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Podcast 5: Horizon scanning

Joanne: Welcome to the latest episode in the Allen & Overy podcast series "*In Credit*". My name is Joanne Owens and I'm counsel in Allen & Overy's financial services regulatory group. I'm joined by senior associate Victoria Ferres and also associate Sophie Skeet.

In keeping with these turbulent times, 2021 promises to turn into a regulatory rollercoaster. We'll hopefully have more details when the FCA publishes its Business Plan in early April, but in the meantime we thought we'd do a round-up of matters coming down the line for consumer credit and mortgages.

Victoria: It's of course impossible to cover everything, but we tried to give a flavour of some of the things we know are on the way. More than in other years, however, we are also expecting the unexpected, as the UK continues to adapt to the coronavirus pandemic and life post-Brexit.

Sophie: The plan is to address four categories of anticipated regulatory developments:

- first off, we'll consider a couple of the big picture changes in the credit space, such as Brexit and the LIBOR transition;
- we'll also run through some of the key consumer credit updates, such as the Woolard Review and the Breathing Space regime, as well as some of the updates expected in the mortgages space; and
- finally, we'll take a look at expected amendments to conduct/SMCR rules.

Some of these were in fact ongoing projects due in 2020 that were delayed when the government and the regulators scrambled to respond to the pandemic. 2021 should see a number of these projects come back to life.

<u>Big picture changes: Brexit and LIBOR</u>

Joanne: Let's start with Brexit – it should be fresh in our minds, given the recent end of the transition period. To date, the main policy and legislative efforts in the retail space have centred on onshoring and correcting any deficiencies in EU-derived rules. For example, from 30 May 2021, firms must have changed the name of SECCI (Standard European Consumer Credit Information) in their standard form pre-contractual document and removed references to SECCI from regulated consumer credit agreements.

Victoria: So the SECCI is no longer a SECCI?

Joanne: Exactly! It's the end of an era. Although on paper this is a relatively minor change, as we know from previous changes to the standard form documents, it can be a fairly big operational effort to implement these changes. We expect that work is already under way for a lot of firms to ensure that systems and operational changes are in place ready for compliance with the new requirements at the end of May. But that's certainly not the end of the story.

Victoria: Policymakers are aware that the Financial Services sector lacks an overarching sense of direction post-Brexit. In the first half of 2021, HM Treasury will publish a second consultation paper on the post-EU regulatory framework. In addition, the UK government is expected to publish a white paper on the future of the UK Financial sector at some point in 2021. These papers might not have an immediate impact, particularly in the retail lending space, but will lay the groundwork for the future regulatory environment. It will also be interesting to see how the UK reacts to the European Commission's plan to publish a legislative proposal in Q2 2021 amending the Consumer Credit Directive. Shared issues – such as coronavirus, data use and digital transformation – have exposed flaws in the CCD that the UK too will be forced to consider, regardless of Brexit. It will be interesting to see whether the UK will study and adopt the same solutions.

Joanne: We'll think about this in a future podcast!

Sophie: Another big change is the planned discontinuation of LIBOR, which will predominantly affect firms offering mortgages and sophisticated retail lending products. The LIBOR cessation date falls at the end of 2021, with the exception of certain commonly used USD LIBOR tenors, which will continue to be published until mid-2023. The FCA and PRA expect all boards and senior managers to put in place the appropriate arrangements to identify their firms' legacy LIBOR exposures and ensure an orderly transition away from LIBOR before the relevant dates. Even if a firm does not themselves provide, distribute or transact in products linked to LIBOR, it may have links to LIBOR in its systems or contractual relationships with other firms.

Joanne: Pending the development of new term rates, firms ceasing to use new LIBOR-linked products appear to be one of the few certainties of 2021. The FCA updated its conduct FAQs in November 2020 to drive home the importance of an active transition. The regulator expects firms' senior managers and boards to understand the risks associated with LIBOR transition and take appropriate action to move to alternative rates before the end of 2021. An overarching concern for the FCA will be whether firms have taken reasonable steps to treat customers fairly. The 'fairness' of any transition will be closely linked to a firm's governance and decision-making (does it have a clear paper trail showing that it is striving to make the best choices for its consumers) as well as its communications strategy (are its customer comms clear, fair and not misleading?). There is a lot to think about here.

