FINANCIAL
CONDUCT
AUTHORITY

Consultation Paper

CP23/5**

Debt packagers: feedback on CP21/30 and further consultation on new rules and perimeter guidance

February 2023

How to respond

We are asking for comments on this Consultation Paper (CP) by **2 March 2023**.

You can send them to us using the form on our website.

Or in writing to:

Elizabeth Kocovska
Financial Conduct Authority
12 Endeavour Square London
E20 1JN

Email:
cp23-5@fca.org.uk

Moving around this document

Use your browser's bookmarks and tools to navigate.

To **search** on a PC use Ctrl+F or Command+F on MACs.

Sign up for our **news and publications alerts**

See all our latest press releases, consultations and speeches.

Contents

Request an alternative format

Please complete this form if you require this content in an alternative format.

Chapter 1

Summary

Why we are consulting

1.1 In November 2021, we consulted (CP21/30) on a proposal to ban debt packagers from receiving referral fees. This was in response to evidence we had seen that there is an acute conflict of interest, inherent to the debt packager business model and which firms do not appear able to manage. The conflict of interest is between the need to have regard to the best interests of customers (as our rules require) and the provision of advice which maximises revenue for the firm. This increases the risk that consumers receive debt advice that may not meet their needs.

1.2 We received broad support from a wide range of respondents for the proposed intervention. However, having reflected on feedback we received about our evidence base, we decided it was appropriate to gather more evidence showing how debt packager firms manage this conflict of interest, in particular from parts of the market not as strongly represented in our existing evidence base.

1.3 We have now analysed that further evidence (set out in Chapter 2 and our Cost Benefit Analysis) and it supports our original conclusions that debt packagers do not appear to manage the identified conflict of interest well. So, we are proposing to make the rules as set out in CP21/30, with minor amendments. We are reconsulting to allow stakeholders to comment on the analysis of our expanded evidence base, feed back on our proposed implementation period and, given the passage of time since the original consultation, allow the opportunity to raise any new issues or developments of which we should be aware.

1.4 We are also seeking views on proposed perimeter guidance to clarify the boundary of the regulated activity of debt counselling in relation to activities commonly carried out by unauthorised lead generators.

Who this applies to

1.5 This consultation applies to:

- debt packager firms, appointed representatives who act as debt packagers and their principals.

1.6 The following will also be interested in this consultation:

- Individual Voluntary Arrangement (IVA) and Protected Trust Deed (PTD) providers and Insolvency Practitioners (IPs)
- persons who provide leads to debt advice and debt solution providers
- firms administering Debt Management Plans (DMP) or the Debt Arrangement Scheme (DAS)

- not-for-profit debt advice providers (NFP)
- consumer groups who represent people who may seek debt advice
- Recognised Professional Bodies who authorise and regulate Insolvency Practitioners

What we want to change

1.7 Debt packagers are authorised, commercial firms that provide debt advice services but do not typically provide debt solutions themselves. As explained in paragraphs 1.6 – 1.12 of CP21/30, we have long-standing concerns about their ability to manage the conflict of interest described above.

1.8 As a result of work we carried out previously which identified concerns regarding debt packagers' practices, a number of large debt packagers have already either left the market or are subject to voluntary requirements to cease business. With the benefit of the additional evidence we have assessed in 2022 we consider that the issues remain widespread in the market. We consider it necessary to ensure all consumers are protected and so we are proposing the new rules set out in this consultation.

1.9 Since our initial consultation, we have seen further evidence of non-compliant advice by a range of debt packagers. We consider that evidence of non-compliance indicates that the conflict of interest is not being adequately managed and is leading to the risk that consumers end up on debt solutions which require them to make payments they cannot afford, or miss out on alternative, cheaper solutions which may be more appropriate to their needs. We remain of the view that this inadequate management of an acute conflict of interest is a consequence of the debt packager business model. This model leads to non-compliant advice and creates an unacceptable level of risk of harm that we have identified.

1.10 For the reasons we set out in CP21/30, we consider that a referral fee ban is necessary to secure an appropriate degree of protection for consumers (we revisit the alternative options in Chapter 2).

1.11 We have not seen any relevant changes to business models in the debt packager market in our analysis undertaken since the last consultation that would affect the need for a ban. However, we are seeking feedback on this point.

1.12 We are also consulting on new perimeter guidance. The routes into debt solutions, in particular those solutions which are most lucrative for the referring firms and those providing the solution, often start with lead generators. Lead generators collect customer data and refer customers to sources of debt advice or debt solutions. They are often not authorised and may not consider themselves to be carrying out regulated activity. Some of these firms may refer consumers to firms or insolvency practitioners who only offer one solution. Our proposed perimeter guidance makes clear that we consider this could be advice (in which case it would be the regulated activity of debt counselling).

1.13 Where firms carry on unauthorised debt counselling by implicitly recommending a particular debt solution, then as well as potentially being a breach of the general prohibition (and therefore potentially a criminal offence), it puts consumers at risk of receiving the wrong solution. This is the harm we aim to address with this guidance.

Outcomes we are seeking

1.14 We want all debt advice firms we regulate to provide a high-quality service to consumers. This service must have regard to their best interests and be appropriate to the individual circumstances of each consumer, as our rules require, and in so doing help them to access debt solutions suitable to them. Our proposals could remove a strong incentive to not offer compliant advice. This could, consequently, reduce the overall number of consumers being referred to solutions that are not right for them, and suffering harm. We also want to provide guidance on when activities carried out by lead generators could be regulated activities.

1.15 Our proposals are important steps to achieving these outcomes. They link to our 2022/23 Business Plan focus area of 'reducing and preventing serious harm'.

Measuring success

1.16 Consumers should be confident that authorised firms will deliver compliant advice which has regard to their best interests and is appropriate to their individual circumstances. If we make the proposed rules as drafted, we expect that the current debt packager business model (based on referral remuneration) would cease to exist. We expect some firms to leave the debt advice market, and some to adopt new business models within this market. As a consequence, the level of risk of harm to consumers caused by the conflict of interest inherent in this business model would be removed.

1.17 If our proposed rules are introduced, we would monitor the market proactively using data-led intelligence. This would allow us to understand whether firms are adapting their business models in response to our intervention or exiting the market. Where firms adapt their business model, we would monitor to determine whether practices evolve in the interest of good consumer outcomes.

1.18 We want to see more consumers receiving appropriate and compliant advice. Some customers will continue to be recommended an IVA or PTD where this is appropriate. But removing the strong conflict of interest should reduce the number of consumers inappropriately referred to an IVA or PTD.

1.19 In line with the proposal in CP21/30, we are not proposing for the ban to apply to debt management firms (see Chapter 2 for more detail). But we see a risk that debt packager firms could look to become appointed representatives of a debt management firm to seek to avoid the proposed referral fee ban. This would not be an acceptable outcome as it would expose consumers to the same risks from the debt packager business model that we are seeking to address. So, our proposals include an obligation on principal firms (including debt management firms) to take all reasonable steps to ensure that their appointed representatives do not receive any remuneration from debt solution providers unless the appointed representative is genuinely acting as a debt management firm itself (see Chapter 2 for more detail). We would monitor this actively.

Next steps

1.20 We want your feedback on our proposed rules and other issues discussed in this consultation paper (CP). Please respond to the questions in this CP by 2 March 2023.

Chapter 2

The wider context

Our original proposals on debt packagers

2.1 Debt advice provides a critical role in helping consumers, who are often in vulnerable circumstances, navigate the range of options available to them. As we explained in CP21/30, debt solutions are complex, with differing eligibility criteria, each having different advantages and drawbacks.

2.2 Where an advisor assesses a customer's individual circumstances with appropriate care, they add value by suggesting a solution that is appropriate for them. However, when advisors fail to have adequate regard to the best interests of the customer, this may lead to harm. For example, customers may pay more than necessary for a solution, or face increased and prolonged indebtedness from early termination of the debt solution, leading to lower wellbeing.

2.3 One reason for an advisor failing to have adequate regard to the best interests of the customer is a financial incentive to refer them to certain solutions which provide greater benefit to the debt packager firm, even where it is not in the customer's best interest. There is a strong incentive for debt packager firms to refer customers to referral fee paying solutions (as opposed to solutions that pay no fees) and among these, to the solutions that pay the most. In the cost-benefit analysis (CBA) for CP21/30, we described these as product bias and sales bias respectively.

2.4 We developed concerns about the potential harm to consumers arising from the conflict of interest through our monitoring of the market. We set out these concerns in a 2018 Dear CEO letter and again in a Portfolio letter to all debt advice providers in 2020.

2.5 In 2020-21, we undertook multi-firm work (MFW) to see if there were still concerns with this sector following our warnings. The MFW investigated this market in 2020 and collected a variety of evidence. This was primarily composed of, but not limited to:

a. referral fee levels paid to firms in respect of different solutions and providers
b. breakdown of referrals to different solutions
c. revenue and other financial information
d. customer case file data

2.6 Having reviewed referral fee data (a) for all debt packagers, our prior understanding that there was an inherent conflict of interest was confirmed by the marked disparity in the level of referral fees between different solutions.

2.7 Our rules anticipate that conflicts of interest may arise in the markets we regulate and require firms to manage them appropriately. Our rules also require that firms have regard to the best interests of customers.

2.8 Analysis of referral and revenue data (b – c) indicated that where a consumer was referred to a solution, it was most frequently to an IVA or PTD (the solutions that pay the highest referral fees). In many cases, firms' revenues were wholly or mostly composed of these fees.

2.9 To more clearly determine whether the conflict of interest between giving advice that is in customers' best interests and generating the highest revenues from referral fees was being adequately managed, we reviewed customer case files (d above) as part of the MFW. These reviews assessed whether the advice provided by firms was compliant with our CONC 8 rules. The case files were sampled from firms that represented c.65% of the debt packager market between April 2019 and March 2020 (2019/20) by customer numbers. These firms were selected as we considered them to be representative of typical debt packagers. Of the files we reviewed, the vast majority showed non-compliance.

2.10 We had serious concerns with 90% of the files reviewed where a fee-generating recommendation was made. In particular, we identified concerns that some debt packager firms appear to have:

- manipulated customers' income and expenditure (I&E) information to meet the criteria for an IVA or PTD
- not presented the risks and benefits of different solutions in a balanced way
- provided advice that did not accurately reflect their conversations with customers or information that customers had given

2.11 In our view, this evidence, specifically linked to practices which steer consumers into solutions that maximise revenue for the firm, combined with the high rates of referrals we saw to these solutions, showed that consumers were being put at risk of substantial harm. Following our MFW, we wrote to several firms identifying our concerns regarding their practices, making clear our concern with firms continuing to offer advice to consumers while those issues remained unresolved. Five firms subsequently applied for voluntary requirements to be imposed. This means they can no longer provide regulated debt advice services unless we are satisfied that they can comply with the rules.

2.12 Since the average referral rate to paid solutions was lower for the MFW firms reviewed than for the whole market, we viewed it likely that similar failings were occurring in other firms. We concluded that the debt packager model itself presented risk of substantial harm, even if some firms at that time were giving compliant advice.

2.13 We considered a number of less intrusive interventions to protect consumers from this significant risk. However, we concluded that none of these options would effectively address the harm posed to consumers. We explain our reasoning for this and feedback from CP21/30 on these alternative options later in this chapter.

2.14 We therefore decided to consult on the referral fee ban. We proposed that debt packagers be subject to the ban, but debt management firms (who provide solutions as well as debt advice) and not-for-profit (NFP) firms should be excluded. As explained in CP21/30, debt management firms and NFPs have a different business model to debt packagers. The conflict of interest presented by referral fees is less acute as it typically makes up only a small part of their revenues. Feedback from CP21/30 on the scope of the ban is provided later in this chapter.

Responses to consultation and new evidence

2.15 We received a range of detailed responses to CP21/30, which are set out in our Feedback Statement in Chapter 4 along with our responses. Overall, there was strong agreement (75% of respondents agreed) that the remuneration model of debt packagers creates an acute conflict of interest which leads to a risk of consumer harm and therefore needs to be mitigated. Several debt advisors recounted their experiences of customers who had been placed on unsuitable IVA/PTDs where other solutions such as Debt Relief Orders (which do not generate revenue from referral fees) would have been more appropriate. One highlighted that this had led to clients ending up with more debt and adverse impacts on their mental health.

2.16 Additionally, nearly two thirds of respondents (27/41) supported our proposed ban on referral fees. Most agreed with the assessment set out in CP21/30 that alternative options were unlikely to be effective. We set out our considerations of these alternative options, and others proposed in the feedback below and in Chapter 4.

2.17 Regarding the evidence we used to justify the proposal, a minority of respondents said it was not as strong as it could be. Some respondents suggested that:

a. We had not provided quantitative evidence, such as the number of customers who go on to suffer harm following advice from a debt packager, to show that non-compliance with the rules in CONC 8.3 leads to the consumer harms we highlighted.
b. The inadequate management of the conflict of interest itself was not sufficiently evidenced for the whole debt packager market. In particular, some said that our evidence base (case file reviews) covered mainly large firms, and that smaller firms' conduct may be or is better.

Evidence of Consumer Harm

2.18 Regarding point (a) in paragraph 2.17, in CP21/30 we explained how compliance with our rules should lead to good outcomes for consumers and that not having regard to customers' best interests is likely to lead to worse outcomes. Moreover, we explained that it is not possible to quantitatively estimate the number of people who end up with unsuitable solutions because:

- **Debt advice is a type of 'credence good'**, which means that it may be difficult for a consumer to assess the quality of the advice even after it has been received. For example, if a consumer is referred to an IVA/PTD and is unable to keep up with the payments, it may be difficult to determine if the solution failed because the consumer received non-compliant advice or other factors.
- **Neither firms nor other regulators collect data** which tracks the outcome of individuals referred from debt packagers. Additionally, we found that some firms

appear to have manipulated consumers' income and expenditure information to meet the criteria for an IVA or PTD. Therefore, we would be unable to determine if the referral was suitable for the customer just by looking at the information recorded by debt packagers.

2.19 As a result, there are limited reliable quantitative evidence sources on eventual customer outcomes. It is not possible, for example, to rely on complaints data, because customers themselves are not able to reliably identify whether the advice they received was non-compliant or biased towards one solution over another owing to their vulnerable circumstances when seeking debt advice, and issues with behavioural biases (discussed further in the Cost Benefit Analysis).

2.20 As with our MFW data, our recent evidence (described below and in the Cost Benefit Analysis in more detail) also showed many instances of advice from debt packager firms not taking account of customers' best interests. For example, we found evidence of:

- manipulation of customers' finances to satisfy the IVA/PTD eligibility criteria
- biased presentation of information
- a lack of explanation of risks
- inaccurate representation of conversations with customers

2.21 Nevertheless, quantifying whether the specific cases of non-compliant advice we identified through our work lead to IVA/PTD failures would take several years, depending on when the IVAs/PTDs are terminated. In any event, knowing the total number of IVA/PTD failures would not give the full picture on whether firms had complied with our rules. We consider that the risk of harm to consumers is too significant to wait to see whether and how these effects play out, and we do not consider it appropriate to delay our intervention for this purpose. Indeed, we consider it imperative to prevent the risk of further harm arising from non-compliant advice in the debt packager market.

Evidence Base

2.22 Regarding feedback point (b) in paragraph 2.17, we have used the time since our first consultation to further expand our evidence base of debt packager firms we have assessed. We collected more evidence on conduct by reviewing files from smaller firm types, which had been underrepresented in the MFW.

2.23 To make sure we had a clear view of the different types of firms in the debt packager market, we categorised firms across the market based on factors that in our view may affect the management of the conflict of interest. These factors were:

- size (by share of customers, as suggested by respondent feedback)
- whether the firm uses Appointed Representatives (ARs) or not
- whether the firm had mixed sources of revenue or was primarily funded by referral fees

2.24 Based on these factors, we divided debt packager firms into 5 groups. We considered that the evidence could be strengthened in 3 categories which represent firms that are not large (ie those with 10% or less market share): small firms which do not have ARs (**small solo**), small firms which do have them (**small principal**), and firms where less than 70% of revenue comes from referral fees (**mixed revenue**).

2.25 We randomly selected 7 firms for review across these 3 categories. We sampled case files from firms in 2 of the 3 categories we intended to sample (small solo and small principal).

2.26 The remaining category, mixed revenue, yielded only one firm in the 2019 – 2020 date range we were targeting which was still active (2 others had cancelled their permissions since 2019/20). We see this firm as an outlier and note it has subsequently left the market. While this firm did not have available customer interactions to review, it referred very high numbers of customers to the highest paying solutions. We still propose to capture this business model under the ban on the basis that it will prevent the risk of conflict of interest in mixed revenue firm entrants (we explain our considerations on scope later in this chapter).

2.27 Case files from small principal and small solo firms (which dated to between 2021 and 2022) were used to supplement our existing evidence. We set out further detail on how we undertook these reviews and the statistical approach we followed in our Cost Benefit Analysis.

2.28 Of the 38 files we were able to review, we found what appear to be high levels of non-compliance across the firms in our sampled categories. We found evidence of:

- manipulation of I&E figures, which in turn altered customers' disposable income figures
- firms promoting IVAs by downplaying the negatives of this option when compared with other solutions
- in some cases, we found that I&E assessments relied on such little information that it was impossible for the FCA to determine what the customer's disposable income was, yet these customers were recommended solutions which generated a fee for the debt packager firm, often an IVA
- in one case the firm did not calculate disposable income, however recommended an IVA

2.29 With the input of an external statistician, we determined a percentage of non-compliance that if a sampled firm exceeds, we can conclude with a high degree of statistical certainty that the sampled firm is not adequately managing the conflict of interest. All firms exceeded this percentage threshold which leads us to conclude that all the firms were failing to adequately manage the conflict of interest.

2.30 We consider that evidence of non-compliance indicates that the conflict of interest is not being adequately managed and leading to the risk of harm we have identified. We acknowledge there may be other causes of non-compliance, however, we have considered the reasons for these (see paragraph 31 of the CBA below) and remain confident in our proposals.

2.31 We were only able to sample files from firms that had retained call recordings, thus the sample may be biased towards firms with good record management procedures which is likely correlated with comparatively stronger governance and processes in other areas.

We therefore consider that the results are likely to be biased towards firms that are more likely to be compliant than the typical firm in the market and so our findings are likely to be an understatement of the true extent of non-compliance.

2.32 Moreover, because our samples were representative of the categories set out earlier, we can conclude that the failure is not specific to the sampled firms, but likely a consequence of all the firms' business models in these categories. Combined with the MFW evidence and other case work, this additional evidence leads us to conclude this failure is common to the whole market.

2.33 We explain our new evidence and the statistical method we employed in more detail in our Cost Benefit Analysis. Please refer to that section for further information.

Q1: Do you have any comments on our consolidated evidence base (including as it is detailed in the CBA)?

Changes in the debt packager market since 2020

2.34 In reviewing additional evidence, we were aware that there may have been changes in the debt packager market since our original evidence was gathered for CP21/30 that might affect the need for our intervention. There is a possibility our consultation in 2021, or other industry-wide impacts over the last year may have triggered changes in how debt packagers operate. In addition, as explained above, following our MFW, 5 debt packager firms applied for voluntary requirements to be imposed meaning they are no longer providing regulated advice services.

2.35 We therefore wanted to assess whether the firms involved in our latest evidence gathering had changed their business models. So, as well as reviewing a sample of their case files, we asked the firms whether there had been any changes in their (or their ARs') business models, policies or procedures since October 2020 that had significantly affected their provision of debt advice or referrals to debt solution providers.

