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Dear Chief Executive Officer

FCA Supervisory strategy for the Debt Advice portfolio

We wrote to you in July 2020 setting out our view of the key risks of harm that debt advice firms pose to their customers and the markets in which they operate. We also set out our 2-year strategy for mitigating those risks. While we have seen improvements in some areas, there are risks of harm that remain and new risks that firms within the portfolio need to address.

We are writing to:

- update you on the key risks we have identified that debt advice firms pose to their customers and the markets in which they operate;
- outline our expectations of debt advice firms, including how firms should be mitigating these key risks; and
- set out our supervisory strategy and programme of work to ensure that firms meet our expectations, and harms are being appropriately remedied.

You should consider the extent to which your firm presents such risks, and ensure strategies are put in place to mitigate them. We expect firms to be able to demonstrate the steps being taken to address the risks we cover in this letter.

It is particularly important that firms mitigate these risks given their important role assisting consumers facing repayment and debt difficulties, including those impacted by the rising cost of living.

The Rising Cost of Living

Many consumers will feel the impact in their personal finances, but we are particularly concerned that consumers least able to bear the rises will be hardest hit. While the headline average inflation rate is at 9% and rising, the Institute of Fiscal Studies estimates that the poorest households may face average inflation rates as high as 14%. This is in the context of a quarter (27%) of the population having low financial resilience, a figure likely to increase over the coming months.

At the same time, we expect to see higher demand for credit, although rising interest rates, and lower disposable income, may make borrowing less affordable, or unavailable, for some. Firms will also see a wider group of consumers in financial difficulty, who will find it harder to pay their debts. Some of these consumers will be in vulnerable circumstances or may be experiencing financial difficulty for the first time. Firms need to remain alert to the changing situation of their customers and target their efforts in response.

As highlighted below, it is important that the quality of debt advice meets the standards set out in our rules and guidance, and that appropriate resource and attention is given to the treatment of customers in vulnerable circumstances.

We expect firms in the portfolio to support consumers struggling with personal debt or showing signs of financial difficulty during this period, helping them obtain appropriate debt advice and debt solutions. Our Tailored Support Guidance and our recently published Dear CEO letter, reiterate the standards we expect lenders to meet in supporting borrowers showing signs of financial difficulty or struggling with debt. This letter sets out our expectation of firms to make consumers aware of and help them to access money guidance or free debt advice. As a result of this, firms in this portfolio should be prepared for the likelihood of increasing volumes of consumers seeking debt advice, including those who may be in vulnerable circumstances.

The cost-of-living crisis may also affect firms' ability to respond to, recover, and learn from, operational disruptions. You should ensure you have robust and effective governance arrangements to identify, manage, monitor, and report the risks you may be exposed to, such as an increase in the need for advice, sudden increases in the volume of consumer contacts and data protection and cyber resilience risks. You should consider different scenarios that may test your operations, to ensure that your internal processes and control mechanisms are adequate. As a regulator, we will continue to work with you and the financial services sector to monitor, manage and mitigate any harms to consumers due to the rising cost of living.

FCA Business Plan and Strategy

In Our Strategy 2022 to 2025, we set out our vision and ambitions for the next three years. We also set out the consistent high-level outcomes we expect from financial services and the key strategic areas we will be focusing on. We have grouped our commitments into three areas:

- **Reducing and preventing serious harm** – our focus is on protecting consumers from the harm that authorised firms can cause, including tackling fraud and poor treatment.
- **Setting and testing higher standards** – we're focusing on the impact that authorised firms' actions have on consumers and markets. We expect all firms we regulate to adopt the same high standards and have an open and cooperative approach.
- **Promoting competition and positive change** – we want to use competition as a force for better consumer and market outcomes. We will support UK growth and innovation that serves our society, underpinned by widely recognised and respected high standards.

Our Business Plan explains our programme of work for this year to achieve this three-year strategy. It outlines the key work we will undertake to deliver these outcomes, and how we will measure progress.

We published this Business Plan at a time where the external environment is changing rapidly. The longer-term impact of Covid continues to be uncertain. Low levels of financial resilience and rising costs mean many people are at risk of serious financial problems. And this is happening against a backdrop of rising inflation and interest rates, and major geopolitical uncertainty. The impact of these factors will be felt by consumers and firms over the coming year and beyond.

By focusing more on end outcomes, and working across sectors and markets, we are better able to respond to new issues and macroeconomic challenges. Our new, more adaptive approach to allocating resources and monitoring our performance will make us more agile and help us respond more quickly to market needs.

The Business Plan details the work we will carry out this year under each of the 13 commitments from the Strategy where we will focus our work.

Our view of the key drivers of harm

As noted above, financial pressure is starting to build with increasing living costs potentially resulting in a net reduction in consumers' disposable income. As such, it is paramount that firms take action in accordance with our rules and guidance to mitigate harm to consumers.

