

Consultation - Regulation of consumer credit activities and SRA's role and obligations as a Designated Professional Body

26 June 2015

The SRA is an independent regulator of legal services providers in England and Wales. This consultation has been published in order to seek the views of our stakeholders, including those we regulate, consumers and their representatives.

Background

1. This consultation invites views on our proposals to regulate consumer credit activities carried on by SRA-authorized individuals and firms under Part 20 of the Financial Services and Markets Act 2000 (FSMA). In summary, following changes which took effect on 1 April 2014, FSMA prescribes that certain consumer credit activities must be regulated. These activities include credit broking, debt adjusting and debt counselling¹. From that date, regulation of consumer credit activities transferred from the Office of Fair Trading (OFT) to the Financial Conduct Authority (FCA). Under Part 20 members of a "Designated Professional Body" (DPB), such as firms authorized by the SRA, are exempt from the requirement to be authorized by the FCA in order to carry out FSMA regulated activities.
2. This consultation follows an earlier consultation in October 2014 in which we sought views on whether to withdraw from the Part 20 regime in relation to the regulation of consumer credit activities². Following that consultation, we decided that there was benefit in us remaining within the Part 20 regime and we have engaged with the FCA in developing proposals for proportionate regulatory arrangements to allow us to do so. Under Part 20, we are required to make rules which govern the provision of consumer credit activities, which must be approved by the FCA and the Legal Services Board (LSB). These must be in place by the time the existing transitional provisions expire³. The FCA has recently extended these provisions until April 2016, on the understanding that we will publish our final regulatory arrangements in November 2015.

¹ This is not an exhaustive list. The "credit-related regulated activities" are set out in full in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

² <http://www.sra.org.uk/sra/consultations/consumer-credit-activities.page>

³ Transitional provisions require SRA-authorized firms that carry on consumer credit activities under the Part 20 exemption to comply with the provisions and guidance in relation to such activities that were in force immediately before 1 April 2014; these include provisions in the Consumer Credit Act 1974, secondary legislation made under that Act and OFT guidance

3. This consultation is seeking responses to our proposed new regulatory requirements governing those activities which we consider should remain with the SRA (set out in amendments to the SRA Financial Services (Conduct of Business) Rules 2001 (the Conduct of Business Rules) and the SRA Code of Conduct 2011 (the Code)) as well as our proposals for those activities for which we suggest FCA authorisation should be required (set out in amendments to the SRA Financial Services (Scope) Rules 2001 (the Scope Rules)). We would welcome views of solicitors and firms on the likely impact of our proposals on their practice, and to hear views about the impact of our requirements on consumers.

Scope of regulation

Exclusions and exemptions

4. As stated in our October 2014 consumer credit consultation paper, we have worked closely with HM Treasury and the FCA to secure an extension to some of the existing exclusions which narrow the scope of the activities which require regulation under FSMA.
5. We have been successful in doing so: Firstly, the "contentious business" exclusion in the Financial Services and Markets Act 2000 (Regulated Activities) Order (RAO) has been extended, via the Financial Services and Markets Act 2000 (Miscellaneous Provisions) Order 2015 (SI 2015/853) which came into force on 24 March 2015, to cover work carried out prior to issue of, and/or in contemplation of proceedings. This will allow certain consumer credit activities, such as debt collecting, to be excluded from regulation under FSMA where those activities are undertaken by solicitors (or other persons authorised under the Legal Services Act 2007) in the course of providing advocacy services or litigation services.
6. In addition, the exemption in article 60F of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO) has been amended by the Financial Services and Markets Act 2000 (Miscellaneous Provisions) (No 2) Order 2015 (SI 2015/352).to increase the number of instalments over which services/transactions can be financed. With effect from 18 March 2015, the number of instalments that fall within the exemption increased from four to twelve.
7. As the legislative changes were not retrospective, arrangements entered into before 18 March 2015 remained regulated under the previous provisions. You can access [further information about these legislative changes](#) on our website.

Scope of Part 20 and proposed prohibitions

8. Under Part 20, consumer credit activities may only be carried out under SRA regulation where the services are provided in a manner which is *incidental* to the provision of legal services (s327(4) of FSMA) and, in relation to the provision of a particular professional (legal) service to a particular client, the activity *arises out of, or is complementary to* that service (s332(4) of FSMA).