2.36 We did not receive any response that demonstrated a clear and significant change in operations that we considered would lead to the conflict of interest being managed appropriately. Moreover, we found concerns with files across all the firms we reviewed (which dated to between 2021 and 2022).

How it links to our objectives

2.37 We are proposing the new rules and guidance set out in this CP in order to secure the appropriate degree of protection for consumers.

Wider effects of this consultation

2.38 Our proposals would end the current debt packager model based on referral remuneration. Firms which currently employ the debt packager model may choose to change their business model or leave the debt advice market.

2.39 As we acknowledged in CP21/30, this would lead to a loss of advice capacity. We previously estimated that around 52,000 of the 1.7 million people who seek debt advice every year start their journey with a debt packager. Although the number of debt packagers has reduced since our original evidence gathering in 2019/20, the number of people seeking debt advice is likely to have risen due to recent increases in the cost of living. We cannot accurately estimate how the number of consumers interacting with debt packagers has changed, however we expect it to be in the same order of magnitude as our estimate for 2019/20.

2.40 We think that the risk of substantial harm from debt packager advice affected by the conflict of interest outweighs its value in providing advice capacity. We explained in CP21/30 that we accept that packager marketing may engage consumers in debt advice who otherwise would not seek or receive it at all. We also accept that some referrals produce good consumer outcomes, particularly those to non-revenue-generating endpoints like debt relief orders or NFP debt advice. Nevertheless, if debt packagers refer customers to NFP debt advice, we consider that the debt packager firm has not added significant value to consumers.

2.41 We acknowledge there may be some loss of benefit to consumers who would not otherwise have sought debt advice but respond to debt packager advertising and subsequently progress with a referral to the NFP debt advice sector or end up with a suitable solution. However, consumers not seeking debt advice is already a recognised risk and part of a wider problem of enabling consumers to engage with their finances, especially where they are experiencing financial difficulties.

2.42 A number of measures are in progress to address this, including the Money and Pensions Service's (MaPS) strategy to increase pro-active engagement with customers and our own work with creditors to make efficient and effective referrals to debt advice. Additionally, we consider it likely that a high proportion of referral fees to debt packagers result from poor advice. Since we do not consider lost revenue that was earned through non-compliant activities as a cost, the (legitimate) losses for the firms of the intervention may be small (see Cost Benefit Analysis).

Q2: **Do you think there have been any developments (since 2020, and since our consultation in 2021) which have materially changed the management of the conflict of interest? If so, can you provide evidence of these developments?**

Q3: Do you think there are any developments in the market which have changed the factors informing our decision as to the right intervention to tackle the harm or risk of harm we have seen? If so, can you provide evidence of these developments?

Scope

Debt management and NFP firms

2.43 In CP21/30 we considered whether the proposed ban should extend to debt management firms or NFP firms. As set out in paragraphs 3.7 – 3.10 of that document, we consider that the business models of such firms are very different to debt packagers, and the conflict of interest is not as acute. We are proposing not to apply the ban to NFPs or debt management firms. The majority of respondents agreed with this assessment in respect of NFPs, though the feedback was more finely balanced regarding the proposal to not extend the ban to debt management firms. Nevertheless, half of respondents agreed with our proposed approach.

2.44 Some respondents who supported the ban but disagreed with the proposal to exclude debt management firms from it suggested that debt management firms should be included to help provide clarity and consistency for firms and consumers. They also thought it could help to prevent firms trying to avoid the ban.

2.45 Having considered this feedback carefully, we do not propose changing the scope of the proposed ban to include debt management firms or NFPs. As we have set out, we are intervening in the debt packager business model because there is a strong and inherent conflict of interest in the business model itself, and we think it is not being adequately managed in practice. We currently see the risk of referral fees leading to non-compliant advice as being low for both NFP firms and debt management firms for the reasons we set out in CP21/30.

2.46 We also do not think that excluding debt management firms from the scope would lead to gaming. This is because debt packagers would need to seek additional permissions from us in order to become debt management firms, and we would monitor any such applications carefully. Additionally, we aim to prevent further gaming by tightening requirements on principal firms with regard to their responsibilities over any appointed representatives they have. As explained in CP21/30, we are proposing to introduce these rules to address the concern that existing debt packagers, or firms wishing to operate under the current debt packager business model, could become appointed representatives of a debt management firm and not be subject to the ban. We are confident that firms can understand the application of the proposed rules and guidance.

2.47 We agree with respondents who said that if the rules are made, firm behaviour needs to be monitored. We will continue to scrutinise planned income streams as part of our consideration of any applications for authorisation as a debt counselling firm. We will monitor firm notifications and received intelligence about debt advice firms. We will also continue to engage with the Insolvency Service (IS) to understand any changes in how IVA/PTD providers source their leads.

Mixed Revenue firms

2.48 As explained earlier in this chapter, we divided debt packager firms into 5 groups and sought to enhance our evidence base in 3 of these categories (small solo, small principal and mixed revenue). We found what appear to be high levels of non-compliance across all the sampled firms in the small solo and small principal categories, indicating that the conflict of interest is not being adequately managed.

2.49 We were not able to review customer interactions from mixed revenue firms for the reasons described earlier in this chapter and in the CBA, however, we still consider that the proposed ban should apply to all debt packager firms. Our primary concern is that the conflict of interest we have identified is not being adequately managed by debt packagers. We consider that, unlike NFP or debt management firms – who operate different business models – referral fees paid to debt packagers, including mixed revenue firms, are likely to always be a driver of harm.

2.50 NFPs cannot retain any revenue in excess of their costs as profit, so the incentive to maximise revenue and profit does not apply to them in the same way it does for debt packagers. With respect to debt management firms, we found that referral fees made up on average only 1% of their revenues. For the 3 mixed revenue firms, meanwhile, referral fee revenue made up all, or a significant majority of their revenue from debt related activities. Also, debt management firms forgo revenue they might have earned from administering a debt solution when they make a referral to another debt solution provider. This is not true for debt packagers, who do not typically provide solutions. All debt packager firms are therefore still subject to an inherent conflict of interest arising from available referral fees.

2.51 Further, we want to prevent debt packagers from being able to avoid our proposed rules by adapting their business models in minor ways so as to be out of scope. We are therefore maintaining the scope of the proposed ban to cover all debt packagers, including mixed revenue firms, but to exclude NFP and debt management firms.

Alternative proposals considered

2.52 We have revisited the alternatives we originally considered in advance of CP21/30 and addressed in that document (3.11-3.19). Taking into account the feedback we received (summarised in Chapter 4), we considered afresh whether the balance of the argument in respect of these alternatives has changed substantially in light of changing macroeconomic conditions, and the fact that 5 large debt packagers have either left the market or are subject to voluntary requirements to cease business. We have also considered the alternative measures suggested by consultation respondents. A full summary is included in the Feedback Statement in Chapter 4.

2.53 We acknowledge that recent increases in the cost of living mean that the demand for good-quality debt advice will be higher than when we published CP21/30. Nevertheless, we remain confident that the supply of debt advice could absorb the numbers of customers who would have been seen by debt packagers (in the event that all debt packager firms left the market). Moreover, it is critical that consumers seeking debt advice, who are often in vulnerable circumstances, get advice that is appropriate and which does not cause them harm.

Supervision

2.54 A minority of respondents felt that we should use our supervisory tools instead of implementing an outright ban. However, we consider that high supervisory focus would not be an efficient use of limited resources given the scale of the non-compliance despite repeated supervisory warnings. Indeed, for every debt packager firm for which we have undertaken case file reviews, we have found evidence of apparent overall non-compliance. This indicates that the conflict of interest is so acute in the majority of cases, that it has no reasonable chance of being managed across the market, even with extensive supervisory work.

2.55 We have to prioritise our resources and carrying out significant further supervisory work on debt packagers, who are only a small part of the sector, would mean diverting resources away from other parts of the debt advice landscape. We do not consider this to be a proportionate, efficient or economic use of our resources (to which the FCA must have regard under FSMA section 3B(1)(a)) in order to meet our objectives.

2.56 Based on the feedback we received, and our additional evidence, we remain of the view that the strong conflict of interest which is a consequence of the debt packager business model will always be a driver of non-compliance with our rules. If the only way to ensure that firms are complying is to monitor them very closely on an ongoing basis then it is reasonable to ask if the firms should be operating under such a business model in the first place and whether consumers would be better served by other firms in the market operating under different business models. Additionally, we do not simply want to tackle the harm of poor advice after it has crystallised, but also prevent models at the gateway that pose an undue risk of consumer harm.

Fixed, single referral fee for all solutions

2.57 We agree with feedback that fixed fees for all solutions have the potential to remove bias towards higher fee solutions. However, as the respondent who suggested this approach acknowledged, this would require fundamental reform of the provision of debt advice and support from all stakeholders, including government and other regulators, and significant resources to enact. It is not within the FCA's powers to do this alone. It is unlikely this could be arranged within a reasonable timescale, leaving consumers' risk of harm unaddressed.

2.58 We also see it as an inefficient method of tackling FCA-authorised firms' non-compliance with existing rules. Further, it does not remove the conflict between referring to a solution and offering the consumer a way to manage their debt without accepting a formal debt solution. Additionally, placing a requirement on debt solution providers to pay a specific fee, even where they do not receive any income from setting the customer up on a solution, would be a significant change for the market. As highlighted by the respondent, this could lead to significant unintended consequences. For example, it may result in all consumers being charged the same flat fee regardless of which debt solution is provided and this could act as a barrier to consumers seeking advice.

Price cap

2.59 A price cap would have the potential to weaken the conflict of interest, in particular by reducing product bias (since fees paid in respect of IVAs and DMPs would become closer). However, sales bias (the incentive to refer to solutions that pay fees over those that do not) would remain. No responses, other than the suggestion of fixed fees for all solutions, suggested how this could be overcome. Therefore, it would not achieve our objective of removing the conflict of interest and the associated risk of harm to consumers. Additionally, as with the alternative above, the coordination and resources required to implement this fundamental change would be disproportionate.

Advisors required to have qualifications

2.60 We do not think qualifications would address our concerns in the debt packager model as they would neither remove the strong and inherent conflict of interest, nor give sufficient assurance that advisers would be able to adequately manage it.

2.61 Additionally, we do not think that requiring advisors to have qualifications would be a proportionate response since it is not a sufficiently targeted response to the issues at hand. It would also have a significant cost implication for the majority of debt advice firms, most of which are NFP organisations.

Widening the insolvency practitioner exclusion

2.62 Some respondents suggested the government should widen the exclusion applying to insolvency practitioners. The existing exclusion allows them to carry on debt counselling without FCA authorisation only if they are 'in reasonable contemplation' of being appointed as the insolvency practitioner for the customer. The rationale for the suggested expansion of the exclusion is that there would be less of a need for debt packagers to give regulated debt advice to customers. We do not think this would address the risk of harm. In effect, it would move the problem to the insolvency practitioner (and outside of our regulatory remit) and we would need much greater assurance regarding their ability to manage conflicts of interest to consider this proposal further.

Equality and diversity considerations

2.63 We considered the equality and diversity issues that may arise from the proposals in CP21/30 (pp. 2.37-2.40).

2.64 We have reassessed these issues and think the considerations remain unchanged. Research from our Financial Lives Surveys indicated that usage of debt advice services between February 2019 and October 2020 was significantly higher amongst men than women and among younger age groups (18-34) than older age groups (55+). The research also found that people from minority ethnic groups were much more likely to have received debt advice than people from white backgrounds. We are aware that people with long term physical and mental health conditions are more likely to suffer financial difficulties than those without.

2.65 We consider that the proposals set out in this consultation paper, including the proposed perimeter guidance, would improve outcomes for people seeking debt advice and so do not consider that they would negatively impact on people with protected characteristics. We set this out in CP21/30 and did not receive any feedback.

2.66 We will revisit the equality and diversity implications if we proceed to making final rules.

2.67 We welcome your input to this consultation on the equality and diversity considerations in relation to our proposals.

Chapter 3

Our updated proposals and implementation period

Proposed rules on debt packagers

3.1 CP21/30 set out our in-depth explanation of the proposed ban on debt packagers receiving referral fees from debt solution providers. Please refer to chapter 3 of that document for further information.

3.2 Our enhanced evidence base and the strongly supportive feedback we received to the consultation reinforces our view that the intervention is appropriate to address this harm to consumers.

3.3 In response to feedback on our draft rules (explained in more detail in Chapter 4), we have made minor clarificatory changes to new Annex A of the draft instrument (which deals with additions to the Consumer Credit sourcebook):

- a new provision CONC 8.3.10G(4), to further explain the purpose of the anti-avoidance provisions and the reference to an "insignificant amount of total annual revenue"
- an amendment to CONC 8.3.11R(2), to clarify that the proposed ban on referral fees does not apply where a debt packager's contractual right to payment has accrued at the time of any rules coming into force
- a clarification to CONC 8.3.14R(3) to ensure that the carve-out for officers of the UK's insolvency services only applies where such person is employed in that capacity

3.4 We have also included a reference to the new Principle 12 (consumer duty) which requires firms to act to deliver good outcomes for retail customers. For new and existing products or services that are open to sale or renewal, this comes into force on 31 July 2023. For closed products or services, the rules come into force on 31 July 2024.

New perimeter guidance

3.5 The feedback to CP21/30 suggested that we could be clearer about how the perimeter applies to lead generators. Our proposed perimeter guidance makes clear that to pass consumers to a solution provider who only offers one solution could constitute the regulated activity of debt counselling, depending on the circumstances of the individual case.

3.6 Conducting debt counselling without authorisation exposes consumers to a risk of harm from being referred to solutions that are not appropriate for them. Our proposed guidance would make it clearer to firms and other stakeholders that making such referrals or recommendations may require FCA authorisation. It is our view that this would raise standards in lead generation, and cause lead generators who provide a poor service to consumers to exit the market.

Q4: Do you have any further comments on our amended proposals and the draft Handbook text in Appendix 1 including the new PERG guidance?

Implementation period

3.7 In CP21/30 we suggested a one-month implementation period, after which firms would have to comply with our new rules. We consulted on this short period on the basis that, should the rules be made, a swift implementation would be desirable to protect consumers. This has to be balanced against the impact on firms. Some industry respondents said that it would not give firms enough time to adapt their business models, while others agreed it was appropriate given the risk of harm. Of the 25 respondents who replied to this question, 19 supported a 1-month period. Additionally, 2 respondents supported the idea of swift action, but did not explicitly support a 1-month implementation period. Several responses noted that a period of 1 month was very quick but felt that this was mitigated by the fact that we have been warning the sector of our concerns for several years.

3.8 Four responses challenged the implementation period. One (from a compliance consultant) felt that it would not give debt packagers enough time to change their business models. Another (from an IVA provider) noted the IS' review of personal insolvency and suggested aligning the timetable with that. Another (from an insolvency provider) felt that it was too short a period for such a fundamental change but did not offer a suggestion for what would be sufficient. Firms also stated that if they wanted to apply for new permissions, they would not receive those in that period. One debt packager stated it did not think the proposal should go ahead at all.

3.9 We are aware that over a year has passed since the previous consultation and a longer period will prolong consumers' exposure to risk. Nevertheless, we do not wish to see firms that provide useful services for customers leave the market. We therefore propose an implementation period of 2 months, and are seeking feedback as to whether this would provide firms sufficient time they need to adapt their business models to the new rules.

Q5: Do you agree with the proposed implementation period of 2 months?

Q6: If you do not agree with the proposed implementation period, what alternative implementation period would you recommend? Please provide evidence for the length of implementation period you believe is required.

Chapter 4

Summary of feedback to CP21/30 and our response

4.1 In CP21/30 we consulted on new rules and guidance around remuneration for debt packagers. In this chapter we present the feedback we received to the questions we asked in that CP and our responses.

4.2 We received 45 responses to CP21/30. These included responses from:

- debt packagers
- other advice providers (including large firms and individual debt advisors)
- consumer bodies
- trade bodies representing lenders, advice providers and debt management firms
- recognised professional bodies
- others including credit unions, insolvency advisors, government bodies and members of the public

Ban on remuneration from debt solution providers

4.3 The primary proposal in CP21/30 was a ban on debt packagers receiving referral fees or any other form of commission or remuneration from a debt solution provider in relation to providing referrals or other related services. We proposed the ban as we were of the view that the remuneration model for debt packagers is driving an unacceptable level of risk of consumer harm.

4.4 We asked respondents the following question:

> **Q1: Do you agree with our assessment that the remuneration model for debt packager firms is driving consumer harm?**

4.5 Overall, there was strong agreement (34 respondents agreed) with our assessment set out in CP21/30 that the remuneration model of debt packager creates an acute conflict of interest which creates a significant risk of consumer harm. These responses agreed that there was a need for the conflict of interest to be mitigated and some felt that intervention by the FCA was overdue.

4.6 Several debt advisors cited personal experience of dealing with customers who had been placed on unsuitable IVA/PTDs where other solutions such as Debt Relief Orders would have been more appropriate. One such response highlighted that this had led to clients ending up with more debt and an adverse impact on their mental health.

4.7 Lenders, trade bodies and all but one Recognised Professional Body (RPB) agreed that the debt packager business model drives consumer harm.

4.8 One RPB agreed with the logic of the argument but felt it was difficult to quantify the actual level of consumer harm from unsuitable solutions. This point was also raised by some respondents who disagreed with our assessment. These responses pointed to our descriptions of how consumers can be harmed by unsuitable IVA/PTDs (paragraph 2.8 of CP21/30) but highlighted that we had not provided quantitative evidence of the number of consumers being harmed or the level of detriment.

4.9 One respondent felt that there were also problems with individual remuneration, as well as the overall business model.

4.10 Several respondents said that in addition to agreeing that debt packagers were part of the problem, there were issues elsewhere in the consumer journey. This included concerns around whether insolvency practitioners are meeting their own regulatory standards and the role played by 'unregulated lead generators'.

4.11 Five respondents disagreed with our assessment that the debt packager remuneration model is driving consumer harm.

4.12 Responses from debt packagers argued that their businesses added value to customers and that the large number of referrals to IVA/PTDs was due to them marketing to customers where it was likely that an IVA/PTD would be a suitable option. Some said that the value of their service was that they were specialists in IVA/PTDs and could help direct customers to particular insolvency practitioners who would best serve the needs of the customer.

4.13 One respondent was concerned that the evidence from the recent supervisory work was potentially limited to a small number of large firms, and that smaller firms were compliant with the rules.

4.14 Similarly, of the respondents who neither agreed or disagreed, some appeared to agree that there were problems with the sector driven by the conflict of interest in the business model, but that not all debt packagers were providing non-compliant advice and some could manage the conflict.

4.15 One respondent agreed that the business model was driving harm but didn't think that there was harm where packagers referred customers to FCA regulated debt solution providers. The respondent asked for more clarity on why the ban applied to all payments by debt solution providers and not just those who provide a limited range of solutions.

Our response:

Evidence base

We note that most respondents (34 out of 45) agreed with our assessment that the remuneration model of debt packagers drives consumer harm and that some respondents from the debt advice sector offered examples from their personal experience which aligned with our findings. In many cases the support was strong, highlighting that the evidence set out in CP21/30 clearly showed there was a problem with the debt packager business model which needs to be addressed.

Moreover, as explained in Chapter 2, we have gathered additional evidence from smaller types of firms to further strengthen our evidence base. The results, as detailed in Chapter 2 and our Cost Benefit Analysis, support our previous findings.

