CREDIT STRATEGY

Risk | Policy | Conduct

January 2017

ALL OUT OF PROPORTION?

How the cost of compliance surged beyond its purpose

LEFT TO THEIR OWN VICES
Has the payday lending price cap pushed borrowers towards loan sharks?

THE CS INTERVIEW
Rahul Pakrashi
Chief risk officer
Funding Circle

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Myths of the near future

Marcel Le Gouais
Editor

In our Watchman series in the magazine we've tried to tackle some myths in corporate communications and correct misconceptions about business-to-business publishing.

Our very own Fred Crawley has punctured misleading usage of the word 'leading' in marketing copy – a common occurence when companies describe themselves. He has also courteously explained the pitfalls of crass PR and now, as we prepare to launch next year's Credit Awards, he has issued a handy guide to writing awards entries (see p15).

Part of the purpose behind the Watchman articles is the need to explain our modus operandi. There are tons of reasons why we publish certain articles and not others, but the rationale involved in this decision-making process isn't always obvious to the outside world. We make these decisions based on a number of factors; take, for example, a supplier's new product launch.

We have to ask ourselves: Who is actually bothered about this? Is it new or a thinly veiled add-on? Is it genuinely different to what's out there?

We also try to assess whether a new product or service will make a tangible, measureable impact. We ask: Who's going to use it? Are those users important in the readership? Are there enough of them in the readership to make this worthwhile?

"The thought of being asked 'to do a nice write up for us', by a company asking nicely for a generous gesture, sends a cold shiver up the spine of any journalist"

What we are not in the business of doing, is offering favours to companies by writing up product launches as free marketing copy.

The thought of being asked "to do a nice write up for us", by a company asking nicely for a generous gesture, sends a cold shiver up the spine of any journalist with a sense of independence.

Every article is published – no matter where it comes from and whether it comes from an advertiser or not – based on an assessment of its worth, its merits and the likelihood of enough readers being interested. And this brings me to another misconception to correct.

When we publish any article about an individual business, this does not constitute an act of support for that company. By our nature as a business-to-business publisher, we write articles about individual firms every day. When we do so we are not acting in support of, or acting against, any particular firm. We're just deciding the most important content to bring to you.

What we try to do is provide content in various forms and channels that matters in some way to you.

One of those channels, as you may have seen, is our newly launched website. Built from scratch during the past eight months, its launch marks the beginning of a more responsive, interactive platform for readers to be involved in. There's also now a much wider breadth of content on creditstrategy.co.uk. A vital element in making this website a valuable community for all of you is your involvement, so please share your views by posting comments on news articles, opinions and analysis.

You are all a collective judging panel that decides whether what I have described above, has been executed successfully. CS

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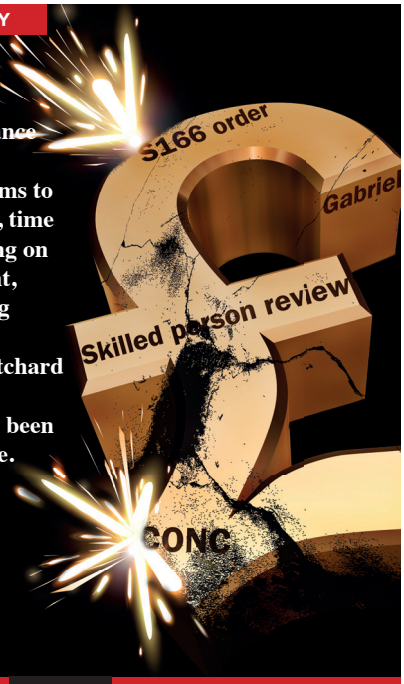

£2m

The total compliance costs that debt purchaser Motormile Finance has had to absorb since 2013

Source:
Motormile Finance

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Printed by: Stephens and George (S&G)

Credit Strategy is a subscription news magazine. Annual rates: (UK) £195 for one year (£351 for two years), (Overseas) £249 for one year (£448 for two years).

It is published monthly by Shard Financial Media.

ISSN 2399-1372.

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FINANCIAL MEDIA

As payday lending contracts, what next for high-cost credit?

The volume of payday lending has plummeted more than 40 percent in the past three years, prompting questions over the future for this market's lenders and customers.

A steep decline in volumes was discovered when the Consumer Finance Association (CFA), a trade body for short-term lenders, investigated how this market has changed since the regulator imposed the payday loan price cap in 2015.

According to the CFA's research the costs of borrowing has fallen since this transition and lenders have been using "tighter" affordability checks.

It also found that of the 1,200 consumers surveyed, those taking out loans in 2015 were on average coming from higher income brackets than in 2013.

The research was conducted in partnership with the Social Market Foundation (SMF), a research and events firm, with input from two YouGov surveys.

Inevitably, the report lit the fuse on a debate around whether any consumers of these products may have been forced to turn to loan sharks, since the price cap was introduced and the market contracted after regulatory intervention.

Nigel Keohane, research director of the SMF, said: "Policy makers should be vigilant about the potential risks to those who are excluded from the market."

The CFA's research emerged in the same week that the Financial Conduct Authority (FCA) said it will conduct a study to examine the same point – whether there's any evidence that the price cap inadvertently pushed people towards illegal lenders.

The FCA said its review of the cap, in the first half of 2017, will determine if it needs changing and the findings will be published next summer.

Crucially, the regulator will also seek evidence and feedback on all types of high-cost credit to inform its work on the market. This will include a focus on a range of products from catalogue credit, guarantor and logbook loans to credit cards and motor finance.

There will also be a greater focus on overdrafts since the Competition and Markets Authority (CMA) identified a number of issues with the product.

Big three purchasers spend close to £500m on portfolios

Three of the UK's largest debt buyers have racked up a spending total of £488m on portfolios for the first nine months of 2016.

A round of results statements from the debt purchasers, which show financials for the first three quarters of the year, show how much they've spent on portfolios up until September 30. All the figures here are for their entire groups.

Cabot Credit Management spent £135m on portfolios during the nine months until September 30.

It also recorded a 24 percent year-on-year increase in its adjusted EBITDA. Its results update shows this increased to £180m during the same period, compared with £146m for the first nine months of 2015. Ken Stannard, chief executive of Cabot, said the increase was driven by 20 percent growth in the company's debt purchase collections and a 34 percent rise in its servicing revenue.

As for Cabot's competitors, at the time of going to press Arrow Global announced a new chief executive and its entry to the Italian market. Its spending on portfolios from January to September reached £154.6m.

Lastly, GFKL Lowell Group said it expects its total spend on portfolios to reach £250m by the end of the year. During the nine months to September 30 it spent £198m on portfolios.

Vital Statistics

75

The number of years' experience between the co-founders of new lender Nava Finance. The unsecured lender hopes to launch its online lending platform early next year. Its services will be aimed at the near-prime consumer credit market.

THE VENT
Choice cuts from social media

Will tighter lending rules push consumers to use loan sharks?

A Twitter debate kicked off this month after the Consumer Finance Association (CFA) published statistics on the decline of the payday lending market (see main story above). This debate centred on whether there's a correlation between the price cap on payday loans and use of illegal lenders.
For context on this debate read our article here: http://bit.ly/2gV5OIC

Appetite for consumption: Credit card debt hits £66bn

Outstanding credit card debt in the UK increased by £0.6bn during October to reach a total of £66.2bn, according to the Bank of England.

The money and credit statistics report showed that outstanding credit card debt in the UK has hit a record high, with also the highest annualised increase since February 2006.

Ahead of Christmas the figure sparked warnings over spiralling debt levels. Peter Tutton, head of policy at StepChange Debt Charity, said: "Consumer credit is rising at its fastest rate for over a decade and the amount owed on credit cards continues to hit record levels."

The report also revealed that consumer credit debt is at its highest level since December 2008, with the highest annualised increase since October 2005.

As a total, consumer credit increased by £1.6bn during October to a total of £190.1bn.

Tutton added: "It is vital that lenders use thorough affordability checks to ensure that people can repay credit in a reasonable time and without hardship. When people find themselves in persistent debt, lenders need to identify them early and offer the vital assistance they need."

A WORD TO THE WISE

"The weakest bank in Europe just got weaker"

Simon Jack

BBC News's business editor on Europe's oldest bank Monte dei Paschi, after Italian Prime Minister Matteo Renzi stood down

"If you think you're going to get an FCA section 166 order, you can influence how it's structured"

Emily Benson

Partner at TLT and an expert on skilled person reviews, Emily Benson explains how to prepare for FCA intervention, at our CDSP Conference in Manchester

"Banks will relax credit criteria because they have shareholder targets to hit"

Dicky Davies

Also speaking at our CDSP Conference, GFKL Lowell Group's business development director shares his view on lending practices next year

"Up to 15 million of the current jobs in Britain could be automated over time"

Mark Carney

The Bank of England governor on how technology could wipe out swathes of jobs

"It's about who is the best at channel management… banks will become a logo"

Daniel Melo

Senior director, business development, at FICO, opines on the future of banking at our CDSP Conference

"Can understand @CFA_PressOffice surveying customers but think No's using illegal loans greater amongst non-customers"

@Andrew_F_Smith
Andrew Smith
ClearDebt

"@Andrew_F_Smith they are of course surveying the wrong population. They should be asking people who were refused a loan what they did"

@DebtCamel
Sara Williams
Debt Camel

"@DebtCamel Not inferring correlation between PDL cap and loan shark use. Nor are @TheFCA - but they want to find out more"

@Andrew_F_Smith
Andrew Smith
ClearDebt

"The advice sector needs to believe that tighter lending rules won't drive folk to loan sharks"

@nwpearson
Nick Pearson
The Debt Counsellors

More compliance costs and M&A: What the future holds for collections

Big data, panel reductions, compliance and more M&A across the industry all emerged as the key themes at this year's CDSP Conference. AMBER-AINSLEY PRITCHARD reports

Compliance has been a more than popular topic across the consumer credit industry; if popular is the right word.