Consumer credit updates: the Woolard Review, the Breathing Space scheme and delayed regulator publications

Victoria: We can also be fairly confident that 2021 will be a big year for industry-specific developments. Given the uncertain nature of the UK's recovery, firms will need to be flexible and ready to adapt to regulatory coronavirus guidance at speed and without lengthy consultation. The FCA also intends to progress its programme of work that has been in train since it took over regulation of the consumer credit sector in 2014 – although much of this activity has been paused because of the pandemic.

Jo, Sophie, what would you advise listeners to watch out for in the credit space?

Joanne: Top of the list for me would be future work by the government and FCA following the publication of the Woolard Review on 2 February 2021. In case you missed it, we discussed some of the key findings from this in our previous podcast. In particular, there were a number of urgent recommendations identified in the report, including the need to:

- bring buy-now pay-later products within the scope of the regulatory perimeter;
- ensuring there is secure provision of debt advice, especially through the recovery from coronavirus; and
- maintaining a sustained regulatory response to the pandemic.

Following on from Mr Woolard's urgent recommendations, it will be interesting to see how the government and the FCA respond to the recommendations and how quickly it seeks to action the recommendations, particularly in the buy-now pay-later space. Early indications from HMT suggest that it agrees with Mr Woolard's proposal to regulate buy-now, pay-later products so we should expect a consultation on this in the coming months.

Sophie: We're also likely to see a lot of work on debt management activities. Evidently, a large part of this is driven by coronavirus. We've spoken in a previous podcast about the 31 March 2021 deadline for consumer credit customers to apply for an initial, or further, payment deferral under the FCA Payment Deferral Guidance. By way of reminder, the existing guidance stipulates that no payment deferral should extend beyond 31 July 2021, being the last day that the FCA Payment Deferral Guidance is in force. Given the latest round of government restrictions, however, it seems unlikely that these deadlines will remain fixed or that this is the last we've heard on coronavirus payment deferral measures.

Joanne: In the debt management sector, we also shouldn't forget the upcoming implementation of the Breathing Space scheme which will come into force on 4 May 2021. Consultations and industry engagement has been ongoing for some time with respect to the scheme, so whilst it did not originate in the Covid-19 outbreak, it is certainly timely. The objective is to incentivise customers in difficulties to seek professional debt advice promptly so they can enter into an appropriate debt solution. The FCA published a consultation in October 2020 on proposed changes to the FCA Handbook to clarify certain of the FCA's rules in light of the requirements of the regulations. The deadline for consultation responses was 6 January 2021, so we expect the FCA to publish a policy statement in due course.

Sophie: Nevertheless, we wouldn't suggest waiting around for the FCA's policy statement! On 24 December 2020, Treasury published its guidance for creditors and debt advisers to support their interpretation of the regulations. We therefore expect that a lot of lenders will have been following the ongoing work in relation to the scheme and may have started their implementation projects to meet the 4 May compliance deadline. Although, we understand that the Insolvency Service has recently written to the non-technical working group involved in this project indicating that the creditor portal will not be ready for scheme launch on 4 May. This means that there will be no portal that allows creditors to see their breathing space notifications in one place and creditors will need to organise for themselves contact between them and the debt advisers by email or telephone until the portal is available.

What about you, Victoria? What are you keeping an eye out for?

Victoria: I think it will be interesting to see what happens with delayed regulator publications. The FCA is expected to publish its interim report on the Credit Information Market Study, which was previously delayed by the FCA as a result of responding to the coronavirus pandemic. The Woolard Review suggested that there are significant opportunities to build a better credit information market to the benefit of both consumers and lenders. As a result, it recommended that the market study is resumed and that the FCA should, in particular, look at how to improve the speed and sharing of information across the credit sector.

Previous indications suggested that the FCA would publish an interim report at some point in 2021 with the final report following later on this year together with a consultation on any proposed remedies (if necessary). It will be interesting to see whether the recommendations in the Woolard Review will escalate those timings.

Joanne: The FCA is also planning to consult during 2021 on removing the minimum repayment amount from the manual repayment screen of credit card, store card and catalogue credit customers. Again, this was part of the package of remedies proposed in responses to the findings in the credit card market study. The key findings suggested that the majority of credit card repayments were made manually and not by direct debit where repayment screens were anchored to the minimum repayment amount. FCA research suggested that de-anchoring the minimum repayment amount from that screen had a dramatic positive effect and significantly increased the value of repayments made.