Debt advice firms have offered an important service to those who find themselves in financially vulnerable positions. However, we are not satisfied that all firms have adequately responded to the key drivers of harm set out in our previous Portfolio Letter. Since that letter, we have updated our view of the key drivers of harm by examining a range of data and engaging with firms and consumers.

Our updated view of the key drivers of harm encompasses harms we have highlighted previously, as well as emerging harms. Firms should be aware of the drivers of harm that surround their business and mitigate them wherever possible.

Our updated assessment of key consumer harms:

- Consumers are unable to access debt advice when they need it, due to insufficient capacity in the sector;
- Poor quality advice being offered to customers, which doesn't adequately support recovery from financial hardship;
- Customers in vulnerable circumstances do not achieve good outcomes, due to firms failing to correctly identify these customers;
- Poor consumer outcomes driven by firms that fall outside of the FCA's perimeter; and
- Consumers do not receive redress owed to them due to firms operating with insufficient financial resources.

Our expectations and areas of focus

Following our analysis of firms in the Debt Advice portfolio, our strategy to reduce harm will prioritise supervisory work in the following areas:

1. **Insufficient capacity**

The impact of coronavirus has amplified potential capacity concerns, highlighting the need to do more to meet the demand for debt advice. The financial hardship arising from the pandemic has been felt by firms and consumers alike, with 16% of UK adults finding themselves over-indebted (October 2020), while firms have faced operational and business model challenges which have had the potential to affect capacity. The expected increase in demand for debt advice resulting from the pandemic has yet to materialise significantly, noting many consumers have received support from government schemes and their lenders in a range of forms. However, it is important the sector is prepared for the implications on consumers arising from the rising living costs forecast, as this may require increased capacity for the sector as more consumers find themselves in arrears.

We are committed to encouraging new, innovative solutions which will improve the sector's ability to meet demand. Our Innovation Department offers a wide selection of tools which have been designed to help firms pilot innovative business models. We encourage firms to engage with the services that we offer, including the following:

- Innovation Pathways, encompasses and builds on two previous Innovation Services (Direct Support and Advice Unit). We recognise that in an increasingly digitised market that there are many different pathways for businesses to operate in financial services. Innovation Pathways provides tailored regulatory guidance to innovative businesses, including established firms, start-ups and technology firms that want to deliver positive innovations and consumer outcomes in the financial services market, including firms serving gaps in the advice market. It helps innovative firms understand our regulatory regime, explaining parts of the regulatory framework that may be impeding market development, as well as helping firms with the authorisation process.

- The Regulatory Sandbox allows businesses to test innovative propositions in the live market with real consumers, alongside regulatory oversight. It allows firms to see how new proposals work in the market in a controlled environment, gives an understanding of the benefits and risks that may arise, as well as helping firms to identify appropriate consumer protection safeguards to build into new products and services. Regulatory Sandbox tests can help firms to deliver innovative propositions at a reduced time to market at potentially lower cost.

Increased emphasis and funding for digital advice has also been promoted by the Money and Pensions Service (MaPS) to address the issue of capacity in their departmental review. Firms looking to enter the automated advice space, to service the need for digital advice, could benefit from these services.

We encourage firms to proactively forecast demand and plan accordingly. Regular reviews of demand in the context of a firm's capacity can help firms collectively improve access to debt advice for consumers on a more consistent basis, and drive sustainable debt advice in the sector.

Firms seeking to enter the debt advice market or wishing to modify their existing permissions can find information on our website about applying for authorisation. When firms apply they must be able to demonstrate that they are ready, willing and organised.

2. Quality of advice

Good quality advice is fundamental to the integrity and functionality of the sector. As such, firms should ensure that:

- all advice given has regard to the best interest of customers, is appropriate to the individual circumstances of the customer and is based on a sufficiently full assessment of the financial circumstances of the customer;
- customers receive sufficient information about the available options identified as suitable for the customers' needs;
- it explains the reasons why the firm considers the available options suitable and other options unsuitable.

Where firms are administering debt management plans, they should regularly monitor and review the financial position and circumstances of the customer. Harm may happen when advisers recommend suitable debt solutions but do not adequately explain what these solutions entail, and the impact they may have on the customer.

Quality of advice can also be compromised when firms offer non-compliant advice that is biased towards debt solutions that generate referral fees for the firm. Our supervisory work identified concerns that some firms in the portfolio appear to have manipulated customers' income and expenditure to meet the criteria for revenue-generating insolvency solutions; used persuasive language to promote these products to customers without fully explaining the risks involved and provided advice that did not accurately reflect their conversations with customers or information that customers had given.