In a vote during the morning session of Credit Strategy's Collections, Debt Sale & Purchase (CDSP) Conference last month delegates were asked whether they thought compliance costs would rise, fall or stay the same next year.

Using the online poll app sli.do to give their answers, more than half the delegates stated that compliance costs for their businesses would increase next year.

Another 33 percent voted to say they thought these costs, which are already at unprecedented levels (see cover feature, p20), would stay roughly the same.

A range of delegates, including chief executives of debt buyers and collection agencies, partners at debt recovery law firms and directors within banks, travelled to the Midland Hotel in Manchester on November 24 for the conference.

As well as compliance costs, the transition among collections firms' models to business process outsourcing (BPO), along with further cuts to debt collection agency (DCA) panels by creditors, was discussed by the speakers.

Those speakers included senior professionals from Barclays, Clydesdale and Yorkshire Banking Group (CYBG), BMW Financial Services and the Student Loans Company.

L-R: Stuart Sykes, Myjar; Nick Winterbottom, Clydesdale and Yorkshire Banking Group (CYBG); Tony D'Agostino, Hito; Daniel Melo, FICO

Chaired by Leigh Berkley, president of the Credit Services Association (CSA), the conference opened with a plenary session before splitting into two streams – UK Collections and European non-performing loans (NPL) and Debt Sale.

Shortly after a presentation from headline sponsor Hito, Berkley provided a rundown on major issues during the past few months and emerging activity - such as the accelerated movement of government debt to the private sector.

He commented on how the government was "only just waking up" to the meaning of treating customers fairly (TCF). Berkley also mentioned the placement of more debt for collection with the private sector via the Debt Market Integrator – the programme now being run out of the Cabinet Office.

As well as oversight costs related to authorisation by the Financial Conduct Authority (FCA), the looming challenge of the General Data Protection Regulation (GDPR), which has to be implemented by May 2018, was also prevalent.

When delegates attending the conference were asked whether or not they had already begun preparing for

its implementation, the majority raised a hand to confirm they had.

Berkley also reminded delegates that the industry is still awaiting an outcome of an Ofcom consultation on silent and abandoned calls, and an update on the new pre-action protocol for debt claims.

Another key theme that emerged was the use of big data by both the private and public sectors in collections, as well as customer interaction with both sectors. Berkley suggested that when it comes to debt owed by an individual to multiple government departments, a slightly nuanced I&E check and payment process could be carried out.

This could work, he suggested, by an individual making a payment, following the I&E check, into a government portal. This amount could then be used to pay off different debts to government departments based on proportions owed.

Integrating credit risk and collections

In the morning, creditors such as short-term lender MyJar, along with Clydesdale and Yorkshire Banking Group (CYBG) and headline sponsor Hito, discussed managing customer data between risk and collections teams.

When asked by the chair about effective ways to integrate the two functions, Stuart Sykes, group head of customer operations and debt recovery at MyJar, said: "It's about how you use big data. You need to understand your customer's journey from day one, and that includes specific details such as the IP address they're using.

"Propensity to pay scorecards are important and we are seeing a lot of benefit in using those. It helps us to target the right group of customers, rather than those who could turn out to be guilty of first party fraud.

Nick Winterbottom
Head of collections strategy and change, CYBG

"There is a trade-off; to what extent is the bank prepared to invest in infrastructure for collections relative to customer acquisition? It tends to focus on the latter"

"Once you can understand what you can do at the front end, you can improve what you do at the back-end. MyJar staff may well be trained better in propensity than staff at high street banks because the firm is smaller."

Nick Winterbottom, head of collections strategy and change at CYBG, explained that the focus within the bank is always going to be geared more towards the capability to acquire new customers, rather than collections.

"The biggest challenge is legacy systems and therefore joining up the customer experience, as well as understanding the journey that the customer starts with an interaction, and tracking that journey through whichever channel is the preference of that customer.

"In collections and recoveries, we are trying to catch up. The system we use is straining and it needs replacing.

"But there is a trade-off; to what extent is the bank prepared to invest in infrastructure for collections relative to customer acquisition? It tends to focus on the latter."

First contact

The same panel in the morning session moved onto discuss specific details that help in contacting customers – particularly nuanced details on letters – and how behavioural science had played a pivotal role in this.

Tony D'Agostino, sales director at Hito, the headline sponsor of the CDSP Conference, remarked that if companies can't engage with people in the preferred way that those customers want to be engaged with, "they will not engage with you at all."

He added that debt management firms face a particular challenge in being able to "build relationships with somebody else's customers."

Moving to specific contact techniques, Berkley pointed out that a behavioural science team at the Cabinet Office had established that information placed in the middle of a letter could draw the attention of customers receiving it.

He added: "You don't have much time to get your message over to customers."

Winterbottom said CYBG had also tracked parts of letters that are effective places in which to put important information. CS

Notes on the vulnerable customer journey

Harvesting data to improve the customer journey, particularly for vulnerable customers, was another key topic at this year's CDSP Conference. Some experts think there's more work to do. AMBER-AINSLEY PRITCHARD reports

"2017 is the year of data but we need to be more demanding."

This was the view offered by research fellow Chris Fitch at the CDSP Conference in Manchester last month, at the Midland Hotel, when referring to the use of data by financial services firms to determine the treatment of vulnerable customers.

He added: "If we don't be more demanding we are just going to have more information and descriptions but no solutions."

Fitch, research fellow at the Personal Finance Research Centre, Bristol University, is running a research and intervention project on vulnerability to help firms identify and support their vulnerable customers.

The project has been launched by the Finance and Leasing Association (FLA) and The UK Cards Association to provide a benchmark of where individual firms currently 'sit' in relation to their work on vulnerability.

So far the project has received data from 26 firms but is still open to more companies joining.

At the conference Jennifer Baldwin, head of strategy, collections and recoveries, at Barclays, said: "Vulnerability checks need to be carried out before the collections stage. It needs to happen at the very start when a consumer begins enquiring about a product."

A member of the audience raised a question about the possibility of consumers pretending to be in a vulnerable situation to escape the consequences of their debt.

Polly Mackenzie, director of the money and mental health institute, said it's possible a couple of people could slip through the system.

She added: "But for the most part you are helping people so you've just got to suck it up and get on with it."

Debt sale, collections and M&A

As well as vulnerability and conduct, debt sale prices were also discussed at CDSP.

Prices have reached eye-wateringly high levels this year, and it was put to the panel that the amount of debt sold will drop this year compared to last year. One panel, featuring GFKL Lowell Group, Premium Credit and headline sponsor Hito, was asked whether such high prices will be sustainable this year.

Dicky Davies, business development director at GFKL Lowell Group, said: "We haven't got a choice over where the market is going with pricing. Creditors are used to having prices as they are now, so current pricing is here to stay."

Nick Isaacs, head of credit risk at Premium Credit, said: "The price depends on the quality of the data that's there in your systems as a

creditor. If you've got decent data and decent history, you will get a good price for that portfolio."

The panel was also asked whether the outdated commission model for DCAs will change.

The general theme from discussions was that this ship may have sailed. Panellists mentioned that, if it was going to happen, it would have happened last year when there was mounting pressure for change.

Davies said: "No one yet has changed commission models on a grand scale, through there have been a couple of tests... the move to BPO has to happen."

When the panel was asked about further M&A activity across the market, Davies said: "There has to be more M&A activity across the (UK) market. Investors are looking to Europe for further expansion. That's what our shareholders want."

European NPL and debt sale

Nick Ollard, director of global asset sale services at TDX Group, chaired the European NPL and Debt Sale stream throughout the day.

He was joined by a colleague Inigo Mato, managing director of global asset sale services at TDX Group, who gave an overview of markets on the continent.

Mato explained that the Spanish market is not as mature in secured assets as it is in unsecured.

Discussing Italy, he said: "Prices are rising in Italy's active unsecured market but local servicing is still a major challenge."

Mato referred to some European countries, such as Portugal, Germany and Austria, as "not too sexy" in the debt purchase world and said Greece is the country with the next biggest investment opportunity.

He added: "Big opportunities in developing markets come from investors leaving the country."

He then made a final note on IFRS9 by saying: "It will have a big impact but we don't know how just yet.

"Banks will probably be forced to look at their balance sheets and sell more." CS

The FCA's mission: What it means for your business

On October 26 the Financial Conduct Authority (FCA) published 'Our future Mission', a paper laying out its thinking about how it regulates and decides its priorities. The regulator explains here the relevance for consumer credit firms in its regular Credit Strategy column

As the regulator we have a large and complex remit, and finite resources with which to fulfil it.

The purpose of the mission is to provide a framework around the strategic choices we make, to clarify our thinking over the way we regulate.

We believe every well-functioning market requires the same conditions: engaged consumers, firms and employees that follow clear minimum standards, and well-judged, timely regulation. This applies to consumer credit firms as much as other sectors.

Credit inevitably involves both the borrower and the lender accepting risk. There is always some uncertainty; circumstances can change, a loan that was affordable when it was taken out can later become unaffordable. It is not our role to adopt a 'zero-tolerance' approach to this kind of failure.

