (MaPS) data, suggests that debt packager firms represent a small proportion (3%) of firms offering debt advice. The FCA survey for the period April 2019 to March 2020 estimates that 54,000 individuals sought advice from a debt packager against the MaPS data which indicates that 1.7 million people receiving debt advice in 2020.

That estimate appears to be considerably lower than ICAS would expect. However, whether accurate or not, the consultation paper acknowledges the FCA's own expectation that *"demand for debt advice will increase significantly over the coming years"*.

The MaPs paper cited in the consultation goes on to state *"In our most recent survey 1.7m people said they had received debt advice, and we estimate (from the same survey) that a further 3.6m people needed debt advice because they had been regularly missing payments throughout the last six months".*

It is therefore clear that the displaced debt advice demand arising from the new Rules will be placed at the door of a sector ill-equipped to absorb it. As a result, this seems to present an opportune moment to revisit the restrictions on insolvency practitioners to provide debt advice.

When consumer credit regulation was transferred to the FCA on 1 April 2014, a regime change took place for IPs. While there was previously an authorisation regime which allowed IPs to conduct a wide range of consumer credit activities through the Group Consumer Credit Licence, this was replaced by a more limited insolvency exclusion, with any IPs conducting work outside this exclusion potentially needing to consider full FCA authorisation.

The insolvency exclusion allows an IP to conduct debt adjusting, debt counselling, debt administration and debt collecting when formally appointed as an IP under Section 388 of the Insolvency Act 1986, or conduct debt counselling, debt adjusting or credit information services in reasonable contemplation of being appointed under Section 388.

IPs are educated and examined in the provision of debt advice to individuals as part of their extensive and rigorous professional qualification. They are regulated, professionally qualified and subject to

ongoing oversight and required to undertake continuous professional development and knowledge updating. As such they should be permitted to provide the regulated activities of debt advice and debt management in totality and not only when it is in contemplation of an appointment. This would serve to assist in alleviating the additional burden that will fall on the free debt advice sector.

Advertising

While there are rightly many concerns with the debt packager operating model, one positive it has brought has been to highlight through large scale advertising that there are options available to those in problem debt.

Without this type of advertising in the market, how does that same messaging reach those who need advice? If the wider profile of debt advice and debt solutions isn't replaced it will mean that people who should be obtaining debt advice won't come forward. This can lead to a significant number of non-financial consequences for those individuals, including a substantial impact on their mental health and general wellbeing.

However, it is also worth stating that with the proliferation of advertising specifically citing IVAs and Trust Deeds as solutions for individuals in problem debt, many individuals are likely to have made a decision before they reach the stage of discussing solutions with debt packagers or IPs. Those adverts are placed by unregulated lead generators, demonstrating a need to consider holistically how to appropriately address consumer harms. Simply striking out debt packagers in isolation does not seem to us to adequately deal with the root cause of this issue.