9. Our overarching aim is to ensure that firms can continue, under SRA regulation, to undertake the consumer credit activities that are, in line with the scope of Part 20, ancillary to their legal practice. Further, we would like to provide clarity around the kinds of activities which we believe are distinct and specialist consumer credit services that should be regulated by the FCA, as the specialist financial services regulator with the appropriate experience and expertise. Providing a clearly defined list of prohibited activities also enables us to adopt a streamlined and proportionate set of regulatory requirements, focussed on what is required to ensure consumers are appropriately protected in relation to those activities which we believe are related to the practice of law.
10. Therefore, we propose to amend the Scope Rules to prohibit those we regulate from carrying out the following consumer credit activities under Part 20:
- entering into a regulated credit agreement as lender except where the regulated credit agreement relates to the payment of disbursements or professional fees;
 - exercising, or having the right to exercise, the lender's rights and duties under a regulated credit agreement except where the regulated credit agreement relates to the payment of disbursements or professional fees;
 - entering into a regulated consumer hire agreement as owner;
 - exercising, or having the right to exercise, the owner's rights and duties under a regulated consumer hire agreement; or
 - operating an electronic system in relation to peer to peer lending or entering into (or exercising or having the right to exercise rights and duties under) a peer to peer lending agreement.
11. It is proposed that restrictions will apply to firms carrying on permitted consumer credit activities. These restrictions will prevent firms from:
- providing the client with credit card cheques, a credit or store card, credit tokens, running account credit, a current account or high-cost short-term credit
 - holding a continuous payment authority over the client's account
 - taking any article from the client in pledge or pawn as security for the transaction (pawn broking)
 - entering into a regulated credit agreement as lender which is secured on land by a legal or equitable mortgage
 - acting as lender under a regulated credit agreement which includes a variable rate of interest

- providing a debt management plan to a client (a debt management plan is a non-statutory agreement between a client and one or more of the client's lenders, the aim of which is to discharge or liquidate the debts by making any payments to a third party which administers and reviews the plan and distributes money to lenders)
- charging a separate fee for, or attributing any element of the firm's fees to, the provision of credit broking services.

The proposed changes to the Scope Rules are set out in **Annex 1**.

12. Our initial discussions with stakeholders have indicated that it is uncommon for firms to undertake the activities listed above, unless conducting business which requires separate authorisation with the FCA. However, we have not to date collected targeted information from those we regulate about the consumer credit activities that they carry out, and those for which they have sought FCA authorisation to date. Therefore we are particularly keen to seek information as part of this consultation regarding whether stakeholders agree with our assumptions in this respect. If we are prohibiting activities that fall into the above category, and this is likely to have a detrimental impact on firms and consumers, please do let us know and provide details of any additional protections that you believe would be appropriate to put in place in light of any risks these activities may present. We will review the proposals, and the list of proposed prohibitions, in light of this information.
13. We are aware that certain arrangements with regards to the payment of professional fees might include the taking of security for credit arrangements (for example, in family matters). We have taken these type of arrangements into account when drafting our proposals and tried to ensure that they will be permitted; in particular there is a restriction on credit secured on land but this only applies where the land is secured by way of a legal or equitable mortgage. We would welcome any views on this subject, including the likely impact of the prohibitions and restrictions as currently worded on firms and their clients. We would propose to adjust the prohibitions and restrictions if it appears that our proposals would not allow these arrangements to continue.
14. We would like to hear whether any firms currently charge fees for or gain profit from credit broking services and, if so, what form these fees or other arrangements take⁴. We would also welcome views on the likely impact of the proposed restrictions around credit broking fees as currently worded on firms and their clients.

Consultation questions

Question 1 - Do you agree that it is appropriate for the consumer credit activities set out above to be 'prohibited' from regulation by the SRA under Part 20 FSMA?

Question 2 - What is the likely impact of the prohibitions and restrictions for firms and consumers?

⁴ Please note 4.1(c) of the Scope Rules which provides as one of the basic provisions that:
(c) the firm accounts to the client for any pecuniary reward or other advantage which the firm receives from a third party.

Question 3 - Should any of the prohibited activities be allowed, or the prohibitions/restrictions be modified?

Question 4 - If so, do you believe that any additional consumer protections should be put in place to address any specific risks that these activities present?