Action on high-cost credit

When we took on the regulation of about 50,000 consumer credit firms in April 2014, we used a combination of powers to enact fundamental change in this market. We introduced a cap for payday lending, and we required high standards for those entering the market with all firms meeting our threshold conditions. We took action against poor behaviour.

The vulnerability agenda

People can become vulnerable at any time in their lives, either permanently or temporarily. This can be made worse where the provision of financial services does not adapt to their specific needs.

We believe that we have a specific role to protect vulnerable consumers and that low income can exacerbate any individual vulnerability. This will mean we may need to give some consumer groups, in consumer credit and other markets, higher levels of protection.

> *"We need to think carefully about any unintended consequences of actions we take. These can range from reducing competition, to imposing unnecessary cost"*

Debt management

We aim to advance our objectives using a combination of measures. A good example of this has been our work in debt management. Around 400,000 people are currently using debt management plans.

Our review of debt management firms found examples of high charges and unfair terms and conditions. We are now completing a firm-by-firm assessment of these firms when they apply for authorisation and around 100 of them have left the market.

We also make sure that firms' customers are not abandoned when we refuse authorisation.

In March this year, we wrote to 16,000 customers of one debt management company to tell them we had refused to authorise the firm and explaining where they could get free, impartial advice.

The competition issue

We have to make tough choices when we decide how to meet our objectives, and there is invariably more than one way to achieve an outcome.

We need to think about the type and scale of potential harm, how urgently any harm needs to be stopped, the capabilities of affected users and whether we need to educate or intervene directly.

We know our actions can have a significant impact on consumers and markets, so we also need to think carefully about any unintended consequences of actions we take. These unintended consequences can range from reducing competition, to imposing unnecessary cost, to leaving a group of consumers without a service.

Next steps

The issues discussed in the mission could have implications for our rules. We are determined to be clearer with firms about their expectations of us and the decisions we will take.

To support this, we are also planning to review our handbook to identify changes that would clarify our rules. To help this review we will issue a call for evidence to seek your views about areas of the handbook that would benefit from clarification.

Consultation across the breadth of our stakeholders is also fundamental to the formulation of the FCA's mission. To support this, we are actively seeking the views and feedback of interested parties. This programme of work will include briefings, regional visits, speaking platforms, discussion forums, digital communications and one-to-one engagement.

It is only through active engagement that we can establish a shared understanding of how we put our statutory objectives into practice.

Stakeholders are invited to send us comments on the mission paper by January 26. CS

The Watchman

Ditch the platitudes, present the detail

We need to talk about the Credit Awards and specifically, how best to write winning entries, says FRED CRAWLEY

Fred Crawley
Consulting editor, Credit Strategy

Now, I know what you're thinking. After months of me using this column to sneer at businesses ham-fistedly disguising adverts as news, do I really have the gall to spend this month talking about one of my own firm's events?

Well, yes, I do. But in my defence, this isn't going to be an advertisement. Because you already know about the Credit Awards: Grosvenor House, bow ties, eerily circular pieces of beef – it's something of a landmark fixture.

What you perhaps don't know, however, is how to win at the Credit Awards – and we're not FIFA, so the answer isn't to sponsor them.

Below, I'm going to use the most depressingly ubiquitous format in journalism – the numbered list – to tell you how to write a sure-fire winner of an entry. Obviously, it will also help if your company is the best in its peer group, but that bit's up to you to sort out.

1. Don't describe business as usual
One of the most familiar complaints judges have about awards entries is that they present standard practice, or the meeting of regulatory requirements, as something extraordinary. When listing your company's achievements, make sure they are things that really stand out from what your peers are doing.

2. Less is more
I've done quite a lot to refine the entry process for the 2017 awards, and part of that – you'll be glad to know – has been to reduce the amount nominees have to write. Next year's awards entries will only allow for about 700 words of evidence – about the same as this article. As such, prioritise dense delivery of facts above flowery language, and don't be afraid to resort to bullet points.

3. Numbers speak louder than words
On the subject of brevity, figures are quite often the most efficient and memorable way to make a point. Where you are able to back up your statements with financial results or other metrics, they are going to make much more of an impact on judges.

4. Show, don't tell
Even where numbers aren't available, hard facts are a lot more useful than vague sentiments. An awards entry stating that a business "puts customers at the heart of everything it does" may be making the right noises, but if it doesn't give any practical examples of how it puts customers at the heart of what it does, it has wasted its words.

"Prioritise dense delivery of facts above flowery language, and don't be afraid to resort to bullet points"

5. Don't use the word 'leading'
Please. We've been through this. Seriously speaking though, marketing copy is always best avoided in awards entries. Not only does it tend to be fairly wasteful in terms of word count, but it tends to fall flat with judges who have hundreds of entries to read, and who want to rapidly be able to identify and digest the facts in an entry.

6. It's OK to admit mistakes
In fact, it's encouraged. Some of the most compelling awards entries I've ever read have been businesses talking about how they used to do something badly, and improved it. The honesty and pragmatism involved in telling that sort of story tends to impress judges more than companies which claim to have always been perfect at what they do.

7. Trust us
This one might be a bit of a tall order – we are journalists after all. But it's a serious point – time after time, companies leave out details of their most impressive achievements, because they worry we will siphon the information from their awards entries and publish it in *Credit Strategy*. We will not do this. If you mark information on a nomination as confidential, the only people who ever read it will be the judging panel – and even then, judges with any potential conflict of interest will remove themselves from discussions. CS

A terminal problem with debt management plans

Clarity is required in the interpretation of rules for when debt management plans should be terminated, explains LEIGH BERKLEY

Leigh Berkley
President, Credit Services Association

When the consumer credit source book, CONC, came into being, it transformed the debt collection guidance from the Office of Fair Trading (OFT). It helped our industry to recognise what was and wasn't considered to be best practice. To a very large extent, CONC has been a tremendous success, and helped to clarify issues that might otherwise have caused angst and confusion among those determined to abide by the rules.

But perhaps, inevitably, it has also unwittingly created issues, and one rule is exercising the minds of free and fee-paying debt management companies (DMCs), debt buyers and debt collection agencies, as to how it should be interpreted. The rule in question relates to debt management plans, and specifically whether or not a plan should be cancelled if a customer cannot be contacted within a specified time period to have the plan reviewed.

In terms of the specifics, section 7 of CONC 8.8.1 states that where a firm makes repayments on behalf of a customer, they must "…review, and amend or terminate, where appropriate, the customer's debt management plan at the earlier of each anniversary of entering into the plan or as soon as the firm becomes aware of a material change in the customer's circumstances…".

Open to interpretation

The challenge within our industry is how those key sentences are being interpreted. In the blue corner is the advice sector, who seem to be suggesting that if you can't make contact with a customer, and therefore cannot review his/her existing plan at the appointed anniversary, then that plan should be terminated. Meanwhile, in the red corner, are debt buyers and collection agencies – and the Credit Services Association – which all read those sentences and the sentiment behind them, somewhat differently, and fear the unintended consequences of taking such draconian action.

"The rule in question relates to whether a plan should be cancelled if a customer cannot be contacted within a specified time period to have the plan reviewed"

We know from experience that an individual in a plan, who has been steadily paying down that plan for a number of years, is most likely to ignore correspondence that is likely to herald bad news.

Sadly, for that individual, however, if the DMCs have their way and cancel a plan, the account will be returned and they are likely to receive not one but probably dozens of letters from DCAs, buyers or the original creditor, seeking to make contact. In our opinion this cannot be in the customer's best interest. It is likely to cause detriment and leave us open to criticism.

Now imagine another scenario where the customer does not receive the letter at all because he has moved and the debt advisor continues to write to him at the wrong address. In those cases, and through no fault of the customer, he could find that his plan is cancelled, with all of the hardship, confusion and distress that would result.

Our concern is that if the advice sector continues to interpret CONC in this way, then that is precisely what will happen, and it is the debt collection agencies that will end up multi-tasking by carrying the can and cleaning up the mess.

We believe the FCA does not intend for plans to be cancelled in this way, and that the advice sector is confusing the ambiguous grammar in the rules. We do not believe that if a plan cannot be reviewed, then it should be stopped; we do not also believe that a review has to be a formal process requiring direct contact with the customer.

An argument has been put that just because a plan is being paid, does not mean it is sustainable. It might mean that a customer is paying at the expense of putting food on the table. Whereas there might be a rare occasion when this is true, the words 'baby and bathwater' spring to mind and the measure of sustainability – in the vast majority of cases – will be apparent if a plan is either being maintained or defaulted upon. The use of the phrase 'where appropriate' in relation to a review is also being overlooked.

There is no implied criticism of the advice sector in their interpretation of the rule, and we are working closely with them – and the FCA – to clarify what action is required.

I think all of us would agree that the idea of regularly reviewing a debt management plan has to be a good thing, but in doing so, we must not create more problems than we intend. CS

The risks of punishing a reformed sector

StepChange's analysis of the short-term credit sector shows a need for consistent regulation across high-cost and mainstream credit, says STUART HOWARD

Stuart Howard

Chief executive, Dollar UK

We welcome StepChange Debt Charity's recent report into payday loans, which recognises the improvements that have been made in the industry since it came under FCA regulation.

The report says debt charities have seen a "significant reduction" in clients approaching them with problem debt issues caused by high-cost, short-term loans.

It also recognises improvements in debt collection practices and a significant reduction in irresponsible lending.

As UK chief executive of one of the leading consumer finance providers, I'm delighted to see that recent changes have led to the departure of the more unscrupulous elements in this sector, and greater professionalisation.

But this is not a moment to rest on our laurels or slip into complacency. Nor is it a time for the leaders in this sector to let their guard down. StepChange's report also makes recommendations for more stringent regulation, and presents an unfavourable analysis of some recent product changes.