Evidence of consumer harm
We address this feedback in Chapter 2.

Concern with remuneration from all debt solution providers
While we focused much of our analysis in CP21/30 on referrals to IVA/PTDs, we note that we also had concerns with the quality of referrals to DMP providers. We found that in many cases it was not clear why the recommendation was being made and found that in a number of cases where a customer was referred to a DMP provider the customer was not accepted on to a DMP. We are also concerned that this is a poor consumer journey, with consumers (who are likely to be in vulnerable circumstances) being passed between multiple firms. We were concerned that if fees are allowed for some solutions and not others that firms would remain incentivised to make recommendations for those fee-paying solutions, without regard to the best interests of the customer. We therefore proposed for the ban to apply to all referral fees, even from FCA regulated debt solution providers. We remain of the view that this is appropriate.

Issues along the consumer journey
While we agree with respondents who highlighted that there are concerns along the whole debt advice consumer journey and not only with debt packagers, this in no way removes, or reduces the requirement of debt advice providers regulated by us to comply with our rules. We discuss the impact on the wider market later in this chapter.

4.16 In Chapter 3 of CP21/30, we set out some alternatives to a ban on all referral fees. These included:

- introducing higher quality standards for debt advice
- providing consumers with more information about fees and commission
- other interventions around remuneration, including capping referral fees or requiring all fees to be set at the same level regardless of solution

4.17 The CP set out our reasoning for why we did not think these measures would be effective. We asked the following question:

Q2: Do you agree that the only effective remedy is to ban receipt of remuneration for referrals by debt packager firms?

4.18 Of the 41 respondents who gave feedback to this question, 27 supported the ban on referral fees. These responses tended to agree with the assessment set out in CP21/30 that alternative options were unlikely to be effective.

4.19 Some who agreed said that they would ideally like to see non-compliance dealt with through supervision and enforcement tools but acknowledged that operationally this may not be practical.

4.20 One response from a consumer body wanted to see more supervision of all debt advice providers, alongside the referral fee ban.

4.21 The respondents who disagreed with an outright ban differed in what action they thought would be appropriate.

4.22 Five respondents favoured a cap on referral fees. One stated that all fees should be made the same regardless of the debt solution (including solutions which currently don't generate a referral fee such as Debt Relief Orders, DROs). The response noted that if firms are required to pay a referral fee on receiving a referral for a customer recommended a DRO then this may lead to firms not accepting these referrals.

4.23 Separately, another respondent raised the idea of all fees being the same but said they didn't think this was viable and would be complicated to implement.

4.24 Six respondents felt that as the issue is non-compliance with existing rules, that we should use supervisory tools to monitor firms more strictly. One response, from a debt packager said that the FCA should always consider putting in place higher standards (as considered as an alternative in CP21/30) before banning business models. One respondent, a debt packager, recommended a review of CONC 8 rules to incorporate debt advice from debt packagers more fully.

4.25 One respondent, a debt packager, suggested the FCA establish a working group of debt packagers to provide key metrics. They suggested assessing referral trends over time, causes and numbers of failures of solutions, and complaints data.

4.26 Several respondents highlighted the importance of working closely with bodies such as the Insolvency Service to tackle issues which cut across our perimeter. One respondent, a debt packager, suggested an assessment of insolvency practitioners.

4.27 One respondent, an individual, suggested that we should introduce a requirement for debt advisors to be qualified and that the FCA should supervise the quality of advice.

Our response:

Capping referral fees
In CP21/30 we set out our assessment of alternatives for a ban on referral fees, and we revisit this above in Chapter 2.

Higher standards
We set out in CP21/30 that we did not think that creating new rules which set out further standards for how debt advice, including by debt packagers, should be conducted would be effective. This is because additional standards would not alter the strong conflict of interest which is a consequence of the debt packager business model, as it is apparent lack of compliance with the existing standards that is leading to a risk of

harm. Since our concern is that the conflict is likely to lead to firms not complying with existing rules, we do not think it reasonable to assume that they would comply with any additional rules. No evidence has been offered against this view and so we remain unconvinced by this option.

Heightened supervision
We agree that if firms were to meet our existing rules, then this would address the concerns which we have with debt packagers. However, we don't agree that this means that more supervision is a suitable option.

As explained in Chapter 2, we have already prioritised the supervision of debt packager firms and have actively engaged with firms through supervision to try to address our concerns. Despite this, we continue to see evidence which suggests there are serious problems with this sector's ability to meet our rules, including in our most recent evidence. Additionally, we do not simply want to tackle the harm of poor advice after it has crystallised, but also prevent models at the gateway that pose an undue risk of consumer harm.

We agree with the respondents who highlighted the importance of us working closely with partners including the Insolvency Service. This is something which we are already undertaking, including through this work. We note their work on the personal insolvency review, and also that the Regulated Activities Order exclusion and perimeter are both set by Parliament.

Debt Packager Working Group
We do not agree that forming a working group of debt packagers would be a proportionate or appropriate response to the evidence of failings we have identified through our evidence gathering. Additionally, such a group would not reflect views from the whole of the debt advice landscape. Instead, we have now issued 2 public consultations to seek views from a broad range of participants, including debt packagers, and we have conducted additional data gathering to ensure we have evidence from a greater variety of debt packager firms. Moreover, as with our response on greater supervision, we do not consider this to be an efficient use of FCA resources.

In respect of the suggestion to gather additional data, we have done so as described in more detail in Chapter 2 and the CBA, and are mindful of the need for efficient use of FCA resource beyond this.

Qualifications
We provide more detail to our response on this alternative in Chapter 2.

Scope

4.28 In CP21/30 we proposed that the ban should not apply to all debt advice providers. Specifically, we proposed for it to not apply to NFP firms and debt management firms.

4.29 We asked the following question:

> **Q3: Do you agree that we should not include debt management firms or not-for-profit debt advice firms in our proposals?**

4.30 **Not-for-profit providers**. The majority of respondents agreed with this on the basis that generally NFPs have fundamentally different business models. Some of those who agreed, however, thought that this should be monitored to ensure that the issues we have seen in the commercial debt packager model did not emerge in the NFP sector.

4.31 However, some respondents (a mix of types) disagreed and thought that the rules should include NFPs. There were 3 primary reasons stated for this:

- firstly, having a blanket ban provided more clarity
- secondly, some respondents felt that the misaligned incentives could emerge in NFPs as they have done in the commercial sector, and felt there was anecdotal evidence of institutional bias in some NFPs to specific solutions driven by the FairShare funding model
- thirdly, not including NFPs in the scope might create a loophole for packagers to set up a structure that includes NFPs and continue to cause harm

4.32 **Debt management firms**. The responses to our proposal to not extend the ban to debt management firms were more finely balanced. Of the 28 responses, 14 supported our proposed approach agreeing with our assessment in CP21/30 that the difference in business models between debt packagers and debt management firms means that debt management firms are much more likely to be able to manage any conflict of interest arising from receiving remunerations from debt solution providers, because our rules (CONC 8.7.2(R)) prevent firms 'front loading' fees, so the DMP provider is incentivised to set up DMPs that are appropriate to the customer's individual circumstances and sustainable in the longer term. Several respondents said that while they supported not including these firms in the ban, the situation should be monitored to see if debt management firms alter their business models in a way that creates similar risks as the debt packager model.

4.33 There were 10 responses which disagreed with the proposal, while agreeing that there should be a ban. These respondents tended to suggest that these firms should be included to provide clarity, consistency, and to ensure firms do not try to game the rules. On the latter point, some respondents noted that current business models of DMP firms could change.

4.34 Several responses supported a blanket ban across all debt advice providers (including NFP).

4.35 The remaining responses highlighted that the position was finely balanced, or it was unclear what outcome they supported.

Our response:

Not-for-profit providers

Our review of the scope is addressed in Chapter 2.

Some respondents felt the ban should be widely applied to remove any conflict of interest or to provide clarity. As stated above, we are proposing to intervene in the debt packager business model because there is a strong and inherent conflict of interest in the business model itself, and we think it is not being managed in practice. We found that debt packagers generate almost all their revenue from referral fees, whereas NFPs rely on a range of funding sources (eg from the Money and Pensions Service, local government and charitable donations).

We currently see the risk of referral fees leading to non-compliant advice as being low for NFP firms and so are maintaining the proposed scope to not include NFP providers. However, we agree that this needs to be monitored and we would scrutinise any applications made by prospective NFP providers to understand their planned income streams. We will also continue to engage with the IS to understand any changes in where IVA/PTD providers are sourcing their leads.

Debt management firms

As set out in CP21/30 and Chapter 2, debt management firms have a different business model to debt packagers and do not rely on revenue from referral fees. We found that debt management firms make around 1% of their revenue from referral fees whereas the equivalent figure for debt packagers is around 90%. We note that many respondents agreed that the business model was different and largely agreed that this meant that there wasn't the same conflict of interest around referral fees as for debt packager firms.

We agree with respondents that business models could change over time and this could alter the level of risk to consumers. In CP21/30 we highlighted that we would look to monitor this.

We do not think that it would be proportionate to extend the proposed ban to debt management firms (or all debt advice firms) to offer clarity. While we acknowledge that some respondents would prefer to see such rules apply to all advice providers to remove the conflict of interest entirely or think that all firms should be subject to the same rules, the evidence we have suggests that there is a different level of risk presented by referral fees. Firms which rely on referral fees to be sustainable have a strong and inherent conflict of interest. Whereas firms that are not reliant on referral fees do not have this. On this basis we do not agree that the ban would have to apply equally to all debt advice firms. We therefore continue to propose not to include debt management firms in the ban, but we will monitor the situation in the market.

Several stakeholders highlighted that we could be clearer about how the perimeter applies to lead generators. We agree and propose to insert additional guidance into PERG, as outlined in Chapter 3.

4.36 In not applying the ban to debt management firms, we were concerned that this could create a loophole. Existing debt packagers, or firms wishing to operate under the current debt packager business model, could become appointed representatives of a debt management firm and not be subject to the ban. We propose that principal firms should have an obligation to ensure that this did not occur.

Q4: Do you have any comments on our proposed obligation on debt management firms who act as principals?

4.37 We received 20 responses to this question. Respondents tended to agree with the proposals.

4.38 Some respondents restated their view that the scope should include debt management firms (and therefore the obligation would not be necessary). One of these respondents stated that if debt management firms are out of scope, then the proposed obligation would be needed.

4.39 Some respondents raised concerns with the AR regime and were concerned that either principals would not do their due diligence, or that ARs would be difficult to monitor in practice, and the FCA wouldn't have the resources to supervise this effectively.

4.40 A small number of respondents suggested the AR model was not fit for purpose for the sector in general and should be removed.

Our response:

As set out above, we do not propose applying the ban to debt management firms. We therefore continue to see a need to address the risk of the debt packager business model simply being moved to ARs of debt management firms and continue to believe our requirements for principals are appropriate.

Banning debt advice firms from having appointed representatives would be a significant change to the whole debt advice sector and we do not see this as a proportionate option to address the particular risk we have identified.

Additionally, we consulted on a package of measures to improve the AR regime in 2021 (CP 21/34) and reduce potential harm for consumers and markets. The new rules clarify and strengthen the responsibilities and expectations of principals and set new requirements on collection of additional information on ARs and strengthen reporting requirements. These new rules took effect on 8 December 2022.

Draft rules

4.41 We set out our draft rules as part of CP21/30 and invited comments. The rules set out the proposed ban and some technical points intended to ensure the scope of the ban didn't interfere with any statutory schemes such as the £10 payments made to advice providers for administering a DRO, or payments made under the Scottish Debt Arrangement Scheme.

4.42 There were also some provisions included to prevent avoidance of the ban through small changes in the business model which wouldn't fundamentally alter the inherent conflict of interest or risk of harm to consumers.

4.43 In particular, the draft rules set out that while the ban does not apply where firms provide debt solutions, it does apply if they only provide solutions on a "single or occasional basis" or if the firm "receives only an insignificant amount of its total annual revenue" from providing solutions.

4.44 We asked the following question:

> **Q5:** **Do you have any comments on the draft rules?**

4.45 We received 8 responses to this question.

4.46 One response from a consumer group (and debt advice provider) strongly supported the drafting of the rules and welcomed the anti-avoidance measures.

4.47 Three respondents felt that phrase "insignificant amount" was unclear and asked for more specific values to be given (eg, a percentage of revenue) or further guidance to be added.

4.48 One respondent, a trade body, stated that advice providers are used by debt solution providers to carry out annual reviews and other related services. The respondent felt there was a case for these firms being able to offer such services as part of a 'transparent supply chain'. The respondent was also concerned that the ban would interfere with the operation of the proposed Statutory Debt Repayment Plan.

4.49 One respondent, an advice provider, was concerned that the draft rules exclude payments made by certain 'officers' (eg, of the Insolvency Service) could mean that payments made by IPs were excluded as they are 'officers of the court'. This respondent also felt there was a case for allowing some payments to be made to advice providers for 'work done' and that we should consider excluding that from the proposed cap.

4.50 Two respondents said that they objected to the overall approach of having a ban.

Our response:

"Insignificant amount"

We appreciate that some stakeholders would prefer to have a more precise meaning of 'insignificant amount', we do not consider it appropriate to specify what percentage would quantify that phrase in

CONC 8.3.9R(2)(b), whilst still avoiding the ban being circumvented. Nevertheless, we do propose to include additional guidance setting out the purpose of the rule (anti-avoidance) so it is clear how it should be applied – that guidance is the addition of CONC 8.3.10G(4). This approach would enable the FCA to make case-by-case assessments, taking all relevant factors into account. We therefore propose to maintain CONC 8.3.9R(2) as drafted.

Payments for work done
We set out in CP21/30 our rationale for putting in place a broad ban on advice providers receiving any remuneration from debt solution providers in relation to customers who have been referred to the firm, rather than a narrow ban on just referral fees. Our concern was that payments for referrals could be restructured as payments for 'work done'. Indeed, some respondents highlighted that the fees paid by debt solution providers to debt packagers are not for referrals but payment for the advice offered to the customers. Regardless of how the payments are described, the conflict of interest remains the same and we think that allowing payments to be made for 'work done' would undermine the effectiveness of the proposed intervention.

Officers
One respondent was concerned that by exempting officers of insolvency agencies would also allow IPs to be excluded. An intended outcome of the rules is that debt packagers should **not** be able to accept remuneration from IPs. We think the draft rules accomplished this but have made a small change to this rule to make this clearer.

Statutory Debt Repayment Plan
While we do not mention the Statutory Debt Repayment Plan (SDRP) specifically in the rules, we proposed a general carve out for all payments which are made 'pursuant to a statutory provision'. Having reflected, we have amended this carve out to apply to payments made 'pursuant to an enactment'. We anticipate that this will mean that payments made in relation to SDRP would not be included in the ban. We will, of course, consider this again depending on the development of the Government's regulations for SDRP.

Implementation period

4.51 In CP21/30 we noted that the number of people in need of debt advice will increase in the coming months. We saw the intervention we proposed as being significant, in particular, for firms that wanted to change their business model rather than exit the market.

4.52 However, we still thought it appropriate to propose a one-month implementation period to ensure that the new rules come into effect as quickly as possible.

4.53 We asked the following question:

> **Q6: Do you have any comments on the planned implementation period?**

4.54 We address the feedback received and our new proposed implementation period in Chapter 3.

Impact on wider market

4.55 We are aware that in proposing the ban on referral fees it will likely lead to a change in the debt advice landscape, with debt packagers either leaving the market or changing their business models.

4.56 Several respondents set out views around the type of changes which could occur in practice and how this could impact other parts of the market. The key themes were that the changes would lead to:

- an increase in activity by unregulated lead generators
- more customers going directly to IPs
- increased pressure being placed on other advice providers

4.57 **Lead generators.** We received 9 responses which suggested that the proposals could lead to an increase in activity by 'unregulated lead generators', who may play a role in directing customers towards IVA/PTD providers but might look to do so in a way which does not include offering debt advice and therefore does not fall under our regulation.

4.58 Several respondents stated that customers cannot easily distinguish between firms which offer 'advised leads' (including debt packagers) and those offering 'unadvised leads'. There was concern that this would mean customers continued to be placed at risk of harm of being directed towards solutions which may not be suitable for them.

4.59 Several of these respondents felt that such lead generation should be a regulated activity. Others suggested that debt solution providers, including IPs, should only be able to accept leads from firms who are regulated to provide full debt advice. Some suggested that we should consider adding additional perimeter guidance to make it clearer where lead generators may be providing regulated debt advice.

4.60 **Insolvency Practitioners.** Some respondents suggested that IPs may look to fill any gap left by debt packagers. Three responses suggested that debt packagers may look to merge with IPs and operate under an exclusion from FCA regulation for providing debt advice which applies to IPs when they can reasonably contemplate that the consumer they are advising will appoint them as an insolvency practitioner. One respondent suggested that more customers will go directly to IPs without seeking regulated debt advice first.

4.61 Overall, 11 respondents raised concerns that IPs may be falling short of the standards expected of them. Many respondents felt there was a need for the FCA to work in partnership with the Insolvency Service as well as bodies such as the Advertising Standards Authority to consider issues across the whole consumer journey.

4.62 The responses from RPBs suggested that the exclusion should be widened to allow IPs to offer full debt advice. Other respondents, including some debt advice providers, suggested that IPs should provide advice only if FCA regulated, or that the exclusion should apply only where customers have previously received full debt advice.

4.63 **Impact on other advice providers.** We received 7 responses suggesting that the rules would lead to additional pressure being placed on other advice providers who may not have capacity to take up this additional demand.

4.64 One respondent felt that there was capacity but there would be longer waiting times for advice and suggested that we consider if creditor forbearance measures need to be adjusted to take into account longer waiting times.

Our response:

Lead generators and IPs

We acknowledged in CP21/30 that a potential consequence of the new rules could be an increase in activity outside of our perimeter and highlighted that we were working closely with the Insolvency Service and other partners to consider the whole consumer journey. This commitment was set out in an exchange of letters between Sheldon Mills, Executive Director of Consumers and Competition at the FCA, and Dean Beale, CEO of the Insolvency Service.

Several respondents highlighted that our approach to debt packagers needed to be part of a wider approach to improving standards. We note that the Insolvency Service has begun conducting a review of personal insolvency, including the role of debt advice within the consumer journey.

We appreciate the desire from some respondents that any changes to debt packagers be timed to coincide with any subsequent changes to the wider insolvency landscape, however, where we see harm we need to act and we do not see a case for delaying our proposals. We will continue to work with our partners to understand the impact of changes in the wider market and to collaborate to find ways to address consumer harm where we see it.

Perimeter Guidance

We note that several respondents highlighted that some lead generators may be straying into offering debt advice. Persons providing leads must consider carefully whether they are carrying out a regulated activity. We agree with respondents who suggested that some additional perimeter guidance could be useful in this regard. We address these points in our proposed new perimeter guidance (PERG) in Chapter 3.

Impact on other advice providers

In CP21/30 we acknowledged that a consequence of the proposed rules was that in future those customers who would have approached a debt packager would need to seek advice from other sources. We set out our assessment that the size of the debt packager market was small enough that we could be satisfied that there was sufficient capacity in the rest of the sector to provide advice to these customers. While many respondents highlighted the concern that there would be more pressure on advice providers, there was no additional evidence offered to suggest our assessment was incorrect. We also note that none of the advice providers who responded to CP21/30 disagreed with our assessment.