Customers should be presented with available options identified as suitable for the customers' needs, whilst also being provided with sufficient information on why these solutions are suitable, in a clear, and not misleading, manner. Moreover, the standard of advice must be regularly monitored within firms. Whilst we will continue to act where we see harm, firms are responsible for compliance and should have effective processes to identify, manage, monitor and report existing or future risks related to the quality of advice being provided. Further to this, we are reviewing our approach to our Debt Advice rules in the Consumer Credit Sourcebook and will provide further update in due course.

3. Customers in vulnerable circumstances

In our most recent Debt Management thematic review we highlighted that customers in vulnerable circumstances are not always identified and that improvements need to be made in this area. The coronavirus pandemic has exacerbated the number of people facing difficult circumstances, personally and financially.

Taking into account the current economic climate, it is imperative that firms embed the fair treatment of customers in vulnerable circumstances into their business models and firm culture, in an effort to reduce harm. In February 2021, we released guidance for firms on the fair treatment of vulnerable customers, detailing how firms can implement policies and procedures that protect consumers across the financial services industry.

Customers in default or arrears difficulties must be treated with forbearance and due consideration (including where firms administer debt management plans). Appropriate support should be offered when required, to ensure customers in vulnerable circumstances achieve outcomes as good as those for other customers.

4. Problems outside of our regulatory remit

There are a number of businesses that are not subject to FCA regulation but are currently involved in recommending and/or arranging debt solutions for consumers. These include businesses which forward the details of potential customers onto debt advice firms and Insolvency Practitioners (IP), in exchange for a fee. In our recently published Perimeter Report, we highlighted concerns over the practices of unregulated lead generators. Often these firms are able to advertise online. In some instances this advertising employs misleading practices, such as:

- potentially imitation of specific debt charities or government agencies;
- misleading descriptions of IVAs;
- misleading claims about the proportion of debts resolved in an IVA;
- misleading illustrative examples;
- potentially false testimonials;
- unauthorised debt counselling or misleading statements over who is giving advice;
- misleading use of the term 'debt free'; and
- misleading use of regulator logos/ regulatory status/ MaPS referrals.

We remind firms that receive leads from lead generators of their obligations under chapter 8.9 of the Consumer Credit Sourcebook ('CONC') in the FCA Handbook. This includes ensuring that lead generators do not provide debt counselling unless they are authorised to do so. Particular care is needed in situations where customers are referred to a provider of debt advice or debt solutions that only offers one debt solution, as this may, in some cases, constitute debt counselling. There is more detailed guidance on the regulated activity and practices that will and won't amount to debt counselling in Chapter 17 of the Perimeter Guidance ('PERG') in the FCA Handbook.

Under CONC 8.9, firms that receive leads from lead generators also have responsibilities to make sure the lead generator does not falsely claim or imply that it is a charitable, not for profit or government or local government organisation and makes clear its role and any financial interest it may have in passing on a sales lead. Firms that are themselves FCA authorised must ensure that their financial promotions comply with CONC 3, which includes ensuring that the communication is clear, fair and not misleading, states the services the firm offers and any relationship with a business associate which is relevant to the services offered. Their financial promotions should also include (if relevant) a statement that the firm's service is profit-seeking and contains a reference to impartial information and sources of assistance from not-for-profit debt advice bodies, and states the most important actual or potential advantages, disadvantages and risk of any options mentioned in detail. Under CONC 8.2.4, an authorised firm must also prominently make customers aware that free debt counselling, debt adjusting and providing of credit information services is available to customers and that the customer can find out more by contacting MoneyHelper. Concerns about the promotions of an FCA authorised firm can be referred to us. There is more information about this on our website here. FCA authorised firms can also make us aware of concerns about unauthorised business or the financial promotions of authorised firms by contacting our Supervision Hub, either by calling +44 (0)20 7066 1000 or emailing firm.queries@fca.org.uk. If a firm is not FCA authorised, it may be possible to raise concerns about its advertising practices with the Advertising Standards Authority.

IPs are overseen by Recognised Professional Bodies (RPBs), who are regulated by the Insolvency Service (IS). We have been working closely with RPBs and the IS on issues of mutual concern, such as lead generators, and to share intelligence to identify cross-regulatory risks and harms. We note recent updates to documents, such as the IS Code of Ethics and IVA Protocol, regarding IPs use of lead generators.

5. **Insufficient prudential resources**

Strain has been placed on the UK economy as a result of the pandemic, the rising cost of living, and stalling supply chains due to the Russia-Ukraine conflict. These economic hardships have further emphasised the need for firms to remain financially resilient to keep providing services to those who need them. We expect firms to be managing their financial resources prudently, with clear planning for the future.

Previously, we have seen firms mismanage their finances, rendering them unable to pay their obligations as they fall due, ultimately leading them to exit the market in a disorderly fashion. Consequently, customers may be left without essential debt advice and/or oversight of debt management plans and with limited scope to receive redress.

