The Future of Insolvency Regulation

BSA Response

March 2022

Building Societies Association

Summary Response

The Building Societies Association (BSA) represents all 43 UK building societies, as well as six large credit unions. Building societies have total assets of nearly £430 billion and, together with their subsidiaries, hold residential mortgages over £335 billion, 23% of the total outstanding in the UK. They hold over £295 billion of retail deposits, accounting for 18% of all such deposits in the UK. Building societies account for 39% of all cash ISA balances. They employ approximately 42,500 full and part time staff and operate through approximately 1,470 branches.

We are **supportive** of the proposals to reform the regulation of the insolvency market and agree that **now is the time** to review the current outdated framework for its regulation. Creating a single regulator, a public register of practitioners and firms offering insolvency services as well as a compensation scheme should result in better protection for vulnerable clients through common standards in terms of both services provided and oversight/discipline of the practitioners providing them

We particularly **welcome the proposals that seek to introduce regulation of firms offering insolvency services**. This regulatory gap has been exploited in the past often to the detriment of vulnerable individuals, and our members have many examples of people being "advised" into an Individual Voluntary Arrangement (IVA) in circumstances where that was not the route that would have delivered the best outcome for those people.

The issue that we see rests with the potential length of time that it may take to enact and implement the primary legislation required to introduce these reforms, particularly the creation of a single regulator. As the country emerges from a pandemic, and with rising household costs and soaring energy costs, there is much greater scope in the short term for people's financial position to be adversely impacted. If there is a mechanism by which these measures, or their equivalent, can be introduced in short order, even on an interim basis, the rewards of protecting vulnerable consumers would be reaped, and we comment on the potential for that later in this response.

Government may wish to consider whether an approach similar to the one adopted when the Financial Services Authority (FSA) became the single regulator for the financial services sector could be adopted to increase the pace of the planned reforms. When the government announced in May 1997 its proposals to introduce legislation to reform how financial services was regulated, steps were taken before the Financial Services & Markets Act (FSMA) was enacted or commenced to transfer the day to day conduct of current regulation of financial services to the FSA. That was effected by transferring certain functions under the Banking Act 1987 to the FSA via the Bank of England Act 1998, and in other cases the FSA contracted with other bodies to perform regulatory functions on their behalf. For example, the Treasury contracted with the FSA to perform certain functions under the Insurance Companies Act 1982, and many staff transferred to the FSA at that time and relocated to its head office. Comparable arrangements were made with the various Self-Regulatory Organisations – PIA, IMRO, SFA etc. These covered a gap of at least two to three years until the new legislation was enacted and took effect.

We have responded to those questions that are of most relevance to the firms we represent.

Response to Questions

Question 1. What are your views on the Government taking on the role of single regulator for the insolvency profession?

We support this proposal, subject to our comments above regarding the need to ensure that the process is completed as quickly as possible, and all possible routes to achieve rapid interim solutions having been fully explored.

Question 2. Do you think this would achieve the objective of strengthening the insolvency regime and give those impacted by insolvency proceedings confidence in the regulatory regime?

Yes. We believe that this would achieve the stated aim of ensuring consistency in approach to the provision of insolvency services and how the regulation surrounding it is enforced. That in turn should lead to a stronger regime and greater public confidence in it.

Question 3. Do you consider the proposed objectives would provide a suitable overarching framework for the new government regulator or do you have any other suggestions? Please explain your answer.

Broadly, yes. We have the following comments:

1. Rather than focussing on securing ***fair treatment*** for those impacted by insolvency, there is an argument to frame the objectives around the concept of ***fair or good outcomes***, which is the approach that has been taken by the Financial Conduct Authority, most recently in its proposals for the introduction of a new consumer duty. While the FSA/FCA approach historically referred to treating customers fairly, its experience has shown that a focus on securing good/fair outcomes is instrumental in improving higher standards of behaviour among the firms and individuals it regulates.

2. It may be helpful to expand the objective which refers to a regulator which "supports those regulated in complying….." The concept of a supportive regulator is good, but we think that reference should also be made to supervision and enforcement which would reinforce the overarching purpose of the changes. Firms may not always perceive strong supervision and enforcement to be supportive.

3. The wording of the objective which refers to the promotion and "maximisation" of return to creditors could be reworded to take account of potential situations where maximisation of return to creditors might be at odds with another objective. Perhaps "optimisation" would be better.

Question 4. Do you consider these to be the correct functions for the regulator in respect of Insolvency Practitioners and in respect of firms offering insolvency services? Please explain your answer.

The functions appear appropriate. We have the following questions/comments;

1. The first function covers setting the requirements for authorisation to act as an Insolvency Practitioner. We consider that this should be expanded to say "act and

continue to act" in order to be clear that the professional body will set standards for ongoing competence and not just at entry to the profession.

2. We think it is important that when performing its functions (especially in relation to the handling of complaints) the regulator is specifically required to act in a fair and impartial manner.