In response to the suggestion that we consider creditors' approach to forbearance, firms are already required to suspend the active pursuit of recovery of a debt from a customer for a reasonable period where the customer informs the firm that a debt counsellor or another person acting on the customer's behalf or the customer is developing a repayment plan.

Cost benefit analysis

4.65 In Annex 2 of CP21/30 ('the CBA'), we set out our analysis of the costs and benefits arising from the proposed rule changes. We asked:

> **Q7: Do you have any comments on, or relevant additional data for, our draft cost benefit analysis?**

4.66 We received 16 responses which offered a view on the CBA or provided additional views or evidence around the arguments contained in it. Several additional responses said they had 'no comments' on the CBA.

4.67 There were 5 responses which supported the CBA. A consumer body said it was "credible" and a think tank felt it was based on "thorough research and analysis". Three responses from individual debt advisors said that the points raised around the impact of customers entering inappropriate solutions accorded with their personal experience.

4.68 In addition, a trade body presented evidence that the level of disposable income for people being accepted onto IVAs had reduced from around £175 to under £100. Combined with the new criteria for DROs, the respondent highlighted that this increased the need for careful consideration of which solution would be most appropriate, although they did not think it was clear how many people this affected in practice.

4.69 Four respondents felt that the CP and CBA showed bias against IVAs or didn't highlight sufficiently that they could be a useful solution to some customers. Of these, some felt that the CBA was asserting that there were 'too many' people entering IVAs without providing a benchmark for how many people should be on IVAs.

4.70 Two respondents, an IVA provider and a debt collection agency, felt that the failure rates for IVAs quoted in the CBA did not accord with the rates they saw for their customers.

One of these respondents predicted our proposed intervention would lead to a decrease in IVA failures.

4.71 One respondent, a debt packager, stated that the level of complaints in the sector was low and that we should have considered this as part of our analysis.

4.72 There were some comments about the evidence base we had used to come to our conclusion that the debt packager business model presented an unacceptable level of risk of consumer harm. We explain how we have enhanced our evidence base in Chapter 2 and the CBA.

4.73 One respondent, a debt packager, questioned the assumptions that 90% of referral fee revenue received by all firms is generated by non-compliant advice.

4.74 One respondent, an insolvency firm, highlighted that our assumption that IVA fees could range from £1000-£2000 and be paid as a lump sum or over the first 5-months of the IVA was out of date with current practices which follow a fixed fee model of £3,650 and with repayments being made after 3 months.

4.75 One respondent, an RPB, thought the estimate of around 14,000 debt packager customers entering an IVA/PTD each year was too low. The RPB estimated that around 70% of customers entering an IVA/PTD had been through a debt packager. Another respondent felt that we should make more use of data available from RPBs.

4.76 Two respondents, an RPB and an insolvency firm, stated that the CBA didn't take into account that there would be increased costs for IPs as a result of the proposal as they would need to do more checks and information gathering in house. One respondent said that debt packagers would be more efficient at doing these checks (and therefore cheaper) than if done in house by an IP. Neither respondent gave an estimate for the likely increase in costs.

4.77 One respondent thought that the proposed obligation on Principal firms would lead to increased monitoring costs.

Our response:

As we have produced an updated CBA that takes account of the additional evidence collected in 2022, we refer readers to that CBA. However, we set out below our response to the relevant points raised about the original CBA.

Presentation of IVAs

We do not agree with the claim that we are biased against IVA/PTDs and note that we set out clearly in paragraph 2.2 of CP21/30 that "where suitable, they can help people in financial difficulties manage their debts". We continue to support that statement in this CP.

We set out in a number of places in CP21/30 and the CBA our findings about the number of customers being referred to IVA/PTDs by debt packagers and that, compared to the wider advice sector, these numbers are high. We note the point raised by some stakeholders that debt packagers may target their marketing towards consumers who may be more likely to be eligible for an IVA. However, when taken together with the financial incentive debt packagers have for making recommendations for IVA/PTDs and the reliance of the debt packager business model on these referrals, the higher rate of IVA/PTD recommendations raises questions of whether debt packagers are managing the conflict of interest between having regard to the best interests of their customers and the financial incentives of making a recommendation of an IVA/PTD referral. It is in this light that we are concerned that customers are being recommended IVAs which may not be suitable for them.

In regard to the statistics used around the failure rate of IVAs, we are aware that this will vary from provider to provider and some will have much lower rates than the average we have used in our CBA. We consider the Insolvency Service to be a reliable source for these statistics.

Complaints data
As further described in Chapter 2, we do not agree with the assertion that a low level of complaints implies that consumers are being treated fairly or being given good advice. Though it may be a signal that there is no customer dissatisfaction, in the case of debt advice there are many reasons why consumers may not complain, including a lack of knowledge on how to complain, not being aware that advice was non-compliant or being unclear which firm they had been dealing with (ie the debt packager firm or the debt solution provider). It also often takes time for the harm from a poor referral to materialise and assessing whether advice was appropriate requires the consumer to know how their outcomes would have differed under a different solution. As we set out in our CBA, there are significant information asymmetries in the debt advice market. We noted in paragraph 9 of the original CBA that with debt advice "consumers face considerable barriers in their capacity to assess the quality of the service provided". In such a situation, customers in this market may be unlikely to make a complaint, even if the solution they end up on turns out not to be effective.

We consider that the features of the debt packager business model and the evidence from our supervisory work are sufficient grounds for the proposed intervention.

Estimation of the loss of revenue from referral fees
Our estimation that 90% of referral fee revenue came from non-compliant advice was based on our reviews of the case files of a number of debt packagers. We have added to these reviews, gathering files from firms with a variety of business structures and a variety of sizes. Our estimate has decreased marginally to 86%. We explain how we came to this estimate and how it affects our costs and benefits in the new CBA. Over 10 years, we expect a discounted net present benefit of £80.3mn from our policy.

Estimate of customer volumes

As part of the work leading up to CP21/30, we surveyed debt packager firms to understand their business models. This included questions about their customer volumes. Our estimate of customer volumes was based on this data, which was received directly from debt packager firms. We consider this to be a reasonable source of evidence, however, we note than one respondent felt that the numbers were an underestimate. As we now estimate there were 33 debt packagers operating between April 2019 and March 2020, rather than 39, we suspect that our original estimate may have been a slight overestimate. We detail why our estimate of the number of debt packagers is lower in the "Changes to CBA figures" section below. We now estimate customer numbers to be 52,000 instead of 54,000. While we are confident about this revised estimate, as it is based on a survey of all 33 debt packager firms, we have considered what the effect would be if volumes were higher than we estimate. Higher customer numbers would not affect our assessment that the debt packager business model creates an unacceptable level of risk of consumer harm. Higher volumes would mean more customers would be at risk of harm. We therefore see that this would strengthen our case for intervention.

One potential concern was whether there is sufficient capacity in the debt advice sector to absorb any increase in demand if debt packagers leave the market. Here we note that the respondent flagged that "the removal of [debt packagers] will displace the demand for debt advice of some 54,000 people towards other sources of advice". Based on discussions with partners, including the Money and Pension Service, we have concluded that an increase in demand of the volume suggested by the respondent would not cause disruption to the wider advice sector and that there is sufficient capacity.

IP fee structures

We acknowledge that our illustrative example of the IP fee structures is only one way IP fees could be structured; one respondent argued that the market norm is moving towards a fixed fee structure. In 2021, we conducted desk research into the 16 largest IPs. We found fee information for 10 of these firms, covering 61% of the IP market by customer numbers in 2020. Our desk research found that only 3 IP firms publicly stated on their website that they charged a fixed fee. We continue to see examples of fees being structured in a way that aligns with our illustrative example.

While we do not consider it necessary for the purposes of quantifying consumer harm, in the interest of completeness and transparency, we provide an additional illustrative example using a fixed fee structure for payments to IPs.

This should be read alongside 'Illustrative example 2: Costs of early solution termination' in the original CBA which provides an estimate for the increased costs of a failed IVA with a variable fee structure.

The example shows the total amount paid in fees for 3 hypothetical individuals.

The additional example at Table 1 shows a fixed fee model of £3,650 (as provided by a respondent), with repayments to creditors being made after 3 months and payments split 30% to IVA fees and 70% to creditors. Table 1 below provides an estimate for the increased costs of a failed IVA in terms of the total amount paid in fees in 3 illustrative examples in which the IVA fails after 6, 12, 24 and 36 months (Table 6 of the original CBA outlines how the average contributions are split over the first 3 years of an IVA in the variable fee model).

Table 1: Breakdown of payments to creditors and IVA fees (under a 'fixed fee model')

Consumer payments	Month the IVA/PTD is terminated			
	6	12	24	36
Individual A paying £80 /mth				
Payment to IVA fees (£)	144	288	576	864
Payment to creditors (£)	336	672	1,344	2,016
Total Paid (£)	480	960	1,920	2,880
Individual B paying £150/mth				
Payment to IVA fees (£)	270	540	1,080	1,620
Payment to creditors (£)	630	1,260	2,520	3,780
Total Paid (£)	900	1800	3600	5400
Individual C paying £300/mth				
Payment to IVA fees (£)	540	1,080	2,160	3,240
Payment to creditors (£)	1,260	2,520	5,040	7,560
Total Paid (£)	1800	3600	7200	10800

The illustrative examples in the original CBA show the potential impact on a customer of entering an unsuitable solution and, therefore, help show the value of compliant debt advice to a customer. The examples were not intended to give a quantitative estimate of harm or of the benefit of the intervention.

As shown in the last column of the above table (Table 1), the illustrative costs of early termination after 3 years are the IVA fees paid over the period. For an individual paying £80/month this is £864, £150/month this is £1,620, £300/month this is £3,240.

Compared to Table 7 of the original CBA, we note that the overall cost of early termination in terms of IVA fees is higher under the fixed fee model than the variable fee model used in the analysis of 'Illustrative example 2' in the original CBA. These amounts are substantial and indicate why it is essential for firms to provide customers with advice which complies with our rules and this applies to both fixed and variable fees models.

Increased costs to Principals

Principal firms should already be monitoring the behaviour of their ARs. As a result, we do not consider that requiring Principals to ensure their ARs do not accept referral fees or otherwise attempt to circumvent the ban would result in significant additional costs for them.

Increases in costs to IPs

In paragraphs 64-70 of our original CBA, we examine the arguments that this intervention would lead to increased costs for solution providers, including IPs. We acknowledge that solution providers may rely on debt packagers to:

- provide initial debt advice to consumers and match consumers with solutions
- market and attract new consumers to their services

However, we find evidence of debt packagers not adding value as an advice and matching service, from Phase 2 described below, and other supervisory and authorisation case work. Our supervision work found evidence which suggested that some packager firms appeared to have manipulated information about their customers' income and expenditure. While some respondents highlighted that debt packagers may offer an efficient way for IPs to collect relevant information about customers and to match them to solutions, the conflict of interest in the debt packager business model could undermine the accuracy of that information and therefore the quality of the service. While it may be the case that it is more expensive for an IP to match consumers with solutions, including information gathering and in-house checks, we cannot compare these costs with the current payments made to debt packagers as we are not convinced that debt packagers are carrying out that service to an acceptable and comparable standard. As a result, our view remains that debt packagers offer a valuable service to solution providers.

Changes to CBA figures

CP21/30 identified 39 firms that were operating in the financial year 2019-2020. As a result of our consultation and interactions with firms since, we now estimate there were 33 firms operating between April 2019 and March 2020. This is because:

- we have re-classified 3 firms as Insolvency Practitioners (IPs)
- one firm provided debt counselling to self-employed individuals and offered a number of solutions themself
- one firm informed us it had submitted data for the wrong financial year, and they were not engaging in debt advice activities in the year we had requested
- one firm had received money from solution providers, but they clarified this was not from referrals, and they had not been making referrals

These changes in the number of firms operating in 2019-2020 (from 39 to 33) mean that some of the information in the CP/CBA is different in the updated analysis. In particular:

- the total number of customers using debt packagers in 2019-2020 falls

from around 54,000 to around 52,000
- the number of customers accepted on to IVA/PTD in 2019-2020 falls from around 14,000 to around 13,000
- the market shares (in customer numbers) of Phases 1 and 2 of the evidence gathering increase (described below), and, consequently, the market share of Phase 3 firms decreases
- the median referral fee increases from £930 to £940; and
- the number and proportion of referrals to solution providers (see table 3 below) change

In our original CBA we describe 3 phases of supervisory multi-firm work we conducted in 2021 (2021 MFW):

- Phase 1 of the recent supervisory work was a data request to a portion of DP firms to understand the debt packager business model in more detail. The aim was to gather information on how leads to debt packagers are generated; how referral fees vary according to each solution; and the oversight in place to ensure compliant debt advice.
- Phase 2 was a review of customer files from a number of phase 1 firms to assess their compliance with the rules and guidance in the Handbook.
- Phase 3 was a second round of data collection sent to all packager firms not included in phase 1. We collected revenue data for each financial year between 2017 and 2021.

Table 3 (below) shows how the changes to firm numbers impact the information included in the CP about our phased supervisory work. Overall, the changes do not affect our conclusion on the cost-benefit balance of the intervention.

Table 2: How the revised number of firms change the figures in CP21/30

Variable	CP21/30	Corresponding amended figures	Direction	Explanation/ Implication
Firms in the market in 2019-2020	39	33	▼ Decrease	6 Firms removed from sample as not operating or no longer classified as DPs
Total number of DP customers in 2019-2020	54,000	52,000	▼ Decrease	Fewer affected customers
Phase 1 Market Share in terms of customer numbers in 2019-2020	82%	88%	▲ Increase	No impact, we have since collected revenue and referral data for the whole market

Variable	CP21/30	Corresponding amended figures	Direction	Explanation/ Implication
Phase 2 Market Share in terms of customer numbers in 2019-2020	61%	65%	▲ Increase	Minimal impact. These file reviewed firms represent a slightly higher market share, we have since reviewed the files of more firms
Phase 3 Market Share in terms of customer numbers in 2019-2020	18%	15%	▼ Decrease	No impact, we have since collected revenue and referral data for the whole market
Market Share of firms included in Phase 1 but not in Phase 2 in terms of customers numbers in 2019-2020	21%	23%	▲ Increase	No impact, we have since collected revenue and referral data for the whole market
Proportion of DP revenue generated by referral fees for x number of firms	94% rounded to 90% in the CP	97% (not rounded)	▲ Increase	Marginally reduces the transfer of non- referral fee income from debt packagers that leave the market to debt advice market participants that remain. Does not affect the proportionality of our intervention.
Median referral fee to DPs for IVAs in 2019-2020	£930	£940	▲ Increase	Minimal impact
Number/ Proportion of customers recommended on to an IVA or PTD in 2019-2020	17k, 29%	16K, 30%	▼ Decrease	Minimal impact
Number/ Proportion of customers accepted on to an IVA or PTD in 2019-2020	14K, 85%	14K, 85%	No Change	No impact

Variable	CP21/30	Corresponding amended figures	Direction	Explanation/ Implication
Number/ Proportion of customers recommended on to a NFP in 2019-2020	24K, 45%	24K, 46%	▲ Increase	Minimal impact
Number/ Proportion of customers recommended on to a DMP/DAS in 2019-2020	9K, 15%	7K, 13%	▼ Decrease	Minimal impact
Number/ Proportion of customers accepted on to an DMP/DAS in 2019-2020	5K, 53%	4K, 53%	▼ Decrease	Minimal impact

Aside from the number of customers affected falling slightly, these changes do not impact our conclusions drawn in the original CP and CBA.

Annex 1

Questions in this paper

Q1: **Do you have any comments on our consolidated evidence base (including as it is detailed in the CBA)?**

Q2: **Do you think there have been any developments (since 2020, and since our consultation in 2021) which have materially changed the management of the conflict of interest? If so, can you provide evidence of these developments?**

Q3: **Do you think there are any developments in the market which have changed the factors informing our decision as to the right intervention to tackle the harm or risk of harm we have seen? If so, can you provide evidence of these developments?**

Q4: **Do you have any further comments on our amended proposals and the draft Handbook text in Appendix 1 including the new PERG guidance?**

Q5: **Do you agree with the proposed implementation period of 2 months?**

Q6: **If you do not agree with the proposed implementation period, what alternative implementation period would you recommend? Please provide evidence for the length of implementation period you believe is required.**

Annex 2

Cost benefit analysis

Introduction

1. FSMA, as amended by the Financial Services Act 2012, requires us to publish a cost benefit analysis (CBA) of our proposed rules. Specifically, section 138I requires us to publish a CBA of proposed rules, defined as 'an analysis of the costs, together with an analysis of the benefits that would arise if the proposed rules are made'.

2. This analysis presents estimates of the costs and benefits of our proposals. These estimates are in monetary values. Where we are of the opinion that particular costs or benefits cannot reasonably be estimated, or it is not reasonably practicable to produce an estimate, we say so and provide an explanation for our view.

Updates to our evidence base

3. This CBA summarises and expands on the CBA from our original consultation (CP21/30). In CP21/30, we used evidence collected from Supervisory Multi Firm Work conducted in 2021 (2021 MFW). This was conducted in 3 phases:

- Phase 1 of the supervisory work was a data request to a portion of debt packagers to understand their business model in more detail. The aim was to gather information on how leads to debt packagers are generated; how referral fees vary according to each solution; and the oversight in place to ensure compliant debt advice.
- Phase 2 was a review of customer files from a number of phase 1 firms to assess their compliance with the rules and guidance in the Handbook.
- Phase 3 was a second round of data collection sent to all debt packager firms not included in phase 1. We collected revenue data for each financial year between 2017 and 2021.

4. Since then, we have expanded our evidence base in the following ways:

- We have added case file reviews of a further 2 firms, conducted by our Authorisations division.
- We have obtained additional revenue and referral data from the remaining firms in the market we were yet to collect this data from. We used this to separate the debt packager market into 5 segments according to firm size and revenue mix.
- We randomly selected 3 firms from 1 of the market segments that was underrepresented in CP21/30 and 2 from another, then:
  - we asked these 5 firms to identify any changes to their remuneration structure since the period between April 2019 and March 2020 (the period covered in our initial MFW data collection in 2021).

  - we supplemented our original findings with a review of a sample of 38 case files from those 5 firms.

5. We now have revenue and referral fee data covering the entire market and have taken file reviews from firms in every segment. The firms represent 85% of the market by customer numbers and 86% by revenue.

6. As a result of the expanded evidence base, we have also updated our view on the likely level of non-compliant, referral-fee paying advice being made to consumers and updated our estimates of the costs and benefits to firms and consumers.

Problem and rationale for intervention

7. The rationale for our intervention is largely unchanged from our original consultation. We provide a summary of the points in that consultation below and refer interested parties to CP21/30 for further details.

The harm

8. Debt packagers are authorised, commercial firms that provide debt advice services but do not provide any debt solutions themselves. In CP21/30, we estimated there were 39 such firms operating between April 2019 and March 2020. Based on our consultation and our interaction with firms since, we now estimate there were 33 firms operating between April 2019 and March 2020. This does not have a significant effect on our view of the market. The reasons for this change are set out in Chapter 4, above.

9. The debt packager business model relies largely on remuneration from referral fees from debt solution providers. These providers primarily supply the following debt solutions: Individual Voluntary Arrangements (IVAs), Protected Trust Deeds (PTDs), Debt Management Plans (DMPs), and Debt Arrangement Schemes (DASs). See Box 1 in CP21/30 for a detailed discussion of debt solutions. Revenue data we obtained for the period between April 2019 and March 2020 showed:

- For 23 of the 33 debt packagers (representing 67% of the market by customer numbers and 52% by revenue), referral fees constituted 100% of their income. These were typically smaller firms.
- for 7 of the 33 debt packagers (representing 29% of the market by customer numbers and 47% by revenue) referral fees constituted over 70% of their income. These were typically larger firms.
- Only 3 firms received less than 70% of their income from referral fees. These are firms we have classified as 'mixed revenue'. They made up less than 1% of the market by customer numbers and by revenue, and were smaller firms.

