ICAEW
REPRESENTATION 119/21

CP21/30: DEBT PACKAGERS: PROPOSALS FOR NEW RULES

Issued 20 December 2021

ICAEW welcomes the opportunity to comment on consultation *CP21/30: Debt packagers: proposals for new rules* published by Financial Conduct Authority on 17 November 2021, a copy of which is available from this link.

We share the FCA's concerns about the role of debt packagers and lead generators in the IVA market.

We believe that this should be addressed through co-ordinated action by both FCA and Insolvency Service. If the FCA proposal is taken forward in isolation there is a risk that the activity in question will continue through involvement of lead generators who are not regulated by either FCA or insolvency regulators. It is difficult to see that this would be in the public interest.

We would, in principle, support changes to insolvency regulation along similar lines to the FCA proposal. However, there will be challenges in framing proportionate regulation and in policing the rules. We note that the FCA has itself been unable to police this sector to its satisfaction and ongoing difficulties should therefore be anticipated even with a co-ordinated approach.

We believe that there is a case for more radical reform and that government should consider moving responsibility for regulation of consumer IVAs to the FCA.

ICAEW
Chartered Accountants' Hall Moorgate Place London EC2R 6EA UK
T +44 (0)20 7920 8100 F +44 (0)20 7920 0547 icaew.com

This ICAEW response of 20 December reflects consultation with ICAEW's Insolvency Committee which is a technical committee made up of Insolvency Practitioners working in large, medium and small practices.

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KEY POINTS

QUALIFIED SUPPORT FOR THE PROPOSAL

1. We have considered the proposal only insofar as it relates to IVAs.
2. We agree that too many debtors are entering into IVAs in cases where there would be better alternatives for them. We also agree that FCA authorised debt packaging firms who refer debtors to IVA providers for a fee are part of the problem including because of conflicts that are not being properly managed.
3. If, as seems to be the case, the FCA is unable to police the activity sufficiently to ensure compliance with its rules, then we agree that the proposed ban is an appropriate step.
4. We agree that alternatives such as capping referral fees could be problematic for reasons identified in the consultation. We also agree that possible avoidance measures should be anticipated, so that, for instance, the ban should cover associates and relevant remuneration generally.
5. However, the proposal may lead to adverse consequences. It also addresses only one concern about the debt advisory and debt solutions market. Looking at the issue more holistically, we believe that more extensive regulatory reform is required.

POSSIBLE ADVERSE CONSEQUENCES

Increase in unregulated activity

6. The proposals only cover FCA authorised 'debt-packager' services and according to the FCA this will 'end the debt packager business model'.
7. However, the concerns relate not just to debt packagers (who provide debt advice) but also to lead generators who may not provide advice (or therefore need to be FCA regulated).
8. The proposal does not, therefore, address the whole problem. Indeed, it may result in expansion of the unregulated lead-generator business.
9. While the FCA may perceive dealings between IPs and unregulated lead-generators to be a matter for the insolvency regulators (see further below), it will nevertheless need to ensure that any 'lead-generator' services provided by non-FCA authorised persons do not, in fact, constitute debt-counselling (which would require FCA authorisation). The distinction may not always be clear cut.

Need for co-ordinated regulatory action

10. The proposal will require some existing materials of the insolvency regulators to be updated to reflect the change. For instance, the Insolvency Service's consumer IVA protocol and its guidance on Monitoring Volume Individual Voluntary Arrangement and Protected Trust Deed providers currently refer to use of FCA authorised lead generators and/or debt packagers or for introducer firms to be FCA authorised. Any necessary changes should be made at the same time as the FCA's changes to ensure regulatory coherence.
11. More significantly, insolvency regulation has in part relied upon FCA regulatory control over debt-packagers. As it will no longer be able to do so, there is likely to be a knock-on effect for insolvency regulation. We comment below on some of the challenges in that respect, but as a matter of principle we believe that the FCA initiative should be co-ordinated with the Insolvency Service and that the overall impact should be assessed, and measures implemented, in a holistic way.

Challenges for insolvency regulation

12. In principle we would support changes to insolvency regulation along broadly similar lines to the FCA proposal. However, the detail would require consideration.
13. In keeping with FCA's conclusions, we think it likely that some market participants will seek to organise (or characterise) the relevant activity in ways that avoid breaching rules, but which could still result in cases being channelled into IVAs when other processes would be preferable. For instance, lead-generator services to IVA providers currently often include collating relevant information about a debtor. That activity might currently be characterised as, or included within, a 'referral' arrangement (caught by a prohibition on referral fees) or could be a self-standing service (which might not be caught).
14. The broad prohibition proposed by FCA has the advantage of simplicity and clarity (and we share FCA's concerns about permitting relevant fees up to a certain level). However, before adopting a similar approach the insolvency regulators would need to assess the potential impact on the market. For instance, it is possible that lead-generators could provide such services more efficiently than an IVA provider, so that simply banning the practice might adversely impact the market.
15. Another area of potential difficulty for insolvency regulators is that they regulate IPs as individuals. It can be difficult for the regulators to identify any payments not made through individual estates of debtors. If an IVA provider were to make payments to an introducer from the provider's own funds, there is little regulatory remit to review their records to identify it. This is, in our view, a flaw in the insolvency regulatory regime and we comment further on that below.