The case for instalment loans

In particular, the shift away from single repayment 30-day loans towards longer term instalment loans has come under fire for the total levels of interest typically associated with these products. There is a role here for the industry to highlight the benefits of such products, which is reflected in their popularity among customers.

They allow for more flexible terms that fit customers' individual situations. With features including no missed payment fees, no rollovers and the option of weekly repayments, they can make borrowing very manageable. This is reflected in the low number of instalment loan customers that are unable to repay – which StepChange's report attests to itself.

As an industry, our aim is to provide products and services that our customers want in a speedy and accessible manner – while at all times being sensitive to a borrower's ability to afford a loan. StepChange's report indicates that more often than not, this balance is being achieved effectively. Some 84 percent of the charity's clients now have debt problems completely unrelated to high-cost short-term loans.

To my mind, this demonstrates the importance of one of StepChange's key recommendations – that the FCA should ensure consistency of regulation across high cost and mainstream credit.

Having joined the industry at a time of strict regulation from the FCA, and seen the important impact this has had in ensuring affordability and tackling problem debt, I think it would be precarious to stifle people's access to credit by overreaching in this reformed sector.

There is still much to be done to protect customers who are adversely affected by other forms of credit products.

I see balanced FCA intervention as an opportunity for the whole credit industry to benefit from the same improvements we have experienced. CS

A collective will to treat SMEs fairly

The LSB has an important role in defining conduct standards for SMEs when it comes to access to finance, explains DAVID PICKERING

David Pickering

Chief executive, Lending Standards Board

What a year this has been. Never would I have envisaged the vote to leave the European Union and Donald Trump becoming the 44th president of the United States.

I have no idea what impact these events will ultimately have on the UK economy in the medium to long term, but I do believe the only way we have any chance of making Brexit work is to become more productive and, in effect, trade out of any financial downturn through efficient working, intelligence, innovation and hard work.

Which brings me on to SMEs and the role they will play in this. According to statistics from the Department for Business, Energy and Industrial Strategy, in 2016 there were 5.5 million private sector businesses at the start of 2016, of which 99.9 percent fell under the SME definition.

These businesses employed 15.7 million people, accounting for 60 percent of all private sector employment in the UK. That's significant by any measure and essential, therefore, that these businesses are given every chance to thrive. Access to finance is central to this, supported by adequate protection from the point at which the business is discussing potential borrowing, through to when the borrowing ends or the business finds itself in difficulty.

So what part is the Lending Standards Board (LSB) playing in addressing this? While the lending code has been replaced by the standards of lending practice for personal borrowers, it still applies for micro-enterprises - businesses with a maximum €2m turnover and 10 employees. It applies in respect of loans, credit cards, overdrafts and charge cards. The responses to the review of the lending code suggested there is substantial industry support to redefine the protection offered to SMEs.

> *"We recognise the importance of vulnerability in the context of SMEs"*

Voluntary standards

In its discussion paper on SMEs as users of financial services, the Financial Conduct Authority (FCA) indicated it would encourage the industry to develop voluntary standards.

We were keen to take a step up from the current lending code and we are addressing issues relating to the number of businesses captured and product scope, with a view to increasing both. There has been a strong desire to offer protection to more businesses and it's likely the standards will capture those with turnovers of up to £6.5m.

Product scope will be extended via phases, with the first covering existing products, including secured loans, with asset finance and peer-to-peer lending to follow in future phases.

The aim is to appeal to a wider range of firms. We hope those who finance or lend to SMEs, but who are not currently registered with us, will want to register, provided they meet requirements.

The LSB has been working with the industry to define the standards for business customers, based along a similar structure to the personal standards, with desired consumer outcomes and principles that cover areas such as credit monitoring, portfolio management and declined applications.

We recognise the importance of vulnerability in the context of SMEs. While there has been considerable progress in relation to personal borrowing, more could be done for SMEs, with some considerations revolving around borrower type and size of the organisation. The LSB will be producing detailed information for practitioners, which will contain good practice to help firms meet the standards.

So when will we see the detail? We are on target for a launch in the first quarter of 2017 for phase one, with phases two and three covering the extended product scope scheduled for later in the year.

There will be a gap analysis period to enable firms to identify where they are currently meeting the standards and where more work is required, before an implementation period is then set for those areas needing more work. As with all new requirements the most important aspect is getting the implementation right.

There is a collective will from firms and other stakeholders to ensure SMEs receive consistent, fair treatment. CS


S166 order
Gabriel
Skilled person review
CONC

ALL OUT OF PROPORTION?

The cost of compliance has forced many consumer credit firms to spend more time and energy focussing on audits and oversight, rather than growing their businesses. AMBER-AINSLEY PRITCHARD asks if a sense of proportionality has been lost over its true purpose

The cost of compliance for consumer credit firms can be most starkly reflected in the case of Motormile Finance (MMF).

MMF, a debt purchase and collections firm, has spent more than £2m on staffing costs, modern systems and legal fees to become compliant since 2013.

Most of this was spent on requirements as part of the section 166 order which triggered a skilled person review of the business in February 2015.

Its chief executive Denise Crossley gave an exclusive interview to *Credit Strategy* in which she outlined the full compliance costs that the business has had to endure.

Crossley said: "The whole of the section 166 process inclusive of the skilled persons' fees, their lawyers, our additional lawyers and other professional fees equates to around £900,000."

These figures exclude the balances of £414m face value debts that MMF had agreed to write off and the customer redress in cash payments of £154,000. These were actions agreed with the Financial Conduct Authority (FCA) as a result of the review.

MMF said during the last two years that it has spent around £250,000 in strengthening teams, letting go of staff members who no longer had the required skills and replacing them appropriately. It also estimates to have spent more than £150,000 on a new IT system. Crossley said it would be true to say the firm had spent more time and energy focussing on audit and compliance rather than growing the business in 2015 and the first quarter of 2016.

She added: "However, we have continued to buy books almost monthly throughout this period from our existing relationships, but under the watchful eye of the regulator and had to spend an average of £10,000 per book for each due diligence sign off, as this was the FCA's primary focus in terms of debt purchasing."

In its own release about the skilled person review, the FCA said it had found failures in the debt purchaser's due diligence and collections process, but it was notable that the regulator mentioned both the changes led by the debt purchaser's chief executive and the extent of engagement between the regulator and the business.

In August 2016, the FCA authorised the firm after being satisfied its poor practices were historical and major changes had been implemented.

Crossley said: "Working so closely with the FCA has provided MMF with a very clear understanding of what is expected under the new regulatory regime, in comparison to how debt purchase was executed previously. I can assure our clients that MMF has embraced this."

MMF is the most recent, most prominent example of how costly and challenging FCA intervention can be, for many different types of regulated firms.

The most recent figures from the FCA show there have been a total of 25 redress schemes put in place since 2014 resulting in just over £782m of redress to consumers.

Skilled person reviews

Skilled person reviews appear to be by far the most expensive measure through which regulatory costs are imposed.

If the regulator becomes suspicious or believes there is misconduct happening within a business it can ask a firm to provide a report by a "skilled person" under section 166 of the Financial Services and Markets Act. These independent reviews are typically carried out by accountancy firms to gather historic information or evidence for determining whether enforcement action may be appropriate. They can also be used to obtain expert analysis for the purpose of seeking remedial action.

However the regulator said this is not the only tool it has when responding to an issue with a firm.

For the first nine months of 2016 there has been only one skilled person review commissioned to a consumer credit firm, which has not been named.

However, there has been a total of 29 skilled person reviews commissioned for consumer credit firms between January 2014 and September 2016.

There are no total statistics available to highlight the costs these consumer credit firms have incurred when being the subject of a skilled person review.

However, the Prudential Regulation Authority (PRA) has statistics for these costs incurred by financial services firms as a whole.

1,747

The number of consumer credit firms which have left the market in two years

£2m

The amount Motormile Finance has spent on compliance since 2013

£782m

Paid to consumers as part of redress schemes since 2014

From April 2013 to March 2014, 33 skilled person reports were commissioned costing financial services firms a total of £11.4m.

Market impact

As at June this year, the last time official figures were published by the FCA, there was a total of 31,000 authorised consumer credit firms.

There are figures that speak volumes about how much the industry has shrunk or contracted in the time taken to authorise these companies.

Nearly 1,750 firms have either had the door closed by the FCA or withdrawn applications – largely among the latter due to the cost of authorisation.

The FCA also estimated during the summer that it will have authorised 35,000 firms by the end of the process in 2017.

John Lamidey, policy advisor at the Consumer Credit Trade Association (CCTA), said: "My own personal view is that the majority of firms that either never even applied for FCA authorisation, or dropped out of the authorisation application process, have done so simply because the regulatory requirements mean they can no longer trade profitably."

In a speech earlier this year, Jonathan Davidson, director of supervision – retail and authorisations at the FCA, said the authorisation process is used to ensure the market works fairly, drive up standards and keep out the firms that don't meet these standards.

He explained how a non-executive director at a consumer credit firm told him the authorisation process had been a "nightmare" but added that his firm was now in the best place it had ever been as a result of the process.

A distant relationship

While many collections firms bar barely a handful, are now over the line, they are now eyeing up compliance costs that form part of the continuous relationship with the regulator.

The FCA has outlined several things a firm must do once it becomes authorised.

A firm must supply information, such as its consumer credit income and transaction volumes, to the regulator on a regular basis.

The FCA uses two online systems, Gabriel and Connect, to ensure firms are up to date with reporting requirements. Gabriel will update firms when they must submit information or reports to the FCA and this information will be used to work out firms' fees for the following year.