Mortgages update

Joanne: Think that covers it for credit! Let's move on to talk about what 2021 has in store for the mortgage market. Again, we should expect lots of activity given the FCA's recent work on mortgage prisoners, the loyalty penalty and switching but we can discuss some of the key highlights.

Sophie: There are a couple of pressing deadlines in Q1 2021. The first was 15 January 2021, which was the deadline for mortgage firms to contact mortgage prisoners about mortgage switching options. This deadline was extended to allow for the development of mortgage products that were otherwise hampered by Covid-19.

Victoria: Mortgage prisoners will remain a focus for the FCA for some time to come. We should therefore expect further announcements from the FCA on this topic during the course of 2021. There have been calls on the FCA to consider not only implementing a cap on lender's standard variable rates but also extending its regulatory perimeter.

In any event, the FCA was due to publish a consultation on mortgage switching in 2020 off the back of the findings in Occasional Papers 54 and 55 and the Mortgage Switching Research Report. The FCA's research suggested there was a case for the FCA to intervene to help mortgage customers who do not switch, but this work was delayed due to the impact of Covid-19. The consultation paper, due in Q1 2021, is therefore intended to set out the potential remedies to engage customers in the switching process, set out the case for switching and to ensure that customers get enough information to help them switch.

Sophie: The next key date is 31 March 2021, the deadline for mortgage customers to apply for an initial, or further, payment deferral under the FCA Payment Deferral Guidance. 31 July 2021 is the current date set for the expiry date of the FCA Payment Deferral Guidance and payment deferrals issued under the guidance should not extend beyond this date. However, as noted earlier in connection with the Credit Payment Deferral Guidance, this depends on the course the pandemic takes and may not be the FCA's final position. Fair treatment of customers in payment difficulties as a result of Covid-19 will continue to be a key area of focus.

Joanne: To round off on the topic of mortgages, I'll touch quickly on other dates you will no doubt already have in the calendar.

Further changes to the FCA's product sales data reporting requirements come into force on 1 April 2021, and the end of July 2021 is the date by which the updated product sales data mortgage reports are to be submitted to the FCA. Updated performance sales data mortgage reports need to be submitted to the FCA by the end of August 2021.

On 31 October 2021, temporary guidance for borrowers of maturing interest-only and part-and-part mortgages, which enables them to delay repaying the capital on their mortgage, is due to expire.

Conduct update: key publications and operational resilience

Victoria: That takes us on to the final section of this podcast. From a conduct perspective, 2021 should bring us the following FCA publications:

- we are expecting the regulator to publish its views on whether its approach to treating customers fairly is sufficient to cover data ethics in financial services;
- there will also be a discussion paper on reviewing the Principles for Business;
- as well as a consultation paper on the proposal to introduce a regulatory duty of care in Q1 2021 following on from the Duty of Care Feedback Statement which was published back in April 2019 (the consultation was delayed as a result of the pandemic); and
- finally, draft guidance on the fair treatment of vulnerable customers.

Sophie: Each item builds on key themes that we touched on in previous podcasts, including the increasing focus on data use and customer vulnerability.

Joanne: Turning to operational resilience, another key focus of EU and UK regulators alike, the FCA, PRA and BoE should publish in Q1 this year policy statements and final rules to introduce an enhanced operational resilience framework following consultations in December 2019. The earliest date for firms and financial market infrastructures to be required to implement [an] enhanced operational resilience framework will be 31 December 2021.

Victoria: Finally, let's talk briefly about SMCR. You'll no doubt be aware that there is an upcoming deadline on 31 March 2021. This is the date by which [the] FCA['s] solo-regulated firms must have completed fitness and propriety assessments and certified relevant employees, as well as trained non-senior managers and certification regime staff on the conduct rules.

Certain firms may also have relied on the FCA's modification by consent to the rules for senior management cover. This was a coronavirus measure and expires on 30 April 2021. From that date, the maximum period for which an employee can cover a senior management position, without requiring FCA approval, drops back from 36 weeks to 12 weeks in a consecutive 12-month period

Joanne: And that brings us to the end of this podcast. If you have any thoughts or comments, or indeed requests for future podcasts, please don't hesitate to get in touch.

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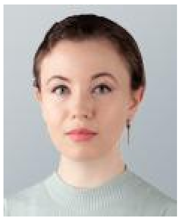

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