Our policy statement on wind down planning should be used to inform firms on how to assess whether they have sufficient resources to wind down in an orderly manner, with minimal adverse impact on customers and the wider markets. Firms operating in the debt advice sector are also reminded of their requirements, as set out in CONC 10.2, to ensure that the firm is always able to meet its liabilities as they fall due. We use several data sources to monitor compliance with these rules and will engage with firms where we consider you may have breached your regulatory obligations. Further guidance on adequate financial resources can be found in our final guidance on assessing adequate financial resources.

Data-led regulation

As we transition towards becoming a more data-led regulator (see the FCA data strategy), we remind firms we will increase our focus on data, not limited to regulatory returns. However, we remind firms of their obligations to report regulatory returns accurately, in a timely manner, as well as ensure that their standing data is up to date. Our move towards automated data collection should enable firms to meet their reporting requirements and submit returns more easily.

Data enables us to make better, more informed, regulatory decisions that benefit consumers and firms alike. We are committed to using the data that we receive from firms to test whether firms' products and services deliver good outcomes for consumers, and to simulate policy outcomes before publishing rules. Equally, we want to share our data with firms so they can use it to test new products and business models themselves.

Principle 11 includes a requirement for firms to deal with its regulators in an open and co-operative way, this encompasses co-operating wherever possible with respect to ad-hoc information requests, such as surveys. Further to this, we expect all firms in this portfolio to be aware of the requirements and guidance in SUP 15, and to submit notifications as required. This should be when an issue or event is identified, and firms should not wait until resolution to notify us. Failure to notify us of matters set out in SUP 15.3 could have serious regulatory impact as it may impact our ability to effectively supervise the firm, and raise questions on whether the firm is meeting the Effective Supervision Threshold Condition (COND 2.3 Effective Supervision).

Raising Standards

We are proposing to introduce a new 'Consumer Duty', that would set a higher standard of care that firms should provide to consumers in retail financial markets. The Consumer Duty would require firms to act to deliver good outcomes for customers (including those in vulnerable circumstances). This reflects the positive and proactive expectation we have of firm conduct, and our desire for firms to think more about consumer outcomes and place consumers' interests at the heart of their activities.

Amongst other things, it would require firms to focus on supporting their customer (including those in vulnerable circumstances) to make good financial decisions and avoiding foreseeable harm and checking whether their customers are getting good outcomes. This includes providing information consumers can understand, products and services that are fit for purpose and offer fair value and helpful customer service. A firm would, for example, not be acting in accordance with the Consumer Duty where it seeks to exploit customers' lack of knowledge, understanding or behavioural biases.

We have seen examples of exploitation and misleading information. These practices are counterproductive and detrimental to a healthy financial services system and are the types of poor practices the Consumer Duty seeks to prevent.

Our second consultation with specific rules and guidance on the proposed new Consumer Duty is now closed and pending the outcome of this consultation, we expect any new rules and guidance to be published by the end of July 2022.

Environmental, Social and Governance

Financial services and markets also have a central role in the transition to a low carbon economy and a more sustainable future. The Government has committed to achieving a net zero economy by 2050. We will support the financial sector in driving positive change, including the transition to net zero. We have developed a refreshed ESG strategy setting out our target outcomes and the actions we expect to take to deliver these in the coming months, spanning over all of our work on sustainability and climate change.

Our work on diversity and inclusion continues, working towards fostering a culture that embraces diversity and inclusion, supports diversity of thought, promotes innovation and unlocks talent. Our joint discussion paper with the PRA and the Bank of England dives deeper into our thoughts on accelerating meaningful change in this area and how we can nurture a more inclusive industry. Firms that lack diversity could be more prone to groupthinking at decision-making levels and may not be able to understand the needs of their customer base, ultimately leading to consumer and market harm. We shall be consulting on rules and guidance to promote diversity and inclusion in the financial services sector later this year.

What we expect from you

All authorised firms in the financial services industry are expected to conduct their activities in a way that treats consumers fairly, provides clear communications to consumers, resolves disputes and complaints fairly, and that complies with FCA Principles and FCA Handbook rules and guidance. We expect you to reflect on the issues highlighted in this letter to challenge how your firm operates and put in place the actions we have requested.

Contact

Please contact us on 0300 500 0597. This is the primary point of contact for your firm's day-to-day interactions with the FCA, and further details of how we can be reached are on our website. You can also email us at firm.queries@fca.org.uk.

However, there may be times when your firm faces urgent issues of strategic importance. If this happens, please contact the Head of Department, Caroline Gardner on 020 7066 8186 or Caroline.Gardner@fca.org.uk, or please contact one of my Managers, Sunil Thakar, on 020 7066 5996 or at Sunil.Thakar@fca.org.uk.

Yours sincerely,

David Raw
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