Question 5. Are there any other functions for which you consider the regulator would require powers? Please explain your answer.

The intention is to include handling complaints against insolvency practitioners, and we agree that that is appropriate. Consideration should be given as to whether or not the regulator should also be given the power to award compensation to those adversely impacted by the action/inaction of a practitioner or firm.

We suggest that where the regulator delegates certain of its activities, provision is specifically made requiring them to do so in a cost effective way and in a manner that ensures they have the level of oversight necessary to ensure the activity is carried out in line with expectations and statutory/regulatory requirements.

In the consultation, reference is made to the level of fees often charged in relation to the provision of insolvency services and our members are also concerned about this issue. Of particular concern is the often disproportionate level of fees and the unsavoury practice of artificial elongation of the process (to increase the total of fees due). As a result, far too high a proportion of the debtor's limited cashflow is swallowed up by the IP's fees and little comes through to creditors – giving the whole IVA process a bad name. An egregious example was the unjustified additional fee that a large volume IP firm attempted to impose on its IVA clients in 2020. It would be helpful if the government could tackle this general issue through this consultation, in tandem with the FCA's proposals to address this in the context of fees chargeable by debt packagers.

Question 6. Do you agree that the single regulator should have responsibility for setting standards for the insolvency profession? Please explain your answer.

We agree that this is appropriate, and that adopting a principles-based approach would be an effective way to proceed.

Question 7. Do you agree that it would help to improve consistency and increase public confidence if the function of investigation of complaints was carried out directly by the single regulator? Please explain your answer.

We think there is some risk in this approach from a perceived independence and effectiveness perspective at the very least. Even where steps are taken to ensure there is no overlap between the investigation of the complaint and any decision on imposing a regulatory sanction, the very fact that these two functions would sit under the umbrella of one body could create the perception of a lack of segregation even if that were not the case in practice. Given that one of the reasons for creating the sole regulator is to restore public confidence in the service, any such perception, whether valid or not, has the potential to undermine that.

Question 10. In your view should the specified functions be capable of being delegated to other bodies to carry out on behalf of the single regulator? Please explain your answer.

We agree that the functions identified as being capable of delegation are appropriate, provided that there is an appropriate level of due diligence and ongoing oversight by the regulator of their activity.

Question 11. Are there any other functions that you think should be capable of being delegated to other bodies to carry out on behalf of the single regulator? Please explain your answer.

No. The other functions should rightly sit with the regulator itself to ensure an appropriate degree of control and consistency of approach.

Question 12. In your opinion would the introduction of the statutory regulation of firms help to improve professional standards and stamp out abuses by making firms accountable, alongside insolvency practitioners? Please explain your answer.

Introducing statutory regulation of firms will in our view undoubtedly help drive better professional standards and reduce the likelihood of abuses. However, it cannot do that in isolation, and essential to the success of such a measure will be the regulator's willingness and ability to supervise and enforce effectively. Government will need to ensure that it is appropriately resourced to meet the challenges that rigorously enforcing requirements will create.

Question 16. If so, would you envisage that the senior responsible person would be an Insolvency Practitioner? If not, please specify what requirements there should be for that role?

We do not have a strong view on this, but do consider that it is not necessary to be an Insolvency Practitioner to be able to assess whether or not a firm is complying with the regulatory regime. Arguably, someone who is not in that position is perhaps better placed to independently assess the rigour with which the firm complies.

Question 18. What is your view on the regulator having a statutory power to direct an Insolvency Practitioner or firm, to pay compensation or otherwise make good loss or damage due to their acts or omissions? Please explain your answer.

The regulator should have the power to do both of these things, provided that it is able and empowered to act in a fair and impartial manner. The proposed amount of £250 does not seem appropriate when considered in relation to other bodies such as the Financial Ombudsman Service (FOS) which currently has a tiered system based on its assessment of the harm caused. While something of that nature may be considered too complex in this context, the maximum level that may be awarded should be increased. Where distress caused is significant, limiting an award to £250 is not in our view appropriate.

Question 19. What is your view on the amount of compensation that the regulator could direct an Insolvency Practitioner or firm to pay for financial loss? Please explain your answer.

Here, we again look to the operation of the FOS, which for complaints brought today could award up to £355,000. We see no reason why there should be a lesser limit for cases relating to insolvency given the potential adverse impact on a person's life and property of, for example, receiving inappropriate advice.

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The Building Societies Association (BSA) is the voice of the UK's building societies and also represents a number of credit unions.

We fulfil two key roles. We provide our members with information to help them run their businesses. We also represent their interests to audiences including the Financial Conduct Authority, Prudential Regulation Authority and other regulators, the Government and Parliament, the Bank of England, the media and other opinion formers, and the general public.

Our members have total assets of over £435 billion, and account for 23% of the UK mortgage market and 17% of the UK savings market.