Proposed changes to the Conduct of Business Rules, the Code and the SRA Handbook Glossary 2012

15. We have striven to ensure that any changes to our rules in relation to the carrying on of permitted consumer credit activities are made only where necessary and wherever possible avoid unnecessary duplication of existing SRA requirements. Our existing regulatory framework is designed to ensure high standards of competence and professionalism, and incorporates stringent qualification and authorisation requirements for entry to the profession, and robust enforcement powers to ensure our standards are maintained. In relation to consumer credit activities, the FCA's approval criteria require us to develop rules which are equivalent to those within the FCA's Consumer Credit sourcebook (CONC). We have mapped our existing principles and outcomes against the relevant provisions in CONC, and propose to issue guidance to explain how these apply to the provision of consumer credit activities and are, in that context, equivalent to CONC.
16. However, there are some areas in which new rules are required in order to achieve the appropriate levels of consumer protection as set out in CONC, or as a result of requirements prescribed in legislation such as the Consumer Credit Directive (2008/48/EC).
17. In summary, we propose amending our Conduct of Business Rules to include certain requirements intended to ensure that firms:
 - communicate effectively, in a manner which is fair and transparent;
 - before entering into or proposing a regulated credit agreement, appropriately assess clients' creditworthiness, and provide clients with adequate explanations to enable them to make informed decisions;
 - ensure transparency when engaging with third parties and when assigning rights under an agreement; and
 - provide clients with a degree of flexibility with regards to payments due in respect of two or more credit agreements.
18. We are proposing a change to the Code to include '*regulated credit agreements*' under the requirements set out in indicative behaviour 6.1 which provide that introductions to third parties will only be made where in the best interests of the particular client and the agreement is suitable for the needs of that client.
19. Finally, we have introduced new defined terms into the SRA Handbook Glossary 2012. The majority of the defined terms have been taken from the FCA Handbook Glossary and adapted where necessary.

20. The proposed changes to the Conduct of Business Rules, the Code and the SRA Handbook Glossary 2012 are set out in **Annex 1**.
21. It is our intention to develop guidance that will complement these changes to help provide clarity for firms and provide illustrative examples of practices/behaviours that we consider would comprise a breach of the Principles or a failure to achieve the Outcomes in relation to consumer credit activities. Our Professional Ethics Helpline (including the dedicated service for small firms) will also be available to help firms comply with our new regulatory requirements. This is likely to be supplemented with a frequently asked questions document, case studies and/or questions of ethics to help firms make the transition to the new arrangements.
22. We are aware that the FCA may review and change parts of CONC from time to time, for example in light of the wider review of the FCA's approach to unfair contract terms⁵. We will consider the implications on our rules and guidance of any such changes to CONC on an on-going basis.

Consultation question

Question 5 - Do you have any comments on the requirements set out in our proposed amendments to the SRA Conduct of Business Rules?

Impacts of proposals

23. As stated earlier, we have not to date collected from SRA-authorized firms specific information about the consumer credit activities they carry out that could help measure the impacts of these proposals.
24. Overall we consider that the proposals are likely to have a positive impact on both consumers and SRA-authorized firms. The proposals provide equivalent consumer protections to those set out in CONC but are targeted at those activities that we understand firms engage in as part of their legal practice. Wherever possible the proposals apply existing Principles and Outcomes from the SRA handbook. This provides an intuitive and proportionate regime for those whose business is primarily involved in the provision of legal services.
25. In response to our previous consultation it was suggested that some firms, and particularly smaller firms/sole practitioners, may be forced out of the market due to the costs of dual regulation. We consider that our proposed approach minimises this risk by permitting firms to continue to undertake, under SRA regulation, consumer credit activities that naturally form part of their legal practice and to continue to provide benefits to consumers, such as deferred payment arrangements, under a streamlined scheme. We consider that the proposed prohibitions, together with minimal additional requirements supported by illustrative guidance, provide a proportionate and targeted approach to regulation whilst providing appropriate consumer protection. We will continue to work with the Sole Practitioners Group and other representative groups to seek views and opinions.