Impact on the IVA and debt advice market

16. As one of the outcomes of the proposals will be to reduce the number of IVAs carried out relative to other available processes, some economy of scale may be lost and IVAs may become more expensive (and so appropriate for even fewer cases). The need for good advice and access to alternative processes will thus remain of vital importance.
17. The consultation appears sanguine about an increased role for not-for-profit providers (**NFPs**). However, our impression is that they are already stretched and may not have resources necessary to fill any gap left by the proposed ban. Their input on the FCA proposals will be vital because, if they cannot provide the services required, it is unlikely that the objective of ensuring that debtors have ready access to good quality advice will be met.
18. The FCA notes that some NFPs are partly funded through referral fees, including from IVA providers. The FCA has concluded that the level of referral funding allows a distinction to be drawn between commercial and NFP providers, but, in principle, similar risks of conflicts arise. In practice, that risk may grow if NFPs step into the shoes of debt-packagers (and the referral fees they formerly benefited from). The FCA will need to ensure that the difficulties encountered in the for-profit sector do not arise in the NFP sector.
19. Provision of information or advice on personal debt and potential debt solutions is increasingly made through on-line channels. There will be an incentive for IVA providers to develop these platforms following changes to the lead generator model and as consumers seek more 'remote' and less face-to-face advice. It will therefore become increasingly important that the regulatory status of such channels is clear and that involvement of unregulated entities does not result in poor outcomes due to any weakness in the regulatory regime.

UNDERLYING ISSUES THAT NEED TO BE CONSIDERED

20. Understandably the proposal is limited to difficulties that are within the FCA's powers to address. But these difficulties are just a symptom of more fundamental issues that, in our view, call for government action (see our response to the consultation on breathing space reforms for more detail on this - Rep 16/19).

21. In considering the various issues and possible solutions, it is important to bear in mind that providing professional debt advice takes skill, time and can involve risk. In short, when provided on a paid-for basis, it can be expensive. But those seeking the advice are inevitably (with rare exceptions) those who can least afford it.

22. While we agree that debt-packaging and lead generator activity has resulted in over-use of IVAs, there are other reasons why debtors may end up in a process that is not, objectively, the 'best' for them (at least from a financial perspective).

23. In many cases, bankruptcy would be the more logical alternative. But debtors may be deterred from taking that route due to the stigma that is still associated with it, and the £680 upfront fee. This is a substantial amount for those in financial difficulty and inevitably a deterrent when compared to processes such as IVAs that appear to be 'free' at point of entry (even if they ultimately cost more).

24. Debtors also seek quick solutions to immediate financial distress (and the emotional distress that accompanies it). Debt-packagers and lead generators may not be doing a good job in crucial respects (as explained in the consultation), but they do appear to be effective at reaching debtors, obtaining basic information about them, and providing a rapid 'solution' (good or bad). Unless NFPs are as effective in these respects, debtors may suffer detriment.

25. While it appears from the consultation that FCA has been liaising with Insolvency Service, we believe there is regulatory tension arising from split responsibilities. The proposal moves many of the problems associated with debt-packaging from the FCA to the insolvency regulators, but the insolvency regulators already face challenges in the consumer IVA sector as noted above.

ICAEW SUGGESTIONS FOR FURTHER REGULATORY CHANGE

26. Assuming FCA proceeds with its proposal and subject to a considered impact assessment by the Insolvency Service, we believe that the insolvency regulators should introduce equivalent measures, ie broadly speaking, ban IPs/IVA providers from paying fees to lead-generators (albeit mindful of the challenges noted above).

27. As noted above (and in our Rep 16/19) there are a number of concerns about the IVA market. We note that Insolvency Service is planning a review of the personal insolvency regulatory landscape as part of its 5 year strategy. We believe that it, and government, should consider changing the regulatory regime so that IVA firms are regulated, rather than just the IPs within them.

28. Indeed (again, as noted in Rep 16/19), we think there is a case for consumer IVAs to be regulated by FCA rather than the insolvency regulators. The same might apply to consumer bankruptcies, so that a single regulator (suited for the purpose) is responsible for all consumer debt solutions.

29. Unless and until such reforms are made, the availability of debt advice by non-FCA authorised professionals will be important. We note, however, that under the current regulatory regime many IPs are, in effect, excluded from providing the full range of debt advice despite being among the best qualified to do so, as explained in our Rep 10/18. While IPs might currently only meet a relatively small amount of the overall need, no source of appropriate advice should be disregarded. Therefore, as a matter of principle and

regulatory coherence, government should address this by allowing IPs to provide a full range of debt advice without the need for FCA authorisation.

ANSWERS TO SPECIFIC QUESTIONS

Q1: Do you agree with our assessment that the remuneration model for debt packager firms is driving consumer harm?

30. Yes.

Q2: Do you agree that the only effective remedy is to ban receipt of remuneration for referrals by debt packager firms?

31. Yes (in practice, given the circumstances outlined in the consultation).

Q3: Do you agree that we should not include debt management firms or not-for-profit debt advice firms in our proposals?

32. We neither agree nor disagree.

Q4: Do you have any comments on our proposed obligation on debt management firms who act as principals?

33. No, we have not considered this in detail.

Q5: Do you have any comments on the draft rules?

34. No,

35. we have not considered them in detail.

Q6: Do you have any comments on the planned implementation period?

36. A one-month implementation period for such a decisive change seems short but, given previous regulatory enforcement activity, perhaps not unreasonable in itself. We would like to see equivalent changes made to the insolvency regime at the same time, but it is most unlikely that this could be done in the timescale envisaged by FCA.

Q7: Do you have any comments on, or relevant additional data for, our draft cost benefit analysis?

37. Please see our key points above on potential consequences of the proposal. As regards the usefulness of cost benefit analysis of this kind generally, see our response to the recent BEIS consultation on *Reforming the framework for better regulation* (ICAEW Rep 94/21).