The consequences of not submitting information on time can lead to a £250 admin fee or in some serious cases a firm can lose its permission.

> "The whole of the section 166 process inclusive of the skilled persons' fees, their lawyers, our additional lawyers and other professional fees equates to around £900,000"
>
> **Denise Crossley,**
> **Chief executive, Motormile Finance**

Connect is used for firms to notify the regulator if there is a change of details such as an address, if an approved person leaves the company or if the permissions the firm hold changes.

The platform will also notify firms when they are due to pay their yearly fees to remain authorised.

Davidson has also pointed out how important it is that firms stay up to date with regulation post authorisation.

This all seems to suggest there won't be a sudden drop off in costs. During *Credit Strategy's* recent Collections, Debt Sale & Purchase (CDSP) conference, delegates were asked, via the online poll app sli.do, whether the cost of compliance would rise, fall or level out for their firms next year.

Just over half said the cost would increase whilst 33 percent thought it would stay roughly the same and the remaining 15 percent believed there would be a decrease.

As for applications, the regulator will carry on working through them until a date, yet to be confirmed, in 2017.

Authorisation fees for consumer credit firms are based upon the income generated from its consumer credit activity, not turnover, and the complexity of the application. Some fees could be as high as £15,000 and this is non-refundable even if the application is rejected.

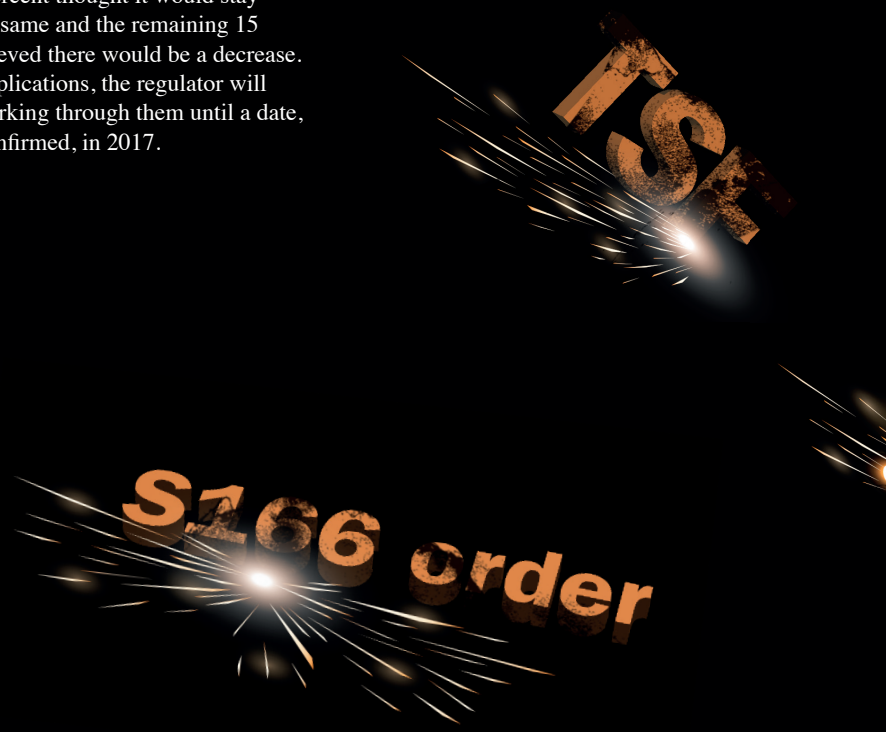
The FCA said it will invoice a firm its first annual fee shortly after it becomes authorised. It added that a new firm's first annual fee will be a pro-rata fee from the date the firm becomes authorised.

The preparation game

During the past couple of years firms have prepared for the new regulatory relationship in different ways, but the common thread has consistently been cost.

Paul Jenkins, chief executive of debt collection agency Wescot, said the firm had already been prepared for the authorisation process by using "common sense" when the thematic review of mortgages was introduced by the Financial Services Authority in 2011. He said Wescot aligned itself with this regulation after attempting to predict what requirements would be brought into the sector.

Jenkins added: "Most of our clients were demanding a higher level of compliance so we read and read every bit of information and consultation the regulators published. Because we took that approach at that time it has meant we haven't had to invest more money than needed – we just keep making decisions aligned to the rules so when



we did, and do invest, we aren't wasting money."

Sigma, the credit management-focussed outsourcing business, said its compliance-related investment has been significant over the past five years.

It said it has expanded its compliance team and added greater compliance responsibilities to the roles of its senior leadership roles.

A spokesperson for Sigma added: "There hasn't been a race or competition to get over the line first – it's been more of a focus on ensuring that everything is done correctly."

Another firm to have increased its staff as part of meeting compliance regulation is deceased account management specialist Phillips & Cohen Associates.

The debt collection agency said it has invested in extra resources and the enhancement of systems to help manage policies more effectively, and to improve process oversight and control.

Nick Cherry, managing director of Phillips & Cohen, said: "We have also significantly strengthened our three lines of defence governance model and similarly our client-facing audit team to ensure we are equipped to provide compliance reassurance to clients. Our biggest single investment has been the implementation of post-call and real-time speech analytics to provide improved compliance reassurance across our business."

Drydensfairfax Solicitors, the specialist debt recovery law firm, is regulated by the FCA and the Solicitors Regulation Authority (SRA). In readiness for FCA authorisation the firm recruited dual heads of compliance in 2014 and since then, staffing costs have tripled.

> "It (compliance) has now become a 'spectator sport' where we are replaying events rather than looking forward at how we might improve our industry and ultimately the customer journey"
>
> **Philip Holden,**
> **Executive chairman, Drydensfairfax**

Philip Holden, executive chairman of Drydensfairfax, said every area of the business has been impacted, so it has been difficult to calculate the overall costs.

He said: "It is not just the direct cost but the lost revenue and increased time of addressing the increased call times associated with what is now customer management rather than debt recovery."

Holden also said the firm has spent considerable time and energy focussing on audit and compliance which has made it challenging to keep the same focus on growing the business.

He added: "It (compliance) has now become a 'spectator sport' where we are replaying events rather than looking forward at how we might improve our industry and ultimately the customer journey."

According to the CSA's Data Gathering Initiative earlier this year, staffing levels in the collections sector increased 2.4 percent from the second to third quarter of 2015.

At the time the CSA released these figures, John Ricketts, vice president of the trade body, said: "What is perhaps most striking about these figures is the continued increase in non-collections or 'back office' employees."

This total rose to 5,384 in the third quarter last year, from 5,203 in the previous three-month period - an increase of 3.5 percent.

In the same report Ricketts added: "Indeed, these non-collections staffing numbers have been through a sea change over the last few years, no doubt driven by the increasing cost of compliance under FCA regulation.

"The number of non-collections staff has now increased by almost a fifth in the last two years."

A growing number of firms appear to hope that logic and common sense will play a more important role in how the FCA's regulations are interpreted - and how these interpretations affect customer interaction.

Holden added: "The application of common sense and a degree of proportionality would help us all in this regard.

"In the absence of such a revised approach, the potential outcome going forward is that suppliers will route customers to self-serve processes to avoid the risk of speaking to customers and reduce the costs of handling. This isn't always in the customer's best interests and (in effect) defeats the point of ensuring an appropriate customer journey in every case." CS

RAHUL PAKRASHI
Chief risk officer
Funding Circle

AGE OF ENLI

GHTENMENT

Circumspect eyes have been cast over the peer-to-peer lending sector, particularly over how it will fare in a full credit cycle. But as RAHUL PAKRASHI, chief risk officer at Funding Circle, explains to Credit Strategy **editor Marcel Le Gouais, the sector needs to educate the uninitiated**

RAHUL PAKRASHI

Chief risk officer
Funding Circle

Funding Circle's office on the City's outskirts has more the appearance of an entertainment venue for the 20 to 35-year-old bracket, than a pioneering financial services business.

Maybe this is exactly what you can expect of a fast-growing, fintech environment.

In a Funding Circle-themed bar that forms a sizeable chunk of the office, millennials are drinking lattes and exchanging ideas that will no doubt redefine credit modelling as we know it.

Next to the bar, employees can play table tennis, shoot a game of pool or sit back for a meeting in bright, circular architecture that pretty successfully, judging by the atmosphere, cultivates a sense of energy.

But the most notable point is that for a company only just six years old, Funding Circle has been picking up awards year-on-year as if it was second nature. I counted 35 industry trophies encircling a central pillar, not least of which is a prize for Alternative Lender of the Year – Commercial at our own Credit Awards scheme in 2013.

Funding Circle's peer-to-peer platform for investors to back small businesses has made waves in the past two or three years, to the extent that it's now attracting talent from the top echelon of financial services; Eric Daniels, the former chief executive of Lloyds Banking Group, joined in September as a non-exec director.

The business has also been described as the first peer-to-peer 'unicorn' – having been valued in the US at $1bn.

Investors using the platform include 50,000 people, local and national government bodies, along with a range of financial institutions such as pension funds, who have invested in around 15,000 businesses. The firm's CRO Rahul Pakrashi revealed to Marcel Le Gouais how the business approaches relationship management with its micro SME customers.

MLG: Tell me about the role.

RP: "I'm accountable for all areas related to risk in the UK. There are three broad dimensions to the role:

- Reputational and conduct risk – which is chaired by our legal counsel;
- Operations risk committee which I co chair;
- Credit risk management committee which I chair.