10. In chapters 1 and 2 of CP21/30 and chapters 1 and 2 of this consultation paper, we set out the risk of consumers receiving non-compliant, biased debt advice which could cause them to enter debt solutions which are not in their best interests. Typically, these will generate substantial referral fees for debt packager firms but may not meet the needs of consumers. Our survey of debt packagers also found that different solutions earn different levels of referral fees:

- the highest referral fees are paid for IVAs and PTDs – on average (median), these were £930 and £1340, respectively
- referrals to Debt Management Plans (DMPs), or in Scotland, Debt Arrangement Schemes (DAS) are on average £240 and £260, respectively
- no referral fees are paid for other solutions such as DROs or in Scotland, Minimal Asset Process (MAP)

11. After increasing the sample of firms whose files we have reviewed for compliance, we remain concerned that consumers served by debt packager firms are not receiving appropriate and valuable debt advice.

12. Our supervisory multi-firm work conducted in 2021 (2021 MFW), and, in particular, the case file reviews we conducted as a part of this MFW, raised concerns that firms appear to fall short of the standards set out in our rules. Evidence shared with us by the largest 2 debt advice not-for-profit firms (NFPs) strengthened these concerns. Both pointed to debt packager firms offering some consumers unsuitable advice and encouraging them to use solutions inappropriate to their circumstances. Further details can be found in CP21/30.

13. Non-compliant advice creates the risk that consumers are placed on solutions (especially IVAs or PTDs) that are unsuitable, which may lead to one or more of the following harms:

- **Consumers paying more than is necessary for a solution:** The most financially vulnerable consumers may be missing out on cheaper shorter-term debt solutions designed for consumers with low income and low assets such as Debt Relief Orders (DRO).
- **Increased and prolonged indebtedness:** If a solution fails, consumers will often find themselves in a similar position to where they started, despite having paid significant solution fees. An inappropriate referral increases the likelihood of solution failure.
- **Lower wellbeing:** If a solution is completed, but the repayments were difficult for the consumer to make in comparison to the repayments for a more appropriate solution, the consumer is likely to have lower wellbeing than they would have had if they had used a more appropriate alternative. Being in debt has a negative effect on consumers' personal wellbeing, so prolonging the period of indebtedness, potentially increasing the size of the debt if the solution fails, or reducing the likelihood a consumer is referred to a more appropriate solution that could allow them to write off a larger portion, will have a negative impact on a consumer's wellbeing.
- **Creditors may find it more expensive and less efficient to recover outstanding debts**

14. It is not reasonably practicable to estimate the number of people who end up on unsuitable solutions for reasons set out in CP21/30 and Chapters 2 and 4 of this consultation. Simply using complaints data will not capture the extent of the harm. This is because a consumer issuing a complaint is dependent on them being able to accurately assess that they have received poor quality advice. We do not believe consumers are well equipped to assess the quality of the advice they have been given because debt solutions are complex, it often takes time for the harm from a poor referral to materialise (such as the failure of a solution) and assessing whether or not the advice was appropriate requires the consumer to know how their outcomes would have differed under a different solution – a consumer with such information is also unlikely to have sought debt advice in the first place.

15. However, our analysis, which the following section summarises, does provide strong evidence that the incentives to offer non-compliant, biased debt advice are inherent to the debt packagers business model and firms are failing to adequately manage this incentive.

Potential drivers of harm

16. We have identified a number of drivers (or causes) of harm described in the previous section, these remain unchanged from CP21/30. They are summarised below.

17. For consumers, harm can be due to:

- Complexity and difficulty in assessing information leading to firms knowing more about the suitability of a solution than the consumer (also known as asymmetric information).
- Behavioural distortions which affect consumers' assessments of debt advice. For example, a consumer may commit themselves to a repayment plan they cannot maintain, as they are overconfident about their abilities to make the payments or may prioritise the immediate peace of mind that a solution offers over the longer-term costs it entails. A full description of the various behavioural distortions that potentially drive harm in this market is given in CP21/30.

18. Factors relating to firms that can cause consumer harm are:

- Reliance on referral fees creating a strong incentive for debt packagers to refer customers to any solution where no solution would be the most appropriate option.
- Where a solution is appropriate, there is a strong incentive to refer consumers toward solutions, and solution providers, that pay the highest referral fees. The highest paying solutions, and solution providers, may be less appropriate than a solution or solution provider that pays a lower referral fee.

19. These market failures create an environment where consumers may not be aware of the most appropriate solution and may in fact be motivated to choose an inappropriate solution by their own biases. Firms are also not always incentivised to choose the most appropriate solution for them and may in fact take advantage of consumers' behavioural biases to present inappropriate solutions in a more favourable light.

20. For consumers to be recommended appropriate solutions, firms must manage the conflict of interest between earning the highest referral fees and recommending the most appropriate solutions to consumers.

Evidence of sales and product bias from referral fees and debt packagers

21. In Chapter 2 of CP21/30 we outlined the findings of our 2021 MFW work, which support our finding that debt packagers are failing to adequately manage the conflict of interest described in the previous section. In particular, we identified evidence of firms manipulating consumers' income and expenditure information to meet the criteria for an IVA or PTD. These practices are an example of sales and product bias. Our evidence from all debt packagers in our revenue and referral data collection shows that average referral fees are substantially higher for personal insolvency solutions (IVAs and PTDs) compared to DMPs or DASs.

22. In October 2022, we collected data from 5 firms on any changes to their remuneration structure since the period between April 2019 and March 2020 (the period covered in our initial MFW data collection in 2021) and July 2022. The 5 firms reported increases in average DMP commission between 12% and 147%. 4 of the 5 firms informed us of increases to average IVA referrals fees between 18% and 46%. 1 firm's average IVA fee fell by 47%, however, it still remained 44% larger than their average DMP commission.

23. This data shows that, for these firms, average referral fees for debt solutions have increased since the period between April 2019 and March 2020. This is likely to increase the incentive to refer a consumer to a referral fee-paying solution even if the customer is better off without a solution. Further, the difference between fees from different solutions to which a firm could refer a customer also remain similar, meaning the incentive to refer a consumer to a higher paying solution still exists. We also found little substantive change in business models since the period covered in CP21/30– between April 2019 and March 2020. This aligns with intelligence our Supervision and Authorisations functions have gathered from interactions with participants in the debt advice market – that the factors driving the conflict of interest in 2019/20 still exist today. Therefore, **we believe the incentive to refer consumers to an inappropriate solution persists**.

Overview of our proposed intervention

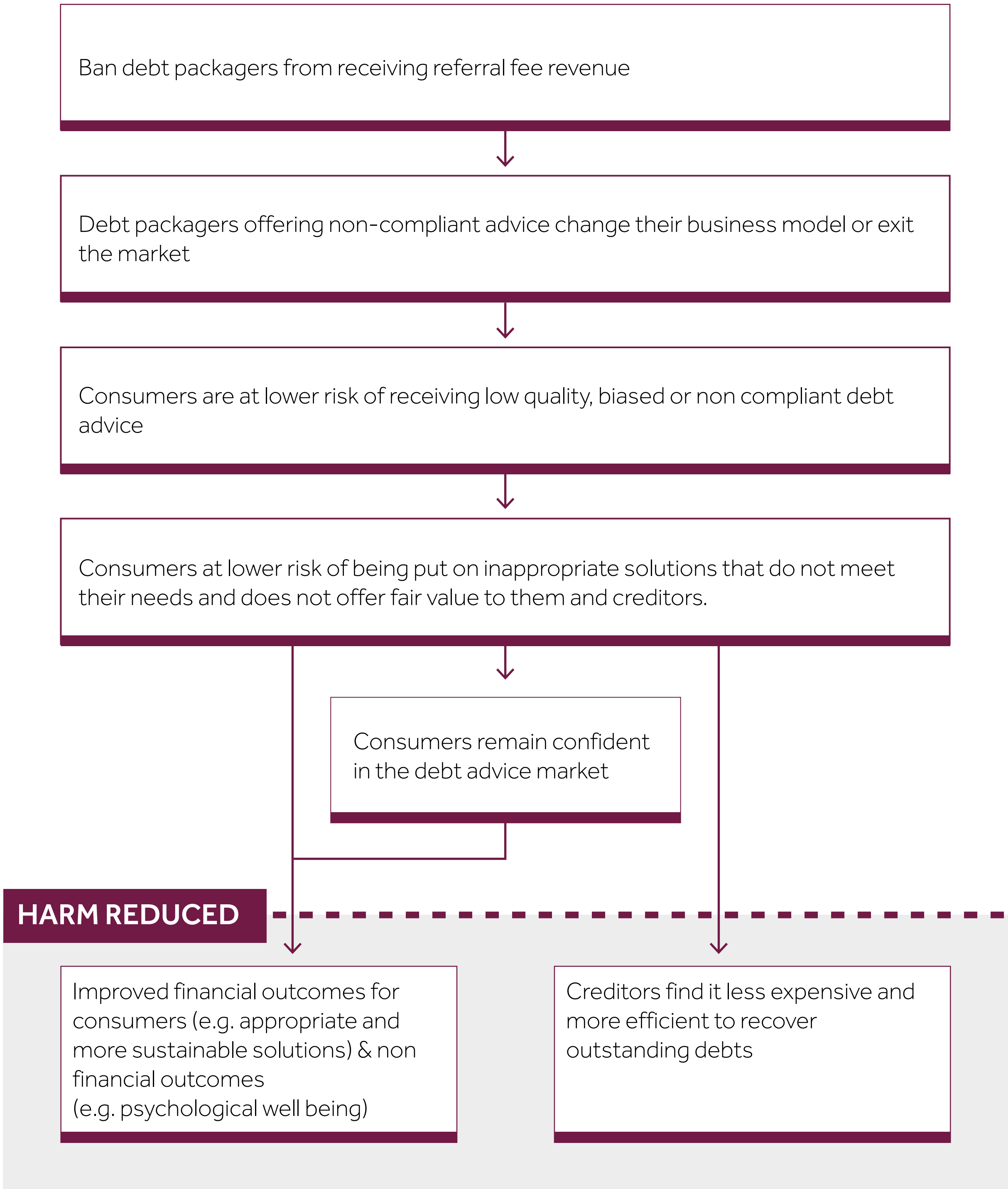
24. Our proposed intervention is unchanged from CP21/30. We are consulting on new rules that would ban debt packagers from receiving renumeration for referring an individual to a debt solution provider. In addition to the proposed intervention, we considered a number of alternatives including:

- enhanced supervision
- a fixed, single referral fee for all solutions
- a price cap
- qualification requirements for advisors
- widening of the insolvency practitioner (IP) exclusion (to allow IPs more freedom to give debt advice without FCA authorisation)

25. We set out in Chapter 3 of the consultation, and again in Chapters 2 and 4 of this CP, why we believe these solutions are either prohibitively difficult to implement or fail to eliminate the underlying drivers of harm in this market.

26. The causal chain for our intervention, Figure 1, is unchanged from CP21/30.

Figure 1 Causal chain for proposed intervention



27. As a result of our proposed ban on referral fees, the participants remaining in the market would have business models that either adequately manage any conflict of interest between consumers and firms, or do not create them. This would reduce the risk that consumers are given biased, low quality or non-compliant advice, increasing the likelihood that they will be put on appropriate solutions. Appropriate solutions save consumers money and are more likely to be completed without the solution failing. Therefore, financial and wellbeing outcomes would improve for consumers, and creditors would spend less money recovering debts.

28. In addition to our policy intervention, we are also consulting on perimeter guidance. Our proposed perimeter guidance makes clear that passing consumers to a solution provider who is only able to offer one solution may fall under the regulated activity of debt counselling, depending on the individual circumstances. We consider the costs and benefits below to cover both the costs and benefits of the policy proposal and any novel element of the perimeter guidance.

Our analytical approach

Baseline and key assumptions

29. For CP21/30, we surveyed all 54 firms that were classified as commercial debt advice firms at the time, which includes debt packager firms. All were classed as small firms under our standardised cost model.[1] We set out in CP21/30 how we excluded 15 of these firms from our analysis, on the basis that they are not debt packagers. We have since excluded a further 6, leaving 33 firms in the debt packager market. The grounds for this are set out in Chapter 4: the Feedback Statement to CP21/30, above.

30. There are 2 types of debt packager firm structures; those that provide advice as an independent solo entity and those that operate a principal and appointed representative (AR) structure. The principal firm can carry out regulated activity in its own right or through an AR (who is not authorised by the FCA for debt counselling), but the principal has regulatory responsibility for ensuring the AR is compliant with our regulations.

31. Based on all our data collection, we make the following assumptions for this cost benefit analysis:

- We assume that the referral fee data we collected for financial year 2019/20 was representative of a typical year. We are confident in this assumption as referral fees were constant as a proportion of total revenue between 2017 and 2020.
- We assume that the types of benefits for consumers and types of costs for firms identified in this CBA are consistent for all debt packagers and their customers. We make this assumption as we found the incentives to offer non-compliant advice were present across all debt packager firms, as they all receive referral fees from solution providers.
- We consider that evidence of non-compliance indicates that the conflict of interest is not being adequately managed creating an unacceptable level of risk of the harms we have identified occurring. We acknowledge there may be other causes of non-compliance, however we are confident in our assumption because:
  - Our evidence-gathering has found a high proportion of non-compliant advice which suggests bias towards certain solutions. In these cases, we have seen the

1 https://www.fca.org.uk/publication/corporate/how-analyse-costs-benefits-policies.pdf

consequences of the non-compliance are that a customer is steered towards the solution through the way the firm presents it, or the firm is manipulating a customer's information so that they are eligible for a certain solution or so that it seems like a better option. We consider firms are failing to adequately manage the conflict of interest and it is driving this behaviour.

- Although we have found evidence of some advice that isn't obviously biased in this way but is still non-compliant, the conflict of interest is still a driver of these types of non-compliance. For example, we have observed instances where debt packager firms do not fully investigate customer circumstances, or they do not dedicate enough attention to other aspects of the advice process. With a referral fee reliant business model, firms are not necessarily incentivised to have proper governance and procedures to limit this kind of non-compliance. Investing in proper governance and procedures would ensure compliance with our rules which govern those matters and deliver benefits to consumers. However, firms operating under such an acute conflict of interest are unlikely to see the value of this and consider those actions are unlikely to increase the number of customers they have or the profitability of each customer, therefore, they may consider it is not in the firm's interest to do so. This means the referral fee business model increases the likelihood of this type of non-compliance too.

How we have expanded our evidence base since CP21/30

32. In our original CBA, our estimation of harm was based on case file reviews undertaken in the 2021 MFW. Since publishing CP21/30 and the annexed CBA, we added all case file reviews of debt packager firms undertaken through our Authorisation function since October 2018 to our evidence base. This included reviews of a total of 10 files from 2 additional firms and a further 15 file reviews for 2 firms that were already included in our original CBA as they were sampled in the MFW. These cases were assessed against the same criteria as our October 2022 sample. While the number of file reviews is a small percentage of all referrals, we have followed a rigorous statistical procedure (set out in Annex 3) to ensure we have enough files, across an appropriate range of firms, to allow us to make statistically robust conclusions about all firms in a segment, and all segments in the market.

33. We also requested revenue data from all debt packager firms for which we had not had this information previously. In CP21/30,we estimated there were 39 debt packager firms operating between April 2019 and March 2020, who served 54,000 customers. We now estimate that there were 33 debt packager firms operating in that period with a total of 52,000 customers. The additional revenue data means we can segment the whole market between April 2019 and March 2020 by firm size, market structure, and revenue mix. We find 5 segments in this period. Table 1, below, summarises the number of firms in each segment:

Table 1 - Debt packager segments: Information on market share and number of firms reviewed

Segment	Share of customers served	Number of firms	Number of firms reviewed for compliance in their case files in 2021 MFW (forming the evidence base for CP21/30)	Number of firms reviewed for compliance in their case files by our Authorisations function	Number of firms reviewed for compliance in their case files in October 2022 sample	Total number of firms reviewed for compliance in their case files
Small solo	23%	20	2	0*	3	5 out of 20
Large solo	16%	1	1	0	0	1 out of 1
Large principal and their ARs	35%	2	2	0*	0	2 out of 2
Small principal and their ARs	24%	7	0	2	2	4 out of 7
Mixed revenue	1%	3	0	0	0	0 out of 3

Note: Our Authorisations function also reviewed case files from a firm in the Large Principal, and a firm in the Small Solo segment, however these firms had already been reviewed as part of the multi-firm work. Although this does not increase the number of firms we have reviewed, it does increase the number of files, so we have added the results of these reviews to our evidence base.

34. Through this segmentation, we identified that we could improve the representativeness of our evidence base in our original CBA by gathering more evidence from 3 of the 5 categories - mixed revenue firms, small solo and small principal, as they were underrepresented in CP21/30.

35. We consulted with an independent expert statistician on the inferences we could make from the evidence we had collected in the 2021 MFW and Authorisation reviews, and how we could sample from more firms to supplement this. Taking into account their advice, we decided to randomly select a sample of firms from the Small Solo, Small Principal and Mixed Revenue categories (we refer to this as the "October 2022 sample"). When we reached out to the selected firms, we found only 1 firm from the mixed revenue category that was both active in the 2019-2020 period and still active in October 2022 (the other 2 had cancelled their permissions since 2019/20). However, technical issues with file storage and personal circumstance made the cost of them supplying files disproportionate to the benefit it would give to our evidence base. Therefore, we did not request files from this firm. Further, we see this firm as an outlier and note it has subsequently left the market so did not review files from them. This left us with 3 firms from the Small Solo category and 2 firms from the Small Principal category from which we planned to sample and review case files.

36. We undertook additional file reviews on a sample of 38 case files from these 5 firms using a sampling scheme called 'Acceptance Sampling'. Annex 3 explains this method in greater detail. This sampling approach allows us to infer whether a firm should be:

- judged to be adequately managing the conflict of interest, due to a tolerably low number of non-compliant case files, or
- judged to be failing to adequately manage the conflict of interest, due to an unacceptably high number of non-compliant case files.

37. As explained in our 'Drivers of harm' section, we consider non-compliant advice to be symptomatic of the failure to adequately manage the conflict between consumers' interests and firms' financial incentives. In many case files, there was evidence of explicit bias toward specific solutions.

38. If the prevalence of non-compliance across firms is low, we can infer that any failure to adequately manage the conflict of interest is due to the actions and structure of specific firms, rather than it being a consequence of the business model. However, if we find evidence of high levels of non-compliance at a significant number of the firms in a segment, we can infer that the failure to adequately manage the inherent conflict of interest is a consequence of the business model of the firms in that segment, presenting a significant risk of poor outcomes to consumers.

39. Our expanded evidence base means we can make inferences for each segment of the debt packager market. We make inferences for the well-represented segments in CP21/30 using file reviews from CP21/30 and the additional reviews from our Authorisations function, while inferences for the segments underrepresented in CP21/30 are made using a combination of file reviews from the October 2022 sample, file reviews from our Authorisations function and file reviews from the 2021 MFW sample.