⁵ <http://www.fca.org.uk/firms/being-regulated/unfair-contracts/library>

26. The biggest impact is likely to stem from the prohibitions and restrictions listed in paragraphs 10 and 11. This is particularly so as SRA-authorized firms authorized by the FCA to carry on consumer credit activities will no longer be able to benefit from the Part 20 regime in relation to any other FSMA regulated activities (for example, insurance mediation activities). This is because a firm cannot be both authorized by the FCA and carry on exempt regulated activities under Part 20 at the same time.
27. However, it is worth noting that if we permitted firms to carry out the activities listed in paragraphs 10 and 11, we would need to ensure that appropriate amendments to our Handbook were made in order to provide equivalent regulatory requirements to those set out in CONC. This could only be achieved by incorporating CONC, or substantial parts of it, into the SRA's rules. Therefore those very detailed and prescriptive requirements would nonetheless apply to firms, and this would go against the SRA's direction of travel, towards a more flexible Handbook.
28. If following this consultation we decide to implement the regulatory scheme going forward we will look to collect better data to review the operation of the scheme and its impacts. This will result in a higher reporting burden on firms. Improved data collection will help better assess the impact of our regulatory arrangements going forward.

Consultation questions

Question 6 - Do you have any views about our assessment of the impact of these changes and, are there any impacts, available data or evidence that we should consider in developing our impact assessment?

Question 7 - Can you provide any specific examples of benefits or risks linked to our proposed approach and/or particular aspects of our proposed arrangements?

Next steps and implementation timetable

29. This formal consultation is open for six weeks, closing on: Friday 7 August 2015.
30. As previously mentioned, we have already engaged informally with a number of firms and other key stakeholders in developing these proposals. For example, we sought early feedback from the small firms virtual reference group, we have invited views at Law Society events and we have spoken to firms that we know undertake consumer credit work. We have also been guided by responses to the October 2014 consultation.
31. In line with our published consultation policy, we will pro-actively target and facilitate discussion with key stakeholders, including firms likely to be affected by these proposals. For example, we will hold an open webinar where participants can raise questions and express views.
32. We aim, subject to FCA and LSB approval, to publish our final regulatory arrangements in November 2015, but these will not take effect until April 2016. This will allow for smooth transition, including providing opportunity to firms who wish to get approval from the FCA to do so, for example those currently undertaking activities that we propose to prohibit from our regime.

The FCA has agreed this extension to the transitional period. During this transitional period, all SRA- authorised firms undertaking consumer credit activities under the Part 20 exemption must comply with the SRA's transitional provisions. These provisions require such firms to comply with the legislation and OFT guidance in place immediately before 1 April 2014.

33. Our forward timetable is set out below

Formal consultation on our proposals	26 June to 7 August 2015
SRA Consumer Credit webinar	16 July 2015
Rule changes to be made by the SRA Board	9 September 2015
Changes to the SRA's regulatory arrangements approved by the FCA and the LSB	October 2015
Publication of rules on SRA website	1 November 2015
End of transitional arrangements	31 March 2016
Rules including prohibitions come into effect	1 April 2016

Consultation questions

1. Do you agree that it is appropriate for the consumer credit activities set out above to be 'prohibited' from regulation by the SRA under Part 20 FSMA?
2. What is the likely impact of the prohibitions and restrictions for firms and consumers?
3. Should any of the prohibited activities be allowed, or the prohibitions/restrictions be modified?
4. If so, do you believe that any additional consumer protections should be put in place to address any specific risks that these activities present?
5. Do you have any comments on the requirements set out in our proposed amendments to the SRA Conduct of Business Rules?
6. Do you have any views about our assessment of the impact of these changes and, are there any impacts, available data or evidence that we should consider in developing our impact assessment?
7. Can you provide any specific examples of benefits or risks linked to our proposed approach and/or particular aspects our proposed arrangements?

To help respondents formulate their response to the questions set out above, a set of questions and answers have been produced and are set out in **Annex 2**.

How to respond to this consultation

Online

Use our [online consultation questionnaire](#) to compose and submit your response. (You can save a partial response online and complete it later.)

Email

Please send your response to consultation@sra.org.uk You can download and attach a Consultation questionnaire.

Please ensure that

- you add the title "SRA – Consumer Credit 2015" in the subject field,
- you identify yourself and state on whose behalf you are responding (unless you are responding anonymously),
- you attach a completed About You form,
- you state clearly if you wish us to treat any part or aspect of your response as confidential.

If it is not possible to email your response, hard-copy responses may be sent instead to:

Solicitors Regulation Authority
Regulation and Education - Consumer Credit 2015
The Cube
199 Wharfside Street,
Birmingham,
B1 1RN

Deadline

Please submit your response by 7 August 2015.

Confidentiality

A list of respondents and their responses may be published by the SRA after the closing date. Please express clearly if you do not wish your name and/or response to be published. Though we may not publish all individual responses, it is SRA policy to comply with all Freedom of Information requests.