"Across these three dimensions, we manage those three aspects of risk. We don't lend from a balance sheet, so while we take credit risk very seriously, business risk is much higher. It's also a start-up, so there's a fairly flat structure for credit risk management, but the purpose of the credit risk committee is to manage credit risk through the entire lifecycle of our borrowers. When we talk of a lifecycle, it has four components:

- Marketing which includes targeting and channel mix;
- Underwriting;
- Customer management which includes pre-delinquency strategies;
- Collections and recoveries.

"These four components drive our loss forecasting methodology. We devise the policies which are aligned around the risk appetite of the company. So any action, policy, strategy or change that we want to make in either targeting, or underwriting or credit risk models in customer management, will be approved by the credit risk committee. We will devise all the credit policies that we want to observe and implement and these are passed onto the frontline team in underwriting. Like the banks, we do have a third line; which provides auditing and independent assurance."

MLG: Would you describe collections as sitting in first line here?

RP: "Yes, collections sits in operations and is first line. The three lines of defence (business/ops in the first line; risk in the second and audit/QA in the third) are distinct in terms of roles and responsibilities, staff and mandates. They are integrated in their approach and goals.

"So the third line audit and sample collections procedures. They listen to calls we have with our borrowers who are in trouble, to ensure policies are being followed and that there's no digression.

"In the second line, we will devise what the criteria for defaults should be. With regards pre-delinquency, I will generate an early warning list to pass onto the pre-delinquency team to help current borrowers, where something bad is about to happen, to make sure things are OK.

"As for borrowers who are already missing payments, I will generate a likelihood of payment for those borrowers. There is so much data available to me; we have a view of how much secured and unsecured borrowing each borrower has. We can harvest that for a view of the affordability of each borrower.

"Collections is very different from how banks manage it, because within the banks, there is a balance sheet to absorb any losses. For us, it's most important that the borrower survives – because these are micro SMEs. The borrower might have only one supplier, so very small movements may make or break them. But if you work with them, understand them and support them, you can default ➢

RAHUL PAKRASHI: THE CV

Chief risk officer
Funding Circle UK
2012 – present

Senior consultant
Oliver Wyman
2010 – 2011

Vice president - credit policy and risk management
HSBC (Chicago)
2010 – 2010

Manager - credit policy and risk management
Discover Financial Services
2007 – 2010 (Chicago)

Manager - credit policy and risk management
Morgan Stanley
2004 – 2007 (Chicago)

them but have a view on how they can overcome their situation."

MLG: So how does your approach to struggling borrowers work in practice?
RP: "Internally, there is a survival for revival methodology that we follow. It is in our interest, and our investor's interest, that the business owner survives through a problem he or she is facing. Quite like ourselves, our borrowers are solid entrepreneurs. If they can survive a crisis, they will be able to start another business one day, and continue to make repayments to us. We will be able to make recoveries for investors.

"Like the banks do, we approach this in three ways:

- Can I identify affordability of the borrower?
- The amortisation nature of the loan – how many payments does the borrower make, before he/she does default?
- If he/she defaults, how much can we recover?

"A vast proportion of our recoveries also comes from personal guarantees. Each and every loan we write will have the director behind it, as a personal guarantee. Again, because these are micro SMEs, they may or may not have unencumbered assets to take security on, so we will take security on large ticket items, but our average ticket is £50,000 to £60,000. Therefore, every loan will be backed by a personal guarantee so if the borrower does default, that's how most of the recoveries are made. We've found this to be very effective."

MLG: So are a lot of your customers start-ups?
RP: "No, most of our customers are established businesses. The average age of businesses on our book today is 10 to 11 years. Interestingly, 11 years means they have survived the last recession. A typical customer could be, for example, a small widget manufacturer in Scotland.

"These borrowers are small businesses with an average turnover of £500,000 to £600,000. Typically, these borrowers also do not have business loans - the borrowing might be on their credit cards. It's much more complicated with these businesses to understand them properly."

MLG: How would you describe a typical customer?
RP: "These businesses are typically one man shops. There's also a lot of 'web-tech' firms that started in around 2004 or 2005.

"These types of firms don't have many assets and they don't have many borrowings. If you look at how they borrow from the banks, they don't have classic SME loans, they don't do things like hire purchase for example. Everyone has a current account but a lot of their borrowing is on credit cards.

"If they don't have company borrowings they can't technically enter insolvency. And if you look at the insolvency rates of these sorts of companies, it almost looks as if they're recession proof.

"However these businesses tend to close instead of entering formal insolvency. During a period of five years that I tracked, from 2006 to 2011, only 25 percent of these types of firms lasted that five-year period.

"So the closure rate is high but many of these are family-run businesses - perhaps just a husband and wife partnership. They basically do it to feed their families and they just want a stable income. They don't necessarily have big expansion dreams; they don't necessarily want to be the next Tesco.

"So typically, after a period of dwindling income, they close the business, pay creditors off and start something else.

"But that's important to remember, because if I start defaulting companies with poor or dwindling turnovers, this will pretty much remove the chance for them to successfully start another business, because directors from a defaulted company will get blacklisted.

"This is the nature of these SMEs that we need to understand. This understanding requires us to have very sophisticated models and it helps us to maximise recoveries for investors. It's also a space where we can add value, but it's much more complicated to understand each business properly."

MLG: What models and data are you using to give applicants fast decisions?
RP: "We have a vast repository of private financial data submitted to us by our customer pool over the past six years. Using this data, we have developed very powerful models for each type of business.

"So when a business applies for funding, we use 50,000-plus data points to score the deal, and provide a price in seconds. Our model software code is modular, so we can test and improve them fast.

"Next year, banks will have to share more credit data on SME customers with the credit reference agencies. This will give us a better view of profit and loss and affordability; it presents a big opportunity for us. However

CREDIT WEEK

CREDIT SUMMIT

As well as appearing at our **F5 Conference**, which is targeted at the alternative lending sector, **Rahul Pakrashi** will be appear on a CRO panel at next year's **Credit Summit,** which is part of our inaugural **Credit Week**.
Visit **creditweek.co.uk** for more details.

the credit reference agencies have now informed us that the data will not be available to any issuer before February."

MLG: There's a lot of cynical industry talk about defaults and loan loss coverage at peer-to-peer lenders, can you tell me about how that works here?

RP: "We are writing new business of about £100m each month in the UK and our default rate in the UK is six percent.

"The good thing is that in terms of coverage, investors are receiving net returns of about seven percent after all fees and losses. The loss rate is about two percent. But if you look at the gross yield, it's about 10 percent minus one percent in fees, so nine percent.

"So you can compare two percent of losses with nine percent of returns before losses, and quite quickly you understand that you have to multiply it by 4.5 before an investor starts to lose money. So the coverage is 4x.

"For the super prime portion of our book – the A pluses and As – the coverage is 10x. That book is performing at 0.4 and 0.5 percent loss rate and earning about seven, eight and nine percent returns. It's 10x, so if you are investing in super prime via Funding Circle, things need to worsen by 10 times as much before losses are incurred.

"If you take a passive slice, which is what we recommend to investors in the Funding Circle book, things need to worsen by four times as much, before you start losing.

"We take this information and we look back at what happened empirically. For example, during the financial crisis of 2008, things got worse 1.66 times. But what about Funding Circle? As we have a micro SME book, what about them? It was actually 1.5 times worse because as I said earlier, these tiny companies don't go insolvent, they just close. If you look at concentrations in the construction industry, as an example, it goes up to 2x. Whichever way you look at it, the last time we had a big financial crisis, things got 2x worse. If I'm running with a 4x coverage, we do not expect investors will lose money in a downturn."

MLG: The former FCA chair Lord Turner famously said that losses will emerge from peer-to-peer lending over the next five to 10 years that "will make bankers look like lending geniuses". He's now rowing back on that. Do you ignore these comments?

RP: "We never ignore these kinds of statements, but it doesn't affect the day-to-day operations of the business. What this does, rightly so, is inform us that we need to do a much better job in telling people what actually works under the hood.

"To some people on the outside, this looks like this is a new alt-fi industry and to them, who knows what goes on inside it? But if you do look underneath the hood, there are very sophisticated models in operation; there are very smart people executing these models, often in much better ways than the banks do – often because those banks are constrained by legacy systems and challenges with implementing any changes.

"So it is for us to educate the market. We need to educate people about our governance structure, which is the same, as is the system of controls. In terms of decision making, it is sometimes even smarter. We can talk about it for a long time, but ultimately, do we have a track record? Funding Circle has six years of performance. If any of what I'm telling you wasn't true, that would show in our performance.

"We know there is this debate around having skin in the game – that we're not lending any money ourselves. But there's a transparency to what we do that outweighs that argument. Every loan-level piece of data – every business which has missed a payment – gets published.

"With a bank, you have to wait for the balance sheet to be published. Again, we need to educate the industry about how we are different." CS

Debt recovery firm hires First Utility's Ian Parry

Ian Parry
Principle consultant
CDS Global

Ian Parry, the former head of credit operations at First Utility, has joined international debt recovery agency CDS Global.

He will act as a principle consultant working across the business to develop new relationships and increase the firm's revenue.

CDS Global, based in the UK, provides corporate debt solutions and commercial recovery and credit management solutions.

The firm uses software that enables it to adjust collections for individual cases based on a client's credit scoring and behaviour.

Parry worked at First Utility for two years and was responsible for operations across credit risk and collections, as well as fraud and recoveries, for business and residential customers.

GFKL Lowell appoints regional boss

Thomas Dold
Regional manager
GFKL Lowell Group

GFKL Lowell Group has appointed the former chief executive of Tesch Inkasso Group, a German collections firm acquired by the debt purchaser, as its regional manager of Germany, Austria and Switzerland.