40. We found evidence which strongly suggested every firm in the combined 2021 MFW, Authorisations and October 2022 sample was non-compliant with our rules to such an extent that we could conclude they were failing to manage the conflict of interest created by the referral fee business model. We therefore infer that, across all segments in the debt packager market, there is failure to adequately manage the conflict of interest caused by referral fees. This confirms and strengthens the findings of CP21/30.

41. Below, we have used our findings to update the costs and benefits we estimated in CP21/30.

Summary of costs and benefits and comparison with CP21/30 CBA

42. CP21/30 originally estimated that from April 2019 to March 2020 debt packagers received £13m in revenue from referrals. This revenue would be lost under our proposals, however, the result of our original file review indicated 90% of the referrals that produced this revenue presented a significant risk of poor outcomes for consumers. We do not consider revenue lost from non-compliant advice as a cost to firms. Instead, we see it as a benefit transferred to customers, solution providers, and creditors. Therefore, we estimated annualised benefits of £11.7m from referral fees, redistributed to other participants in the debt advice market, and annualised costs of £1.3m from lost revenue from compliant advice. This is an annualised net benefit of £10.4m.

43. In CP21/30 we produced illustrative examples of the typical monetary benefits of appropriate referrals to indicate the ways in which the redistributed referral fees could manifest as improved financial outcomes. We have updated the illustrative examples to include monetary estimates of the benefits to psychological wellbeing that reduced debt creates. In our example, explained below, an individual with £30,000 in debt who is referred to an IVA when a Debt Relief Order (DRO) would have been more suitable suffers a monetised loss to well-being between £186 and £297 in addition to the £4,720 financial loss resulting from the referral. Though we cannot estimate the total effect on well-being of our policy, this example illustrates the potential increase in well-being we expect our proposed policy would produce for consumers.

44. It is not reasonably practicable to estimate the benefits to creditors for the same reasons it is not reasonably practicable to estimate all the benefits for consumers.

45. Based on our expanded evidence-gathering since the original CBA, we are now able to refine our estimates of the costs of lost revenues to debt packager firms. Our estimate of the total revenue that debt packagers received has marginally lowered to £12.77m from April 2019 to March 2020. The small change in our revenue estimate from CP21/30 is largely due to us now estimating there were 33 rather than 39 debt packager firms. This revenue would be lost under our proposals. However, based on our expanded evidence base, explained in the previous section, we estimate £11.05m (comparable point estimate) of this revenue comes from referrals that present a significant risk of poor outcomes to consumers (our previous estimate was £11.3m).

46. **We estimate a £1.72m loss per annum from referral fee payments to debt packagers** (compared to our previous estimate of £1.3m).

47. Our intervention would lead to some market restructuring which may impact debt packagers, lead generators, solution providers and creditors. We discuss the potential unintended consequences of our policy in paragraph 78. One such consequence is some debt packagers may choose to exit the market, forgoing the revenue they had from other activities. We would expect the revenue lost on these other activities to be transferred to other market participants who take the business following a restructuring of the market. Therefore, we count this lost revenue from non-referral fee activities as a transfer rather than a cost. As it is uncertain how firms would respond, the indirect costs and benefits to these firms cannot be reasonably estimated. We provide an explanation

of the expected effects and explain in more detail why we cannot give monetary estimates for these costs.

48. Table 2 below summarises the updated costs and benefits from our intervention. We compare our estimated figures to those in CP21/30. Where we have produced ranges, the most likely outcomes of the policy would be clustered around our central estimate, not the mid-point of the range.

Table 2 - Summary of costs and benefits of the proposed policy

	Estimated One-off costs/benefits		Estimated Ongoing costs/ benefits per year	
	CP21/30 CBA	Updated	CP21/30 CBA	Updated*
Compliance Costs				
Familiarisation and Legal costs	-£27,000	-£26,000[2]		
Direct Costs to debt packagers				
Loss of revenue from non-compliant advice – treated as a transfer for purposes of CBA			*-£11.70m*	***Central Estimate:*** *-£11.05m* *-£7.50m - -£12.14m*
Loss of revenue from compliant advice[3]			*-£1.30m*	**-CE: £1.72m** -£0.63m - -£5.27m
Loss of non-referral fee revenue			*-£0.60m*	*-£0.44m*
Total Costs	-£27,000	-£26,000	*-£1.30m*	**CE: -£1.72m** -£0.63m - -£5.27m
Benefits				
Benefits from redistributed revenue from non-compliant referrals			*£11.70m*	**CE: £11.05m** £7.50m - £12.14m
Net Cost/Benefit		-£26,000	*£10.4m*	**CE: £9.33m** £2.23m - 11.51m

Source: FCA data collection.

Note: Estimates are rounded. Non-compliance is estimated at the segment level based on our file reviews. The costs/benefits for each segment are summed to produce costs/benefits for the whole market. Transfers in Italics (loss of non-referral fee revenue, as a transfer, see paragraph 47, is not included in net cost/benefit). Where we have produced ranges, they represent the cost/benefit for upper and lower 95% confidence intervals for our estimates of non-compliance. This means that if we were to conduct our case file reviews 100 times over, randomly selecting the same number of case files in each review, of the 100 figures we produced as an estimate for non-compliance, 95 would lead to costs/benefits within the range we have given. We would expect the estimates to be clustered around the level we measured. The central estimate is not in the middle of this range but is based on the measured level of non-compliance, the most likely outcomes for the policy would be clustered around this figure.

2 £4,000 of these costs come from debt packagers, £6,000 of these costs come from the relevant regulators and £16,000 of these costs come from solution providers that pay debt packager firms.

3 We did not review any case files from the Mixed Revenue category, so we cannot justify with case review data any conclusion about the compliance level of their referrals.

49. We expect our proposal would be net beneficial. Our estimates of the revenue that would be lost from referral fee revenue that presents a significant risk to consumers is greater than the estimated costs to debt packager firms. There are also unquantified benefits to our proposal, such as improved consumer wellbeing, therefore our quantified net benefit is likely to be an underestimate of the actual net benefit.

50. **Over 10 years we expect a discounted net present benefit of £80.3m**, with a lower estimate of £19.1mn and higher estimate of £99.0m.[4] We would expect our annual benefits to persist until there is a major market structure change that is not in our baseline. If this were to occur sooner than 10 years, then we might expect the benefits to be smaller or larger.

Costs

Loss of debt packagers' revenue from referral fees

51. Data provided by debt packagers about the period from April 2019 to March 2020 showed they received £12.77m in revenue from referrals to debt solutions between April 2019 and March 2020. Approximately 82% of this revenue was from referral to an IVA, 10% for a referral to a PTD, and the remaining 8% from referrals to a DMP or DAS or other solutions.

52. The policy proposal would ban debt packagers from receiving the above income from referral fees. However, we do not consider the loss of revenue from providing advice below acceptable standards as a cost to firms as they are exploiting a market failure to the detriment of consumers. CP21/30 estimated only 10% of the recommendations to enter an IVA, PTD, DAS, or DMP did not present a significant risk of poor outcomes for customers. Based on our additional evidence gathering, we estimate around 14% of paid referrals are compliant. Using our updated evidence base, **we now estimate the cost to firms of lost referral fee revenue from compliant advice is £1.72m (central estimate)**. Table 3 shows the range within which we expect this cost to fall, and how this is distributed across segments.

4 Assuming a yearly discount rate of 3.5%, as per HMT Green Book guidance

Table 3 Estimated Annual Cost from Lost Revenue from Compliant Referrals

Market segment	Total revenue from referral fees	Estimated lost revenue from referrals that are compliant with our current rules		
		Lower Bound	Upper Bound	Central Estimate
Small Solo	£2.94m	-£1.15m	-£0.11m	-£0.26m
Large Solo	£0.70m	-£0.17m	-£0m	-£0m
Small Principal	£3.61m	-£2.07m	-£0.18m	-£0.62m
Large Principal	£5.51m	-£1.87m	-£0.33m	-£0.81m
Mixed Revenue	£0.02m	-£0.02m	-£0.02m	-£0.02m
Total	£12.77m	-£5.27m	-£0.63m	-£1.72m

Source: FCA data collection.

Note: Estimates are rounded. Figures are inferred from the proportion of case files found to be non-compliant in case files reviews for CP21/30, additional file reviews by our Authorisations function, and the October 2022 sample. Where we have produced ranges, they represent the cost/benefit for upper and lower 95% confidence intervals for our estimates of non-compliance. This means that if we were to conduct our case file reviews 100 times over, randomly selecting the same number of case files in each review, of the 100 figures we produced as an estimate for non-compliance, 95 would lead to costs/benefits within the range we have given, and we would expect the estimates to be clustered around the level we measured. The central estimate is not in the middle of this range but is based on the measured level of non-compliance, the most likely outcomes for the policy would be clustered around this figure.

Loss of lead generator revenue from referral fees

53. We expect the perimeter guidance could cause some lead generators to exit the market and some to become authorised. It is not reasonably practicable to quantify this cost. However, we would expect the lost revenue to be redistributed through the debt advice market, as solution providers would pay less for consumer leads. Further, where revenue is lost that was previously earned through poor conduct, we do not consider it a loss to the firm.

54. We expect the main impact of the perimeter guidance would be to mitigate the risk that some of our estimated benefits are not realised due to debt packagers adjusting their business model to lead generation.

Costs to consumers

55. In CP21/30 we recognised that our intervention would reduce the capacity of the debt advice market. Debt packagers' active presence in the debt advice market allows them to act as factfinders for consumers and increase awareness of the debt support available. There is a risk that if debt packagers exit the market, consumers that would have been engaged through debt packagers' advertising may not seek advice.

56. However, of the 52,000 consumers that get referred by debt packagers, around 46% of people are already referred to the not-for-profit (NFP) sector. This means the increase in demand for NFP services is small relative to the size of the market. In 2020, Money and

Pensions Service (MaPS) estimate that 1.7 million people received debt advice, implying debt packagers give advice to around 1.4% of the debt advice market.[5]

57. We do not believe there would be significant competition costs for consumers as we do not believe competition is working in their interest. For competition to improve consumer outcomes, consumers must have the capacity and information to make decisions in their interests. Otherwise, they cannot judge providers' quality and price levels, and thus choose the best product. We have set out in the CP and CBA why we believe consumers do not have the information or capacity to make these decisions accurately.

58. Therefore, we do not believe the costs to consumers would be material, particularly in comparison to the scale of the benefits.

Costs to the FCA

59. There are no expected additional costs to the FCA.

Benefits

60. Based on our evidence used in CP21/30, and supplementary evidence we have gathered since, **we estimate the amount of debt packagers' lost revenues that would be redistributed to consumers and the rest of the supply chain as a benefit is £11.05m**. Our estimate has changed (from £11.7m) because we have found lower levels of non-compliance in our October 2022 sample than in the MFW. In our combined sample, around 86% of the files we reviewed showed evidence of non-compliance, which is lower than the 90% we stated in the original CBA. However, it is still sufficiently high to cause significant concern about debt packagers practices. Full details of our updated estimates are in Table 4 below.

Table 4 Estimated annual benefits from redistributed debt packager revenue from non-compliant referrals

Market segment	Total revenue from referral fees	Estimated revenue from referrals that present a significant risk of a poor outcome for customers		
		Lower Bound	Upper Bound	Central Estimate
Small Solo	£2.94m	£1.79m	£2.83m	£2.67m
Large Solo	£0.70m	£0.53m	£0.7m	£0.7m
Small Principal	£3.61m	£1.54m	£3.43m	£2.99m
Large Principal	£5.51m	£3.64m	£5.18m	£4.69m
Mixed Revenue	£0.02m	-	-	-
Total	£12.77m	£7.50m	£12.14m	£11.05m

Source: FCA data collection.

Note: Estimates are rounded. Figures are inferred from the proportion of case files found to be non-compliant in case files reviews for CP21/30, additional file reviews by our Authorisations function, and our representative sample of 5 firms in the

5 https://moneyanDebt Packagerensionsservice.org.uk/wp-content/uploads/2020/01/UK-Strategy-for-Financial-Wellbeing-2020-2030-Money-and-Pensions-Service.pdf

October 2021 Sample.We are unable to estimate how this revenue would be redistributed due to the range

61. of possible outcomes of market restructuring, however, we expect several potential benefits to consumers and the rest of the supply chain:

- consumers would not pay more than necessary for a solution
- reduced risk of prolonged indebtedness from early termination
- improved well-being from quality debt advice
- increased likelihood of debt repayment

62. We note that the benefits of this intervention may exceed the £11.05m from redistributed referral fees as there are wider benefits to society (or positive externalities) from the provision of good quality debt advice, for example the benefits to well-being. Though we cannot quantify the exact welfare gains to consumers of our intervention, as we cannot be certain of the debt solutions that consumers would otherwise be referred to, we offer an illustrative example of the monetised gain to wellbeing a consumer may receive by our intervention.

Psychological benefits from a recommendation to a suitable solution

63. In CP21/30, we gave an illustrative example of how the benefits may manifest for consumers. We consider a hypothetical case for an individual who was referred to an IVA where they would have been eligible for a DRO. IVA repayments are dependent on the individual's spare income after expenses. In the circumstances proposed (which, based on our evidence gathering, is similar to many real circumstances), the individual would be put on an IVA paying £80 a month for 60 months (totalling £4,800). Alternatively, they could have been eligible for a DRO where they would pay a one-off fee of £90, and if their circumstances did not change in 12 months, the debt would be written off.

64. An individual could be eligible for a DRO for debts up to £30,000. We have used this amount to estimate the monetary value of the net wellbeing benefit created by reduced psychological stress for an individual. We have used the approach in the Treasury's Green Book to convert the value of increased wellbeing into a monetary benefit.[6]

65. We have used the findings from a report commissioned by the FCA into the effect of debt on subjective wellbeing,[7] to estimate the wellbeing benefit that an individual in this scenario would gain. The report estimates the change in an individual's subjective wellbeing on a scale of 1 to 10 (with 10 as the highest level of subjective wellbeing) caused by a change in their debt. The monetised increase in wellbeing is additional to the financial gain that reducing debt creates. Being in debt is a psychologically stressful experience, so reducing debt increases wellbeing.

66. Comparing a referral to an IVA to a referral to a DRO in these circumstances we find the following:

6 HMT Green Book estimates a 1-point increase in wellbeing is worth between £10,000 and 16,000 to a typical consumer, with a mid-point of £13,000

7 https://www.fca.org.uk/publication/research/simetrica-jacobs-wellbeing-impacts-debt-related-factors.pdf

Table 5 Monetised wellbeing benefit of referral to a suitable solution in illustrative example 1

	IVA	DRO	Difference
Debt written off by solution	-84%	-100%	**16%**
Change in life satisfaction	+0.364	+0.382	**0.018**
Monetised benefit of increase in life satisfaction[8]	£3,636 - £5,817	£3,821 - £6,114	**£186 - £297**

Note: The Simetra-Jacobs report estimates a log linear model. The model estimates that reducing credit card debt by ~1% increases subjective wellbeing by 0.00467 (the per % increase in wellbeing is non-linear and decreases as the amount written off approaches 100%). This leads to a change of 0.364 for the IVA referral and 0.382 for the DRO referral. In both cases, the consumer goes from being in arrears, to no longer in arrears. In addition to increased wellbeing due to reduced debt, the report estimates that no longer being in arrears increases wellbeing by 0.355. We have applied these estimates of effect to the illustrative example to show the change in subjective wellbeing caused by the IVA and DRO respectively and calculated the difference in outcomes between the two to give the benefit of a suitable referral in this case.

67. An individual in this circumstance has 16% more of their debt written off, and their life satisfaction (out of 10) increases by 0.018 more under a DRO than an IVA. **This is equivalent to an endowment between £186 and £297**.[9]

68. To understand how debt level impacts welfare change, we have additionally produced our estimates based on a debt of £20,000. Although a lower debt would reduce the absolute (£) difference in the amount written off by a DRO compared to an IVA, and the absolute benefit gain of being referred to either of these solutions rather than not being referred, it would not change the increase in welfare experienced by an individual referred to an IVA rather than a DRO.

69. The report also examines the effect of other circumstances on the change in welfare caused by reduced debt. They find unemployed consumers gain a larger welfare boost from reduction in debt than employed consumers. We would therefore expect the welfare benefits to be higher in cases similar to this illustrative example for unemployed consumers, than employed.

70. Many debt solutions, particularly IVAs, are terminated early as consumers fail to keep up with the repayments. 28% of IVAs issued between 2014 and 2018 have failed.[10] This is more likely to happen where an IVA is not suitable for a consumer, and making the repayments is extremely difficult. If we consider the consumer in the first illustrative example fails to keep up with the IVA repayments due to an overestimation of their disposable income by the debt packager (a scenario we have seen in our case file reviews), they will have to terminate their solution early.

71. Early termination of an IVA leads to the consumer paying significant solution fees, and often only a small amount of their debt. In the 'Cost Benefit Analysis' section of Chapter 4, we show how termination of an IVA after 3 years, for a consumer in our illustrative example would lead to them paying £864 in fees and £2,016 in debt. As the solution has failed, they will be in arrears debt totalling £27,984 (£30,000 - £2,016). If they had been

8 See above

9 See above

10 https://www.gov.uk/government/statistics/individual-voluntary-arrangements-outcomes-and-providers-2021/commentary-individual-voluntary-arrangements-outcomes-and-providers-2021 Figure is for all IVAs, not just those originating from debt packagers

on a DRO, their capacity to make future repayments would not influence the success or failure of the solution, as they do not make future repayments. In fact, a DRO will only fail if the financial situation of the consumer improves, and in this case, they can start an IVA having only paid £90 in solution fees.

72. In our illustrative example, being referred to an IVA that has ultimately failed means the consumer has paid substantial fees towards a solution that has not substantially reduced their debt, and they are still in arrears. This would not be the case had they been referred to a DRO instead.

73. Using the findings from the report commissioned by the FCA into the effect of debt on subjective wellbeing,[11] we estimate that being in arrears decreases subjective wellbeing by 0.355 relative to not being in arrears. This is equivalent to a cost between £3,550 and £5,680.

74. By increasing the probability that a consumer receives a suitable referral and therefore decreasing the likelihood that the referral fails, the proposed policy would decrease the chance a consumer could end up back in arrears due to solution failure and incur the stated cost to their subjective wellbeing. **In these cases, our solution would provide a benefit equivalent to an endowment between £3,550 and £5,680, relative to the baseline scenario where we do not intervene.**

75. Although we cannot estimate the aggregate wellbeing benefit created by the reduced psychological stress, we have illustrated it is a significant benefit in the types of cases we would expect our proposed intervention to affect.

Impact on creditors

76. In CP21/30, we outline our view that this policy would not have a significant negative impact on creditors. Only a small proportion of debt advice (approximately 1.4% of the consumers seeking debt advice per year) is supplied through debt packagers so there is only a small risk that creditors do not receive repayment as a result of a consumer not receiving debt advice. In fact, based on our experience of the debt advice market we believe creditors are more likely to receive repayments as we expect our intervention would mean consumers are more likely to be referred to appropriate debt solutions that they can afford, increasing the likelihood of them seeing the solution to completion as set out in our above illustrative examples. CP21/30 contains a more detailed explanation of this.

Lower supervision costs for the FCA

77. Supervising a sector where non-compliance is widespread requires significant resources. By removing the driver of non-compliance, we expect we would free supervision resources to be used in other sectors.