The group said Thomas Dold will fill the newly created role of regional manager to bring the capacity and capability needed for growth.

Dold previously spent 13 years working at IBM in Germany and across Europe, the middle east and Africa, before moving into the new media and technology sectors.

He was then managing director of credit information provider Dun & Bradstreet Deutschland for nine years before joining the team at Tesch Inkasso Group in early 2015.

Enforcement firm hires former fraud officer

Joe Chapman
Enforcement manager
Court Enforcement Services

Court Enforcement Services has appointed a former on-street audit and fraud officer from Marston Holdings as its new enforcement manager.

Joe Chapman, also a certificated enforcement agent, will report directly into operations director Daron Robinson.

He will work with the support services department and enforcement agents to provide support, advice and guidance.

Robinson said: "We feel the strong link between the office and field team has helped us achieve some exceptional results for our clients, and Joe's role is vital in maintaining and further developing that."

Non-prime lender makes four senior appointments

Elevate Credit International, provider of short-term loan Sunny, has added four new members to its executive team in the UK.

Karen Taylor has joined as general counsel, Lauren Darby as vice president of marketing and director of HR, and George Power as senior director for product development. Steve Grice has also been appointed as chief technology officer.

Taylor is joining full time, having worked with Elevate UK as a consultant since the launch of the Sunny brand in 2013.

Darby is heading up Elevate UK's marketing division, which includes leading the strategy and development of the direct marketing, brand, CRM, partnerships, PR and social media departments, having previously been at Experian.

Power will be responsible for the service portfolio and strategic partnerships. He brings more than 20 years' experience in international telecoms. Grice will be leading all aspects of technology, having previously held various senior technology leadership roles in financial services, most recently at RBS.

Rob Lankey
Chief executive
NACFB

The former managing director at Aldermore Bank has been appointed as interim chief executive of the National Association of Commercial Finance Brokers (NACFB).

Rob Lankey has taken over the role of chief executive since Adam Tyler stood down at the end of October, after 11 years in the position.

Lankey will assist NACFB with the transition from the departure of Tyler to the recruitment of his replacement.

Lankey previously worked at challenger bank Aldermore for nine years, up until June this year, in several positions including managing director of commercial mortgages and property development finance.

He previously held the position of executive director of lending and operations at Base Commercial Mortgages which merged with Ruffler Bank in 2009 to become Aldermore.

Jerry Barrie
Head of asset management
Aldermore

Aldermore has made several new appointments across risk management, to support its business finance division. Jerry Barrie, who has been appointed as head of asset management, will monitor and evaluate the bank's asset finance portfolio and collateral. Prior to joining Aldermore, he worked in asset management at CIT Vendor Finance, a commercial and business finance provider.

Paul Buckland has also joined as head of in-life credit; David Fabia as head of flow credit and Eamon Foley as interim head of analytics and policy.

David Farnell
Partner, recoveries services group
Shoosmiths

Law firm Shoosmiths has appointed dispute resolution and asset finance expert David Farnell as a partner in its recoveries service group. Joining from competitor Addleshaw Goddard, Farnell has more than 20 years' experience as a finance litigator. Having worked with UK banks and financial institutions on various disputes, he has particular expertise in consumer credit, corporate recovery, enforcement of securities and fraud. Farnell will be working in Shoosmith's new Leeds office.

The champions of service

This year marked a decade of the Collections & Customer Service Awards. A revised roster of categories for 2016 reflected the profession's journey towards customer centricity, during these past 10 years. AMBER-AINSLEY PRITCHARD reports

Customer service management has now become the more common phrase to describe the day-to-day operations of the debt collection sector.

That's why our awards scheme targeted specifically for collections firms took on a new name last year. The narrow word 'collections' didn't quite do justice to the comprehensive service now provided by the vast majority of the profession.

Last month the 10th annual Collections & Customer Service (CCS) Awards, at the iconic Midland Hotel in Manchester, celebrated those who are leading the pack on both fronts.

This year, in fact, *Credit Strategy* received an influx of entries across a diverse range of categories which had been refreshed to reflect the industry's constantly evolving approach to customers.

As Kamala Panday, publishing director at *Credit Strategy*, explains: "We have recognised that agents and contact centre teams – as well as their leadership – are on the front line when it comes to driving excellence in conduct, and so we have moved to give them more recognition.

"The scheme has also broadened its base to recognise the ongoing growth of debt purchase internationally, as well as the general treatment of non-performing loans."

Another purpose for revamping the awards was to recognise the focus on conduct and compliance, particularly when it comes to the treatment of vulnerable customers.

This is one of the reasons why the Vulnerable Customer Support Initiative Award was split into two sub-categories of 'creditor' and 'non-creditor'. It says something that this category's popularity forced a split into sub-categories.

Once again, the CCS Awards judging panel featured some of Britain's biggest banks such as RBS, HSBC and Santander, along with MBNA, Tesco Bank and the Credit Services Association.

And on the night itself, as well as senior directors at the banks, partners at law firms and chief executives, the event united individuals from trade bodies and government authorities. HMRC, particularly, has engaged fully with the scheme.

UK debt purchaser 1st Credit was the only firm to bag more than one award on the night. It won both the Best Conduct & Compliance Culture Award, sponsored by Lowell Group, and the Best Customer Service Award, sponsored by communication solution company Adare.

During the evening, guests were entertained by Canadian comedian Sean Collins, while London-based band Beat Bandito provided a Mexican musical backdrop.

On the night guests also raised £2,276 for *Credit Strategy's* chosen charity, the Children's Air Ambulance, which flies critically ill children across the UK to get the specialist care they need. Thanks to a subsequent generous donation of £724 from judicial services group Marston Holdings, a total of £3,000 was raised for the charity.

Emma Jones, national partnerships manager for the charity, said: "It is the first and only dedicated paediatric helicopter emergency transfer service in the country. The bespoke, specialist equipment on board our helicopter provides a flying intensive care unit for children. When a child is too sick to fly, the Children's Air Ambulance can fly a specialist team to them."

The awards night followed our annual Collections, Debt Sale & Purchase (CDSP) Conference which had two streams focussing on the UK and Europe, with speakers from creditors including Barclays and the Student Loans Company all taking part. See Analysis, p8-11, for a full report. CS


Arrow Global scooped the International NPL Expertise – Company award

The Barclaycard team, winners of the Vulnerable Customer Support Initiative – Creditor category


Money Advice Trust picked up the trophy for Debt Advice Provider of the Year

CCS AWARDS WINNERS 2016

Best Technology
WINNER: Zinc Group – powered by Enghouse Interactive technology

Charitable Initiative of the Year
Sponsored by Marston Holdings
WINNER: Shop Direct
HIGHLY COMMENDED: Dollar UK

Public Sector Collections Team of the Year
WINNER: North Warwickshire Borough Council

Debt Advice Provider of the Year
WINNER: Money Advice Trust

International NPL Expertise – Company
Sponsored by Credit Week
WINNER: Arrow Global

Agent of the Year
WINNER: James McShane, HMRC – Debt Management Telephone Centre

Best Legal / Judicial Services Provider
Sponsored by Hito
WINNER: The Keith Jones Partnership

Best Conduct & Compliance Culture
Sponsored by Lowell Group
WINNER: 1st Credit

Contact Centre Team of the Year
WINNER: HMRC Debt Management Telephone Centre, Livingston

Best Customer Service
Sponsored by Adare
WINNER: 1st Credit

Vulnerable Customer Support Initiative - Non-creditor
WINNER: StepChange Debt Charity

Vulnerable Customer Support Initiative – Creditor
Sponsored by Phillips & Cohen Associates (UK)
WINNER: Barclaycard

A decade of pioneers

As part of the 10th Collections & Customer Service Awards, Credit Strategy honoured 10 individuals for their pioneering work across consumer credit. KAMALA PANDAY provides a brief synopsis of their lasting impact on the market

To mark 10 years of the Collections and Customer Service Awards, *Credit Strategy* recognised the individuals and partnerships that have been instrumental in developing a modern, mature and fair collection market in the past decade. Those awarded in this list have broken new ground in the field of collections, debt sale, customer services and debt counselling. These pioneers have also shown great intuition in creating public and private sector partnerships, spearheading charity campaigns and leading the way in continental expansion. CS

CCS Awards category sponsors:

DECADE OF PIONEERS WINNERS

Paul Atefi
Acquisition and leveraged finance
JP Morgan
Paul Atefi has been at the centre of change in the UK debt purchase industry due to his pivotal role in arranging bonds for debt buyers. He has engineered rated public high-yield bonds for a range of debt purchasers, starting with Lowell Group in 2012, and has since paved the way for billions of pounds of capital to be brought into the industry.

Paul and Selina Burdell
Co-founders
Link Financial Group
Paul and Selina Burdell have led the way in showing how to build a successful European credit management business from a UK base. Link was one of the first UK debt purchasers with a presence in Spain and its expertise has become truly continental - Paul himself is a senior adviser to the European Central Bank.

James Cornell and Andrew Bartle
Chief executive and Chief operating officer
Lowell Group
"The duo behind the founding and growth of one of the largest debt buyers in the UK, James and Andrew, have been behind innovations in NPL bonds, as well as playing a major role in changing the culture of UK collections conduct. Through a merger with GFKL, they have seen Lowell become a major league European collections player.

Gareth Hughes
Chief executive
Marston Group
Gareth has led the creation of the largest judicial services organisation in the UK. Under his leadership, Marston's progress has been marked by a series of acquisitions and major contract wins. Gareth himself has had a major impact on standards of conduct and legislation across the enforcement world.