11 https://www.fca.org.uk/publication/research/simetrica-jacobs-wellbeing-impacts-debt-related-factors.pdf

Risk of unintended consequences

78. We recognise there is a risk that debt packagers could adapt their business model to avoid the rules, or other market participants such as unauthorised lead generators could approach the types of customers previously served by debt packagers and replicate the behaviour we are seeking to prevent by referring them straight to solution providers based on the solution that pays the most for a lead rather than the solution that is most appropriate to the customer.

79. We are working in collaboration with the Insolvency Service to mitigate the risk of harm from a rise in unauthorised lead generation and trying to make sure that the quality of advice given outside our perimeter (such as where an exclusion applies) is suitable. We are consulting on perimeter guidance to further mitigate this risk.

Distributional effects

80. Based on our knowledge of the sector, we expect that the redistribution of referral fee revenue to consumers and firms from our intervention would most benefit consumers at the lower end of the income and wealth distribution. We also expect our intervention would benefit vulnerable consumers, especially those with low financial literacy as they are more liable to struggle with asymmetric information and the behavioural distortions that put them at greater risk of harm unsuitable referrals.

81. However, we have not collected data on the distributional impact of debt advice in the debt packager market, so we cannot confirm our expectations.

Impact on the competitiveness and growth of the UK's financial system

82. We recognise this measure may add a stringent requirement that could restrict the choice of business model for firms considering entering the debt advice market. However, we expect this measure would increase the efficiency with which creditors can collect debts, reduce the likelihood of an individual remaining in debt or an adverse financial position and improve trust in the debt advice sector. We would expect this to positively affect key drivers of productivity including trust and reputation, and thus improve competitiveness and drive mid to long term growth.

Monitoring and evaluation

83. In Chapter 1 of the CP, we discuss our proposed approach to monitoring and evaluation. The outcome we are seeking is:

- We want all debt advice firms which we regulate to provide a high-quality service to consumers, which has regard to their best interests and is appropriate to the individual circumstances of each particular consumer.

84. Using data-led intelligence we would look for signs that the outcomes we are seeking are not being achieved such as:

- Firms adapting their business models in a way which could cause harm. For example, we see a risk that debt packager firms could look to become appointed representatives of a debt management firm. This would not be an acceptable outcome. Therefore, our proposals include an obligation on principals (including debt management firms) to take all reasonable steps to ensure that none of their appointed representatives receive any remuneration from debt solution providers, unless the appointed representative is genuinely acting as a debt management firm itself. We will actively monitor this.
- The number of consumers being referred inappropriately to IVAs/PTDs does not fall. While some customers would continue to be recommended an IVA or PTD where this is appropriate, removing the strong conflict of interest should reduce the volume of consumers inappropriately referred to an IVA or PTD.

Annex 3

Description of the Sampling and Inferential Approach Applied to Firm Selection and File Reviews.

1. Following feedback to CP21/30, we concluded our evidence base could be supplemented through further file reviews. On the advice of an independent expert statistician, we used a sampling method called 'Acceptance Sampling with double sampling' to infer whether each firm was giving non-compliant advice at a level that would indicate it is or is not adequately managing the conflict of interest (COI) created by referral fees. We applied 'Acceptance Sampling with single sampling' at the segment level to infer whether or not there were enough firms inadequately managing the COI in a segment to infer it was likely all firms in the market segment were failing to manage the COI.

2. We used case files from CP21/30, the additional case files reviewed by our Authorisations function, and case files from a sample of 5 firms from categories that were underrepresented in our original CBA to make these inferences.

3. We explain below how we produced the criteria for this process, then executed it. Figure 6, at the end of the annex, is an overview of the process.

Determining the number of firms to sample

4. To assess whether or not a segment of debt packager firms is adequately managing the COI, we select a sample of firms from the segment and assess a sample of their case files. As we cannot assess all the firms in the market, we make inferences about the firms we do not sample based on the ones that we do. The strength of these inferences is determined by the number of firms that we choose to sample from the segment. To decide how many firms to sample, we calculated the 'acceptance number' (explained below) and proportion of the segment that we would need to sample to ensure we are likely to reject the segment if more than half the firms in it are failing to adequately manage the COI and accept the segment if only a few were failing to adequately manage the COI (as in this case, our proposed intervention would be unlikely to be the most suitable one).

5. We already had a full census of Large Principal and Large Solo firms, so on the advice of our independent expert statistician we concluded that we did not need to sample any more from those segments. Sampling a further 2 firms from the Small Principal segment and 3 from the Small Solo segment in the October 2022 sample took our combined MFW, Authorisations and October 2022 sample to:

- 5 Small Solo firms (2 from the 2021 MFW work, 3 from October 2022 file reviews) out of a total of 20
- 1 Large Solo firm (1 from the 2021 MFW work), out of a total of 1
- 2 Large Principal firms (2 from the 2021 MFW work), out of a total of 2

- 4 Small Principal firms (2 from Authorisations work and 2 from the October 2022 file reviews) out of a total of 7

Determining appropriate 'acceptance numbers' of firms for each segment

6. We set a segment-level 'acceptance number' for these samples. This is the number of failing firms, at or below which we would accept the segment and infer the firms in the segment are likely to be managing the COI adequately, and those that aren't are anomalies rather than typical. The acceptance numbers were:

- **Small solo: if 2 or fewer firms out of 5 failing then accept the segment**. Under these testing conditions, if in total fewer than 5 out of the 20 firms in the segment are failing, then we are extremely likely (in excess of the 95% confidence level) to accept the segment. If more than 10 out of the 20 firms are failing, we are more likely than not to reject it. If more than 15 out of the 20 are failing, we are extremely likely (in excess of the 95% confidence level) to reject the segment
- **Small principal: if 2 or fewer firms out of the 4 are failing then accept the segment.** Under these testing conditions, if in total fewer than 3 out of the 7 firms in the segment are failing, we will definitely accept the segment. If more than 5 out of the 7 firms are failing then we will definitely reject the segment. If more than 4 are failing, then we are more likely to reject than accept the segment.

Acceptance and rejection criteria

7. Having established how many firms to sample, and appropriate 'acceptance numbers' for each segment, we establish a process for determining whether or not an individual firm is adequately managing the COI. First, we take an initial sample of 6 files per firm and review them for non-compliant advice. There are 3 possible outcomes:

- The number of non-compliant records is equal to or below a firm level acceptance number (0 out of 6 non-compliant). We therefore infer it is highly likely the firm is adequately managing the COI.
- The number of non-compliant records is equal to or above a firm level rejection number (3 out of 6 non-compliant). We therefore infer it is highly likely the firm is failing to adequately manage the COI.
- The number of non-compliant records is between the firm level acceptance and rejection numbers (1 or 2 out of 6 non-compliant). We are unable to infer whether the firm is adequately managing the COI or not. In this case, we take a second sample of 6 customer records. We combine the first and second samples and compare the number of compliant and non-compliant records to another, higher, threshold (2 out of 12 non-compliant).
  - If non-compliance is in excess of this threshold, then we conclude it is highly likely the firm is failing to adequately manage the COI,
  - if not, then we cannot conclude the firm is failing to adequately manage the COI.

8. As we do not have the resources to review every case file for a firm (usually a firm deals with hundreds or thousands of customers), we make inferences about the advice we don't review, based on the advice that we do. The more files we review the more certain we can be that the files we have seen are reflective of all the advice the firm has given. However, the marginal benefit of reviewing more files decreases as the number of files reviewed increases – ie our certainty ***increases*** by a smaller and smaller amount as the number of files we review increases, to the point where reviewing more files has a negligible effect on certainty. We therefore choose a number of files to review that ensures we can make conclusions with a high degree of certainty but not disproportionately burden us or the firms we are requesting files from by requesting more files than is necessary to make robust conclusions.

Acceptance thresholds

9. We chose the number of files we will review, the rejection and acceptance numbers, and the second acceptance number (used if the second sample of 6 is taken) in this review to optimise the certainty with which we will accept a firm where non-compliance in its full book of cases is below a specific low level (an Acceptable Quality Level, AQL), and reject a firm where non-compliance in its full book of cases is above a specific higher level (Lot Tolerance Percent Defective, LTPD).

10. We determined the AQL (lower level) and the LTPD (higher level) by modelling the highest level of non-compliance that would lead to consumers being better off under the status quo than our intervention (see section Methodology for estimating appropriate AQL and LTPD thresholds). By varying the assumptions about the value and harm debt packagers create we can estimate a lower or a higher level of non-compliance at which a debt packager is causing more harm to consumers than benefit, and our intervention would therefore be net beneficial to consumers.

11. Our rationale is that a low level of non-compliance might be tolerable as debt packagers benefit some individuals by giving good advice or reaching those who would not have received advice without debt packagers' marketing. We varied our assumptions about the proportion of customers who would lose debt advice under our proposals (the drop-out rate), and the average cost/benefit of receiving non-compliant advice relative to compliant advice, to produce more and less conservative estimates. Specifically:

- **The (lower level) AQL threshold of 8%** non-compliant customer records comes from assuming **5% of debt packager customers lose debt advice under our proposals** and that on average **non-compliant debt advice is worse than no advice**. Non-compliance at a rate greater than this means the debt packager is causing more harm than good, given our prior assumptions. Given these are our least generous assumptions about the value of debt packagers, if we find non-compliance less than this level it is very likely the debt packager is creating a net-benefit in the real world.
- **The (higher level) LTPD threshold of 47%** non-compliant customer records comes from assuming that **15% of customers lose debt advice under our proposals** and that on average **non-compliant advice is better than no advice, but not as beneficial as compliant advice**. Under these assumptions, non-compliance at a rate more than this will result in the debt packager creating more

harm than benefit. Given these assumptions are very generous about the value debt packagers create relative to the harm they cause, it is very likely that a firm with a higher non-compliance rate than 47% is causing more harm than benefit in the real world.

12. The AQL and LTPD thresholds (8% and 47% non-compliance across all the firm's files respectively) are set to ensure we are likely to accept firms who are causing more benefit than harm and reject firms that are doing more harm than benefit. For firms between the thresholds, the likelihood of us rejecting them increases as the level of non-compliance across their population of referrals increases.

Methodology for estimating appropriate AQL and LTPD thresholds

13. We cannot quantify the harm from non-compliant advice and benefit from compliant advice accurately as the contexts and outcomes are varied and difficult to predict. Therefore, we produced modelling based on a wide range of assumptions to find appropriate AQL and LTPD levels. We recognise neither scenario explained below is likely to be completely accurate, but the accurate estimate for a non-compliance threshold past which a debt packager is causing more harm than benefit is very likely to sit within the bounds of the two scenarios.

14. We have estimated appropriate thresholds by considering a baseline which is the current state of the market, and an alternative which is the debt advice market under our proposal.

15. Under the baseline:

- ***N*** people get debt advice through debt packagers (52,000 in 2019/20).
- ***m*** is the proportion that are referred to non-fee-paying solutions, mainly NfPs (57%, totalling 30,000),
- **1 – *m*** (43%, totalling 23,000) are referred to a fee-paying solution.
- ***x*** is the proportion of those referred to fee-paying solutions, that are given non-compliant advice, and
- **1 – *x*** is the proportion referred to fee-paying solution that are given compliant advice
- ***z*** is the cost/benefit of non-compliant advice.

16. Those given compliant advice realise their maximum net benefit vs a baseline of no advice (= 1). As we are not assessing the compliance of referrals to non-fee-paying solutions, we take the conservative assumption that a referral to a non-fee-paying solution allows the consumer to realise as much of their potential benefit as a compliant referral (i.e. benefit = 1). Those given non-compliant advice incur a benefit or costs which can be represented as a portion of the benefit of compliant advice $z \times 1$.

17. If $0 < z < 1$ then non-compliant advice gives a benefit that exceeds getting no advice, but it is smaller than the benefit from compliant advice. If $z < 0$, then non-compliant advice puts the consumer in a worse position than were they to have not been advised at all. Therefore, the net benefit/cost to consumers under the baseline is:

$$mN + (1-x)(1-m)N + (1-m)Nz$$

18. where:

- ***mN*** – total benefit for consumers referred to non-fee-paying solution
- **(1 – *x*)(1 – m)*N*** – total benefit for consumers compliantly referred to fee-paying solutions
- **(1 – *m*)*Nz*** – total benefit/cost for those non-compliantly referred to fee paying solutions

19. Under our proposal, we would expect debt packagers not to continue in their current business model. This means a portion of those consumers that would've been given debt advice by a debt packager will go straight to an NFP or commercial debt management firm and receive compliant advice. A portion receive no advice. We expect this portion to be small as debt packagers serve a small portion of the market. Further, MaPS are executing a strategy to increase pro-active engagement with customers, and we are conducting our own work with creditors to make efficient and effective referrals to debt advice. We represent this as:

- ***y*** is the proportion of consumers that would not receive debt advice as a result of debt packagers not continuing in their current business model, this is the drop-out rate.
- **1 – y** is the proportion of consumers that would've been debt packager customers, but instead go straight to an NFP or commercial debt provider under our proposal.

20. Therefore, the total benefit for consumers under our proposal is $(1 - y)N$

21. We consider the outcomes for a consumer on a scale between realising none of the benefits of debt advice as 0 and realising their maximum potential benefit through compliant advice as 1. The net benefit/cost to consumers of our proposal relies on 2 assumptions:

- the proportion that receives no advice, but would've if debt packagers had been operating (the drop-out rate): ***y***
- the benefit/cost of non-compliant advice relative to no advice and compliant advice: ***z***

For the net benefit of our proposal to exceed baseline net benefit:

net benefit under proposal > net benefit under baseline:

$$(1 - y)N > mN + (1 - x)(1 - m)N + x(1 - m)Nz$$

$$x > \frac{y}{(1 - m - z + mz)}$$

22. Where ***x*** is the threshold level of non-compliance, if measured non-compliance exceeds

$$\frac{y}{(1 - m - z + mz)}$$

then our policy would be net beneficial under our assumptions about ***y***, ***m*** and ***z***.

23. We estimate two scenarios with more and less conservative assumptions. We believe these higher and lower estimates cover a range within which we could reasonably expect to find the true drop-out rate and true relative value of a non-compliant referral. These ranges come from knowledge gathered through interaction with the firms and consumers in the sector, and other stakeholders such as consumer bodies and firms in related sectors.

24. In both scenarios, we assume the proportion of consumers referred to non-fee-paying solutions is the level we measured in 2019/20, and that both a referral to a non-fee paying solution and accessing debt solutions directly through an NFP or commercial debt packager allow consumers to realise their maximum potential benefit, as in both cases there is no conflict of interest. Based on our judgement, formed through interaction with stakeholders in the sector, in the more conservative scenario we assume:

- ***y*** = 15%, this portion of people would no longer receive any debt advice as a result of our intervention
- ***z*** = 25%, non-compliant debt advice is an average better than no debt advice, as it allows consumers to realise, on average, a quarter of the benefit of compliant debt advice
- This yields a non-compliance threshold of ***x* = 47%**

25. Given these assumptions, non-compliance would need to exceed 47% in paid referrals for our proposal to be net beneficial to consumers.

26. In the less conservative scenario, we assume:

- y = 5%, this portion of people would no longer receive any debt advice as a result of our intervention
- z = – 50%, non-compliant debt advice is on average worse than no debt advice, as it costs consumers the equivalent of half the amount, they would benefit from compliant debt advice. For example, if a compliant referral could benefit a consumer £1000 relative to no advice, then a non-compliant referral would cost them -£500 relative to no advice.
- This yields a non-compliance threshold of ***x* = 8%**

27. We recognise that the threshold will increase if we have underestimated the drop-out rate, or the value of non-compliant advice, however, it is difficult to perceive of a market being beneficial to customers if half of the recommendations it is making are non-compliant with our rules.

Conclusions on segments' compliance

28. Having conducted a review of the firms' files using assessment criteria consistent with the Authorisations file reviews and the 2021 MFW file reviews, and applied the acceptance sampling methodology, we use the results to draw conclusions about compliance in the segments to which the firms belong. We can infer either the structure of the debt packager referral fee-based business model is such that the failure to adequately manage the conflict of interest is a consequence of the referral-fee based

business model in the given segment, or it is likely the firms we sample are anomalous in their failure to adequately manage the conflict of interest (if any do fail), and others in the segment may be managing adequately.

29. The sampling for the 2021 MFW and the Authorisations reviews did not follow the same process described here, so the number of files sampled per firm differs compared to the October 2022 sample. However, the files at these firms were chosen at random, and a significantly high proportion of the files at each firm (100% of the Authorisations reviewed files and 90% of the 2021 MFW files) were found to show evidence of non-compliance. This proportion well exceeds the threshold to conclude the firms are very likely to be failing to adequately manage the conflict of interest when we apply the same criteria we applied to conclude this in the October 2021 sample. Therefore, on the advice of our independent expert statistician, we included these firms in our evidence base and concluded they were failing to adequately manage the conflict of interest created by referral fees.

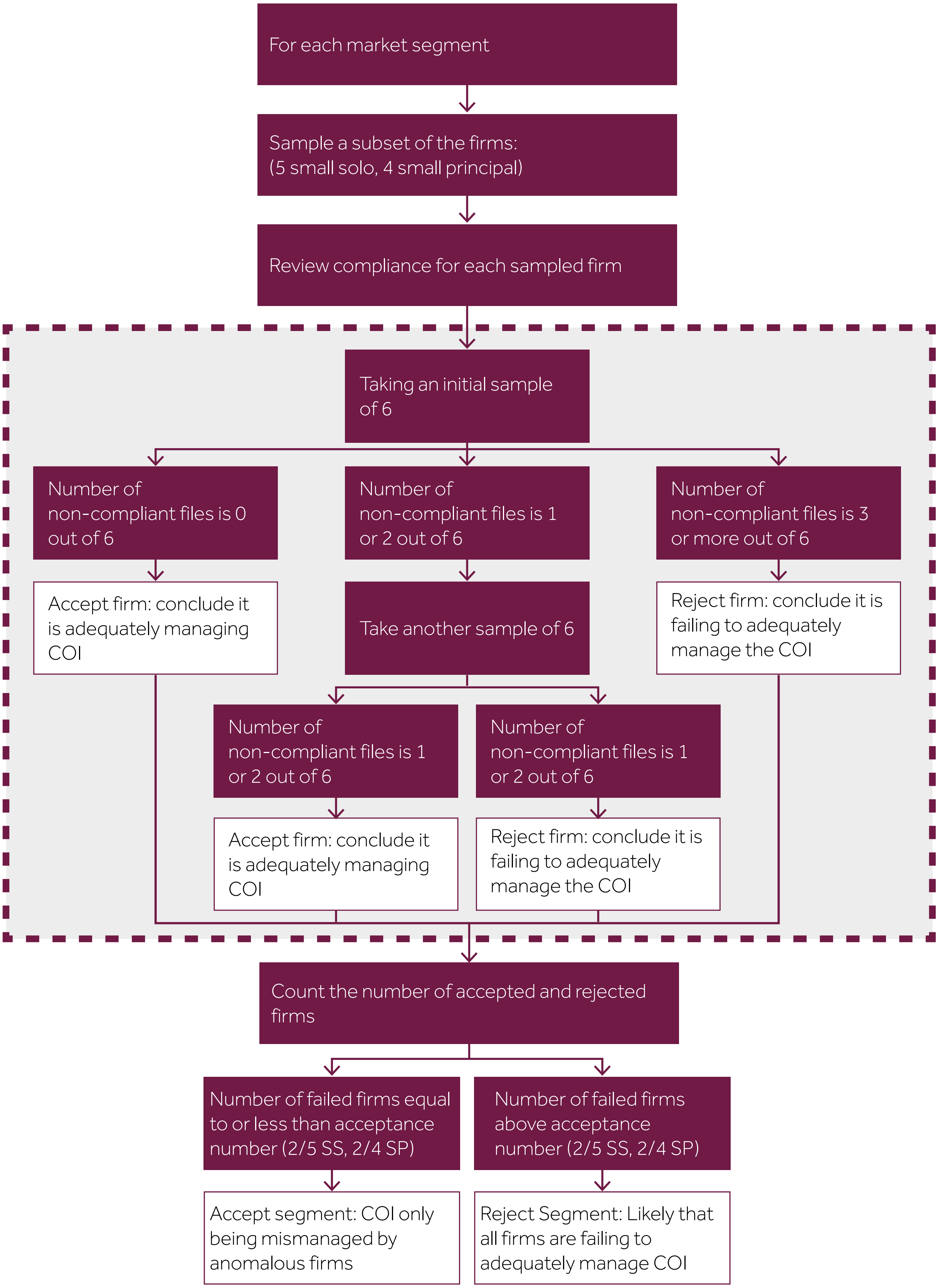
30. We combined the results of the October 2022 file reviews with the 2021 MFW and Authorisation reviews and assessed against the segment acceptance number. All of the files reviewed from the 2 firms in the Small Solo segment and the 2 firms in the Small Principal segment were non-compliant, so we concluded they were both failing to adequately manage the COI.

31. In the October 2022 sample we found the following:

- **Small Solo Firm 1: 8 non-compliant files out of 8 files reviewed**. The firm provided us with 2 extra files due to miscommunication. We decided to review these 2 extra files, as there is a risk there could evidence of misconduct. The firm exceeded the rejection threshold.
- **Small Solo Firm 2: 5 non-compliant files out of 12 files reviewed:** In our initial sample of 6 we found 2 non-compliant files, triggering a second sample of 6. We found 3 of this 6 were non-compliant. The firm exceeded the rejection threshold.
- **Small Solo Firm 3: 5 non-compliant files out of 6 reviewed:** The firm exceeded the rejection threshold.
- **Small Principal firm 1: 4 non-compliant files out of 6 reviewed:** The firm exceeded the rejection threshold
- **Small Principal firm 2: 4 non-compliant files out of 6 reviewed:** the firm exceeded the rejection threshold

32. **5 out of 5 firms in small solo** (3 from the October 2022 sample, and 2 from the 2021 MFW) and **4 out of 4 firms in small principal** (2 from the October 2021 sample and 2 Authorisations reviews) **exceeded the rejection threshold**. Therefore, we inferred there was significant failure to adequately manage the conflict of interest (and therefore significant consumer harm) in these segments.

Figure 6 Overview of Acceptance Sampling Process



Annex 4

Compatibility statement

Compliance with legal requirements

1. This Annex records the FCA's compliance with a number of legal requirements applicable to the proposals in this consultation, including an explanation of the FCA's reasons for concluding that our proposals in this consultation are compatible with certain requirements under the Financial Services and Markets Act 2000 (FSMA).

2. When consulting on new rules, the FCA is required by section 138I(2)(d) FSMA to include an explanation of why it believes making the proposed rules is (a) compatible with its general duty, under s. 1B(1) FSMA, so far as reasonably possible, to act in a way which is compatible with its strategic objective and advances one or more of its operational objectives, and (b) its general duty under s. 1B(5)(a) FSMA to have regard to the regulatory principles in s. 3B FSMA. The FCA is also required by s. 138K(2) FSMA to state its opinion on whether the proposed rules will have a significantly different impact on mutual societies as opposed to other authorised persons.

3. This Annex also sets out the FCA's view of how the proposed rules are compatible with the duty on the FCA to discharge its general functions (which include rule-making) in a way which promotes effective competition in the interests of consumers (s. 1B(4)). This duty applies in so far as promoting competition is compatible with advancing the FCA's consumer protection and/or integrity objectives.

4. In addition, this Annex explains how we have considered the recommendations made by the Treasury under s. 1JA FSMA about aspects of the economic policy of His Majesty's Government to which we should have regard in connection with our general duties.

5. This Annex includes our assessment of the equality and diversity implications of these proposals.

6. Under the Legislative and Regulatory Reform Act 2006 (LRRA) the FCA is subject to requirements to have regard to a number of high-level 'Principles' in the exercise of some of our regulatory functions and to have regard to a 'Regulators' Code' when determining general policies and principles and giving general guidance (but not when exercising other legislative functions like making rules). This Annex sets out how we have complied with requirements under the LRRA.

The FCA's objectives and regulatory principles: Compatibility statement

7. The proposals set out in this consultation are primarily intended to advance the FCA's operational objective of securing an appropriate degree of protection for consumers. In considering the proposals set out in this consultation, we have had regard to the 8 matters listed in s.1C(2)(a)-(h) FSMA on consumer protection.

8. The proposals are intended to protect consumers from the risk of seeking debt help from non-compliant sources of debt advice that are not in their best interests. We want to reduce the harm to consumers from being wrongly recommended debt solutions and in particular IVAs and PTDs as a result of such advice. We want to protect consumers by enabling them to access compliant debt advice more quickly, reducing the risk of disengagement from their debt recovery journey.

9. We consider these proposals are compatible with the FCA's strategic objective of ensuring that the relevant markets function well because they aim to remove a business model which delivers a consistently poor quality service. Consumers face considerable barriers in their capacity to assess the quality of the service provided, including information asymmetry. This was explained in detail in CP21/30 and is further explained in our CBA. For the purposes of the FCA's strategic objective, "relevant markets" are defined by s. 1F FSMA.

10. In formulating these proposals, we have had regard to the importance of taking action intended to minimise the extent to which it is possible for a business carried on (i) by an authorised person or a recognised investment exchange; or (ii) in contravention of the general prohibition, to be used for a purpose connected with financial crime (as required by s. 1B(5)(b) FSMA). We do not consider that this is relevant to our proposed rules and guidance.

11. As with CP21/30, in preparing the proposals set out in this consultation, the FCA has had regard to the regulatory principles set out in s. 3B FSMA.

The need to use our resources in the most efficient and economic way

12. As well as delivering the appropriate degree of consumer protection, our proposals to tackle the underlying business model risks of debt packager firms would enable us to avoid a resource-intensive cycle of supervision and enforcement activity. We can focus our resources on addressing issues in debt advice firms which do not have the same underlying incentives driving non-compliance but could benefit from our intervention to raise their advice standards.

The principle that a burden or restriction should be proportionate to the benefits

13. As we explained in CP21/30 and set out in this CP as well, although this measure is interventionist, we consider it to be proportionate given the evidence of poor practice and misaligned incentives seen in this sector and absence of effective alternatives. We explain our assessment of the costs and benefits of intervention more fully in our CBA.

The desirability of sustainable growth in the economy of the United Kingdom in the medium or long term

14. We do not consider that these proposals are relevant to sustainable economic growth. The debt packager sector is too small to have any significant impact on to economic growth.

The general principle that consumers should take responsibility for their decisions

15. To take responsibility for their decisions in relation to debt solutions, consumers need to be provided with appropriate, compliant advice. These proposals support the principle that consumers should take responsibility for their decisions by reducing the risk that consumers access poor quality advice that fails to properly inform them of their choices.

The responsibilities of senior management

16. We warned the senior management of debt packager firms in our Dear CEO letter and subsequent Portfolio Letter that they needed to ensure they managed the conflict of interest inherent in their business. Our subsequent evidence gathering, including most recently in 2022, has led us to conclude that the incentives created by referral fees are too strong for senior management to ensure these risks are effectively managed.

The desirability of recognising differences in the nature of, and objectives of, businesses carried on by different persons including mutual societies and other kinds of business organisation

17. We explain in Chapters 2 and 4 why we are excluding not-for-profit debt advice organisations from the scope of our proposals.

The desirability of publishing information relating to persons subject to requirements imposed under FSMA, or requiring them to publish information

18. We do not consider that this relevant to these proposals.

The principle that we should exercise of our functions as transparently as possible

19. This consultation paper, together with CP21/30, sets out our evidence and rationale for the proposals.

Expected effect on mutual societies

20. The FCA does not expect the proposals in this paper to have a significantly different impact on mutual societies.

Compatibility with the duty to promote effective competition in the interests of consumers

21. In preparing the proposals as set out in this consultation, we have had regard to the FCA's duty to promote effective competition in the interests of consumers. Under the competition duty, if we have more than one option available to us that will deliver the necessary protection, then we should choose the most pro-competitive option – but here other options are deemed to not provide adequate protection (and the competition duty does not require us to choose a more pro-competitive option if it does not achieve the protection sought). As effective competition must be promoted "in the interests of consumers", we consider the proposed intervention to be in line with the competition duty.

Equality and diversity

22. We are required under the Equality Act 2010 in exercising our functions to 'have due regard' to the need to eliminate discrimination, harassment, victimisation and any other conduct prohibited by or under the Act, advance equality of opportunity between persons who share a relevant protected characteristic and those who do not, to and foster good relations between people who share a protected characteristic and those who do not.

23. As part of this, we ensure the equality and diversity implications of any new policy proposals are considered. The outcome of our consideration in relation to these matters in this case is stated in paragraphs 2.63-2.67 of the Consultation Paper.

Annex 5

List of non-confidential respondents to CP21/30

Advice NI

Association of British Credit Unions Limited

Basis Insolvency

Benjamin Hughes

Building Societies Association

Capital Credit Union

Citizens Advice Scotland

Colin Preston

CreditFix

Debt Movement UK Limited

Debt Managers Standards Association Limited

Eriko James

Financial Services Consumer Panel

Gillian Nuttall

Harper McDermott Limited

Institute of Chartered Accountants of England and Wales

Institute of Chartered Accountants of Scotland

Insolvency Practitioners Association

Jubilee Debt Campaign / Centre for Responsible Credit

Money Advice Scotland

Money Advice Trust

Money Matters Leicester

MoneyPlus Group

No.1 Copperpot Credit Union

Promethean Finance Limited

R3

Sara Williams

Scotwest Credit Union

StepChange

Superior Insolvency Solutions

TDX Group Limited

The Mortgage Expert

Totemic

UK Finance

Annex 6
Abbreviations used in this paper

Abbreviation	Description
AR	Appointed Representative
CBA	Cost Benefit Analysis
CEO	Chief Executive Officer
COI	Conflict of interest
CONC	Consumer Credit sourcebook
CP	Consultation Paper
DAS	Debt Arrangement Scheme
DRO	Debt Relief Order
DMP	Debt Management Plan
DP	Debt Packager
FCA	Financial Conduct Authority
FSMA	Financial Services and Markets Act 2000
IP	Insolvency Practitioner
IS	Insolvency Service
IVA	Individual Voluntary Arrangement
I&E	Income and Expenditure
MaPS	Money and Pensions Service

Abbreviation	Description
MFW	Multi-firm work
NFP	Not for profit
PTD	Protected Trust Deed
SDRP	Statutory Debt Repayment Plan

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

All our publications are available to download from www.fca.org.uk.

Request an alternative format

Please complete this form if you require this content in an alternative format.

Sign up for our **news and publications alerts**

Appendix 1
Draft Handbook text

CONSUMER CREDIT (DEBT PACKAGER REMUNERATION FROM DEBT SOLUTION PROVIDERS) INSTRUMENT 2023

Powers exercised

A. The Financial Conduct Authority ("the FCA") makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137A (General rule-making power);
(2) section 137T (General supplementary powers); and
(3) section 139A (Power of the FCA to give guidance).

B. The rule-making provisions listed above are specified for the purposes of section 138G(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on [*date*].

Amendments to the Handbook

D. The Consumer Credit sourcebook (CONC) is amended in accordance with Annex A to this instrument.

Amendments to the material outside the Handbook

E. The Perimeter Guidance manual (PERG) is amended in accordance with Annex B to this instrument.

Citation

F. This instrument may be cited as the Consumer Credit (Debt Packager Remuneration from Debt Solution Providers) Instrument 2023.

By order of the Board
[*date*]

Annex A

Amendments to the Consumer Credit sourcebook (CONC)

In this Annex, underlining indicates new text.

8 Debt advice

…

8.3 Pre contract information and advice requirements

…

8.3.8 G …

Prohibition on debt packager remuneration from debt solution providers

Scope

8.3.9 R (1) *CONC* 8.3.11R to *CONC* 8.3.15R:

(a) apply to a *firm* with respect to *debt counselling* where the *firm* does not itself provide *debt solutions*; and

(b) do not apply to a *firm* that is a *not-for-profit debt advice body*.

(2) A *firm* is treated as not itself providing *debt solutions* for the purposes of *CONC* 8.3.9R(1)(a) where the *firm*:

(a) provides *debt solutions* on a single or occasional basis; and/or

(b) receives only an insignificant amount of its total annual revenue from providing *debt solutions*.

Context, purpose and anti-avoidance

8.3.10 G (1) *Firms* are reminded that when referring *customers* to *debt solution* providers, or carrying on related services, a *firm* must comply with its obligations under:

(a) *Principle* 12 (Consumer Duty) to act to deliver good outcomes for *retail customers* and/or *Principle* 6 (Customers' interests) to pay due regard to the interests of its *customers* and treat them fairly, subject to the date *CONC* 8.3.9R to *CONC* 8.3.17G come into force; and

(b) *CONC* 8.3.2R(1) to ensure that all advice given and action taken by the *firm*, its agent or its *appointed representative*:

(i) has regard to the best interests of the *customer*;

(ii) is appropriate to the individual circumstances of the *customer*; and

(iii) is based on a sufficiently full assessment of the financial circumstances of the *customer*.

(2) The purpose of the prohibition in *CONC* 8.3.11R is to remove the conflict of interest between a debt packager's obligations under *CONC*, including those referred to in *CONC* 8.3.10G(1), and the financial incentive to act in a way which generates revenue in the form of referral fees from *debt solution* providers.

(3) The effect of *CONC* 8.3.9R(2) is that *firms* will not be able to avoid the prohibition in *CONC* 8.3.11R by starting to provide a small number of *debt solutions* for that purpose.

(4) For the purposes of *CONC* 8.3.9R(2)(b), the amount of total annual revenue received from providing *debt solutions* is unlikely to be considered significant if an undue risk of non-compliant debt advice arising out of a conflict of interest of the kind described in *CONC* 8.3.10G(2) continues to exist.

Prohibition

8.3.11 R (1) A *firm* must not (and must take all reasonable steps to ensure that none of its *associates*, or its *appointed representatives*):

(a) enter into an agreement to receive;

(b) solicit or accept; or

(c) seek to exercise, enforce or rely on rights or obligations under an agreement to receive,

any commission, fee or any other financial consideration, directly or indirectly, from a *debt solution* provider in connection with the *firm* referring *customers* to a *debt solution* provider, or any other related services, except as provided in *CONC* 8.3.14R.

(2) *CONC* 8.3.11(1)(b) and (c) do not apply where the *firm* has an accrued contractual right to payment for the referral, or related services, in relation to a *customer* prior to the coming into force of *CONC* 8.3.11R(1).

8.3.12 R 'Related service(s)' for the purposes of *CONC* 8.3.9R to *CONC* 8.3.11R includes:

(1) recommending a *debt solution* provider;

(2) providing *debt counselling* services to *customers* prior to those *customers* being referred to a *debt solution* provider or entering into a *debt solution*; and

(3) providing *debt counselling* services to *customers* who have been referred to the *firm* by a *debt solution* provider.

8.3.13 R '*Debt solution* provider(s)' for the purposes of *CONC* 8.3.10G to *CONC* 8.3.12R includes such providers' *associates* and *appointed representatives.*

8.3.14 R *CONC* 8.3.11R does not apply to payments made:

(1) pursuant to an enactment;

(2) in relation to the administration by a 'money adviser' approved under The Debt Arrangement Scheme (Scotland) Regulations 2011 of a *customer*'s application for a Debt Arrangement Scheme under those Regulations; or

(3) by a person employed as an officer of:

(a) (in relation to England and Wales) the Insolvency Service;

(b) (in relation to Scotland) the Accountant in Bankruptcy; or

(c) (in relation to Northern Ireland) the Insolvency Service.

Record keeping

8.3.15 G *Firms* are reminded of their obligations in *SYSC* 9.1.1R to keep orderly records, which must be sufficient to enable the *FCA* to monitor the *firm's* compliance with the requirements of the *regulatory system*.

Application of the prohibition to appointed representatives

8.3.16 R *Principals* which have an *appointed representative* to whom *CONC* 8.3.9R(1) would apply if the *appointed representative* were an *authorised person* must take all reasonable steps to ensure that such an *appointed representative* complies with *CONC* 8.3.11R as if the references in that *rule* to '*firm*' applied to such an *appointed representative*.

8.3.17 G The purpose of *CONC* 8.3.16R is to prevent a debt packager *firm* from becoming an *appointed representative* in order to avoid *CONC* 8.3.11R applying to it and continuing to be conflicted by the financial incentive to act in a way which generates revenue from *debt solution* providers.

Annex B

Amendments to the Perimeter Guidance manual (PERG)

In this Annex, underlining indicates new text.

2 Authorisation and regulated activities

…

2.9 Regulated activities: exclusions applicable in certain circumstances

…

Insolvency practitioners

…

2.9.26	G	These exclusions apply to a *person* acting as an insolvency practitioner. The term "insolvency practitioner" is to be read with section 388 of the Insolvency Act 1986 or, as the case may be, article 3 of the Insolvency (Northern Ireland) Order 1989. The exclusions relating to *debt adjusting*, *debt counselling* and *providing credit information services* also apply to any activity carried on by a *person* acting in reasonable contemplation of that *person's* appointment as an insolvency practitioner. In relation to *debt counselling*, insolvency practitioners may find *PERG* 17.7 helpful, including examples 12, 13 and 13A.

…

17 Consumer credit debt counselling

…

17.7 **Examples**

Q7.1 Please give me some examples of what is and is not debt counselling

Please see the following table. All the examples assume that the advice or information relates to debts under a *credit agreement* or a *consumer hire agreement* or to a group of debts that include such debts.

Examples of what is and is not *debt counselling*	
Example	Explanation
…	

(13) A *person* recommends that a debtor obtains advice from a particular *debt counselling firm*, ABC Debt Management.	Taken on its own it is not *debt counselling* because the adviser is advising the debtor to obtain advice from another adviser. However, if ABC Debt Management only offers one debt solution (e.g. a debt management plan), the referral could constitute a recommendation intended implicitly to steer the debtor in the direction of that particular debt solution and, therefore, could be advice (in which case it would be *debt counselling*). Consequently, whether or not *debt counselling* is involved will depend on the individual circumstances in each case and is likely to involve a consideration of the process as a whole.
(13A) A *person* recommends that a debtor obtains advice from a particular insolvency practitioner or their *firm*.	Taken on its own it is not *debt counselling* because the adviser is advising the debtor to obtain advice from another adviser. However, where the insolvency practitioner or their *firm* only offers advice in relation to a particular *debt solution* (e.g. an individual voluntary arrangement or a protected trust deed), the referral could constitute a recommendation intended to implicitly steer the debtor in the direction of that particular *debt solution* and, therefore, could be advice (in which case it would be *debt counselling*). Consequently, whether or not *debt counselling* is involved will depend on the individual circumstances in each case and is likely to involve a consideration of the process as a whole.

Pub ref: 007973

FINANCIAL
CONDUCT
AUTHORITY

12 Endeavour Square London E20 1JN
Telephone: +44 (0)20 7066 1000
Website: www.fca.org.uk