DECADE
OF PIONEERS
AWARDS
2016

Malcolm Hurlston
Founder
CCCS (now StepChange Debt Charity/ Registry Trust)
Malcolm has been a household name in credit management for many years. In particular, he is known for his pivotal roles at StepChange Debt Charity (formerly CCCS), one of the largest debt counselling charities in the country, and Registry Trust, the central repository of CCJs in the UK.

John Kirkby
Founder
Christians Against Poverty
A man of enormous principle, John Kirkby (second from left, above,) launched a landmark charity with little but faith and determination. Christians Against Poverty now helps 38,000 consumers in five countries and 22 locations in the UK, and maintains a major call centre in John's native city of Bradford.

Zach Lewy
Founder and chief investment officer
Arrow Global
A gifted technical expert as well as a widely respected leader, Zach Lewy launched a UK debt buying operation with a unique model in Arrow Global. After a journey that saw the business become the first of its kind to float on the London Stock Exchange, Arrow has become an international leader in its field.

Francis Maude
Former minister of state for trade and investment/minister for the Cabinet Office
Francis Maude spearheaded a more joined-up approach to management and collection of public sector debt by launching a 'one gateway' legal basis for sharing data between government departments. His work lead to the pioneering use of private sector debt collection agencies by several government departments.

Mark Onyett
Founder
TDX
Mark Onyett saw the opportunity for a more analytical approach to debt management, leading him to leave Capital One and launch TDX Group, providing creditors with platforms to maximise returns from debt portfolios. Mark has also founded or backed businesses including HD Decisions, Grove Capital and Oakbrook Finance.

David Philpott
Former technical specialist
Financial Conduct Authority
A public servant accredited with the creation of the consumer credit rulebook, David Philpott was instrumental in the transfer of regulatory responsibility for consumer credit to the FCA. Initially seconded to the Financial Services Authority from the Office of Fair Trading to provide technical knowledge and expertise on consumer credit, he has since informed the development of several ground-breaking regulatory measures.

Regulator joins elite line-up of speakers for Credit Week

Soon after announcing our first ever Credit Week, Credit Strategy can now reveal more of the speakers lined up to appear in a seminal series of events. AMBER-AINSLEY PRITCHARD reports on the regulators and banks now on board

As the centrepiece of Credit Week, the Credit Summit will be extended and expanded to cover new streams in 2017.

It will be one among a range of conferences and networking events that bring together individuals from major lenders, regulators and government personnel working within the most senior credit-related roles.

Mirroring *Credit Strategy's* transition upstream in terms of content, Credit Week will shine a spotlight on how chief risk officers create policy, the interactions of first and second line, how risk appetite is formulated, how buying decisions are made and how this impacts front-line operations within credit risk, collections and compliance.

The latest of confirmed keynote speakers at the Credit Summit is Johnathan Davidson, the director of retail - supervision and authorisations at the Financial Conduct Authority (FCA).

Davidson will enlighten delegates on the regulator's focus over the next 12 months as well as describing how the authorisation process has shaped the consumer credit market.

He will also be discussing innovation within the fintech sector, how the industry can mitigate conduct risk to ensure fairer treatment for customers and what 'business as usual' should look like post-authorisation.

Not only has the FCA stepped up to join our panel of speakers, but *Credit Strategy* has also had two more senior speakers confirm their places at the Summit.

Both Rahul Pakrashi (see The CS Interview, p26), chief risk officer of Funding Circle UK, and Stewart Livingstone, chief credit officer at Santander, have agreed to take part in a panel discussing credit risk insight.

This session will focus on how major lenders are enhancing the customer journey through credit risk and collections and how to best gauge the appetite for debt sale.

Chief risk officers from HSBC, RateSetter and Clydesdale & Yorkshire Banking Group will appear alongside Pakrashi on this panel.

We're also proud to announce we'll be expanding the Credit Summit even further to re-introduce the Trade Credit stream alongside our partners at CICM.

This will help shape the discussions around data, litigation and collections that consumer finance also faces.

Our in-depth masterclasses and roundtables will allow attendees to immerse themselves in complex and technical subjects to get the answers they need.

Further new features for the 2017 Credit Summit include the Credit Strategy Boardroom, which will bring together c-level representatives from the major lending firms.

Finally, we'll be bookending the day with a networking breakfast for 2016 Credit 100 members and finishing with the Credit 100 Gala Dinner to welcome in the 2017 members.

CREDIT WEEK
Supported by CICM Chartered Institute of Credit Management

CREDIT WEEK AT A GLANCE

What is it? A week of networking events, industry parties and conferences including the Credit Summit, which will bring UK and European credit professionals to London
Where is it? Various venues in London including the House of Commons, QEII and others TBC.
When is it? Starts Tuesday March 28, with a parliamentary reception at the House of Commons.
Who's coming? CROs at Europe's largest lenders, chief credit officers at UK retail banks, chief executives and directors from UK and European credit management companies.
How do I get involved? Visit **creditweek.co.uk** for more details, or call us on **0207 940 4835**, follow Twitter updates via #creditweek.

Political impact

Just three months after the Italian referendum resulted in the resignation of Prime Minister Matteo Renzi, Credit Week will bring together key players in the Italian and European non-performing loan (NPL) and debt sale world.

The referendum saw the country vote against constitutional changes proposed by the government to streamline decision-making by centralising power with the lower house of parliament.

After a few months of digestion this 'no' vote will be a hot topic for our speakers to discuss during the CDSP: European NPL Conference. They'll all be assessing the impact of political changes on the Italian banking sector and, therefore, NPL transactions.

This conference will host a range of speakers from Italy including Davide Falconi of BNP Paribas and Andrea Clamer of Banca Ifis. CS

Dates for your diary

Put these critical industry events, organised by Credit Strategy, in your outlook calendar.

CREDIT WEEK

March 27-31 2017
London
creditweek.co.uk

CREDIT AWARDS 2017

11 May 2017
The Grosvenor House Hotel, London
creditawards.co.uk

CREDIT AWARDS

CAR FINANCE CONFERENCE 2017

June 2017
carfinanceconference.co.uk

cf CONFERENCE CAR FINANCE

CAR FINANCE AWARDS 2017

June 2017
carfinanceawards.co.uk

cf AWARDS CAR FINANCE

Enforcement

Marston Holdings (Marston) is the UK's largest judicial services Group. We work on behalf of the government, courts and companies and individuals, to provide the fastest and most effective form of enforcement in the UK. Our strong overarching ethical framework brings consistency in terms of our five core values – respect, transparency, accountability, professionalism and innovation; values that are at the forefront of our business.

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Email: sales@marstongroup.co.uk
Website: marstonholdings.co.uk

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Website: Stripes-solicitors.co.uk
Contact: David Gallagher

The Fifth Estate

2016 – it wasn't all that bad

This is a magazine diary page, and we're within spitting distance of the new year, which means it's time for a mildly self-congratulatory retrospective on the last 12 months. Get ready to relive it all

It's not as if 2016 was an uneventful year on a global stage, but let's not waste any time talking about all that. While you can count on *Credit Strategy* for a solid treatment of what's going on in credit, it's probably not your first port of call for hardcore political analysis. So rather than rehash well-trodden political crises, it is now time for navel-gazing from us on a level that would make the *Guardian* jealous, and it's fair enough – we've worked hard this year.

For a start, *Credit Strategy* was not even our name when we entered 2016. We were an entirely different magazine, with a different remit and different ownership. All that changed at the end of January, when Shard Media Group finally gave us our chance to join the M&A party we had been writing about for so long.

From day one we set about completely changing what we do. While historically we had evolved into a media property focussed almost entirely on collections, new ownership, new energy and (if we're honest) more money gave us a chance to extend our reach.

Now, we're covering the entire credit lifecycle, from origination right through to recoveries. It has been fantastic to expand the range of things we write about, although admittedly now we seem a bit less menacing when we explain what we do at dinner parties.

As part of this expansion, we've launched new events focused more on lending - our Car Finance Conference and Awards in June, and our F5 event for the alternative finance and fintech communities in December.

Looking ahead to next year, we've also expanded our landmark Credit Summit event into Credit Week, a frankly enormous proposition involving a parliamentary reception, several new conferences, and yet more black tie dinners (but no awards) - you can find out more on www.creditweek.co.uk.

> ***"This is your chance to feedback directly to us, in a place for all to see: We are in the stocks, and you have a basket of rotten digital cabbages. Get throwing"***

But of course, we are not just an events business. In fact, we've doubled down on print publishing: Shard decided not only to retain our magazine product, but to fully rebrand it, increase the resource involved in putting it together (welcome aboard Amber), and even print it on better quality paper. Go on, treat yourself, give this very page a feel. Marvellous, isn't it.

And of course, to cap off the year, we've utterly redesigned and rebuilt our web presence from the ground up, creating something with functionality that can go toe to toe with national news brands. The new site is drastically easier to navigate, contains a wider breath of content, and will allow us to post much more in the way of blogs, analysis, reports and features.

The new website also allows users to comment on absolutely everything we write.

As such, it seems fit to finish this rundown of our year by asking you to have your say in return. Do you like what we're writing? Are there other stories we should be covering? Are we, in fact, getting it all completely wrong? This is your chance to feedback directly to us, in a place for all to see: We are in the stocks, and you have a basket of rotten digital cabbages. Get throwing. You can post your views beneath any article on the site.

Until next time, wishing you a restful Christmas season, and a great start to the new year. CS

The relaunched creditstrategy.co.uk is now smartphone and tablet-friendly

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0.2%

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