

For the attention of: Malcolm Le May, Chief Executive Officer

19 April 2021

Dear Sirs/Madam

Provident SPV Limited (the "Company") – Proposed Scheme of Arrangement pursuant to Part 26 of the Companies Act 2006 (the "Scheme")

- 1.1 We refer to the Company's application to the High Court of Justice of England and Wales for an order for permission to convene a meeting of certain of the Company's creditors for the purpose of considering and, if thought fit, approving (with or without modification) the Scheme. The convening hearing is, as we understand it, due to take place on Thursday, 22 April 2021.
- 1.2 We are writing to the Company in view of this forthcoming hearing, specifically, to draw to the attention of the Company the FCA's position in respect of the Scheme.
- 1.3 In summary, the FCA's position in respect of the Scheme is as follows:
 - (a) the Group has stated that it no longer proposes to provide support to the Lenders to pay redress claims in full to customers. Therefore, the alternative if the Scheme does not proceed is that the Lenders would enter insolvency proceedings, in which customers are very likely to receive less (if any) payment in respect of their compensation claims. Given this alternative, the FCA is not opposing the Company's application for leave to convene meetings to vote on the Scheme. However, the FCA does not support the Scheme for the reasons set out in this letter and the FCA does not believe that the Scheme is the fairest compromise that could have been offered to customers with valid redress claims by the Group;
 - (b) on the basis of the information currently available to it, the FCA is not currently proposing to take any immediate regulatory action that might otherwise prevent the Scheme from having substantial effect were it to be agreed by the requisite majority of creditors and sanctioned by the Court, but is reserving its position to, if appropriate, take such action in the future; and
 - (c) noting the FCA's consumer protection objective in securing an appropriate degree of protection for consumers (s.1C Financial Services and Markets Act 2000 ("FSMA")), and its integrity objective to protect and enhance the integrity of the UK financial system (s.1D FSMA), the FCA has identified significant concerns with the Scheme which it would like to draw to the attention of the Company.
- 1.4 We expand upon these aspects further below in sections 4 and 5.
- 1.5 The FCA intends to appear by counsel at the convening hearing to make submissions in respect of the Scheme. As soon as practicable after the convening hearing on 22 April, we propose to publish this letter on the FCA's website. The FCA considers that it is appropriate for it to provide this letter given:
 - (a) its position as the relevant regulator (for certain entities within the Group) whose views may therefore be considered by the Court to be at least potentially relevant;

- (b) the fact that the FCA's position may be relevant to the question of whether the Scheme can have substantive effect; and
- (c) the FCA's consumer protection function which the FCA considers means that it is appropriate that it should express relevant concerns in case Scheme Creditors, who are consumers, are not in a position to do so.

1.6 The FCA notes that the issues identified below are more likely to be relevant to the consideration of whether the Scheme ought to be sanctioned, rather than whether or not a convening order should be made. However, the FCA considers that it is likely to be helpful for its concerns to be identified at the present stage, rather than waiting until the sanction hearing before raising these issues.

1.7 Please note that unless otherwise defined, capitalised terms have the meaning ascribed to them in the draft Scheme.

2. **THE FINANCIAL CONDUCT AUTHORITY'S ROLE**

2.1 It is customary for regulated firms to request a "letter of non-objection" from the FCA in respect of any scheme of arrangement they intend to propose. Provident Financial plc (the "**Group**" or "**Provident**") initially requested a "letter of non-objection" in respect of the Scheme. Following initial feedback from the FCA on the Scheme, Provident subsequently withdrew this request.

2.2 Nevertheless, as part of its usual supervisory functions, the FCA has considered and continues to assess the Scheme and its terms, as the Scheme has evolved.

2.3 At all times, the FCA has considered the Scheme by reference to the FCA's statutory objectives under FSMA, which for ease, are enclosed with this letter (Annex 1). As part of this, pursuant to the consumer protection objective, the FCA is duty-bound to seek to secure an appropriate degree of protection for consumers and to ensure the UK financial system is sound, stable and resilient. In this case, the Group's business involved providing door-step lending with high interest loans to persons likely to have experienced financial difficulties, many of whom may therefore be vulnerable persons. To give an indication of the nature of the loans offered, we note that Provident currently states on its website that the representative annual percentage rate in relation to the loans it offers is in the range of 299.3% to 1,557.7% APR (variable). It is therefore especially important that the Scheme is designed as simply as possible, is openly and clearly explained, and that it works as a customer might expect, i.e. to provide redress as proposed by the Scheme.

2.4 The Company has provided to the FCA copies of the draft Scheme documentation, including the Scheme document, the Explanatory Statement and the Company's evidence in support of the Scheme. As appropriate, the FCA has also made formal requests of the Group to provide additional information and documents in relation to the proposed design, implementation, costs and likely outcome of the Scheme, particularly in relation to customers to whom redress may be payable.

3. **THE FCA'S APPROACH TO ASSESSING THE SCHEME**

3.1 The FCA's general approach and background on the Group is set out in more detail in Annex 2.

3.2 The FCA's assessment of the Scheme is distinct from, and potentially broader than, the Court's assessment of the Scheme (in considering whether to convene a meeting of the Company's creditors for the purpose of considering and, if thought fit, approving the Scheme, and to ultimately sanction the Scheme).

3.3 As part of its consideration to date, the FCA has had regard to:

- (a) information and documents provided by the Company (as above);
 - (b) the FCA's wider knowledge of the Company, the Group and its business; and
 - (c) the FCA's experience of similar proposals and/or arrangements in respect of other regulated consumer credit businesses
- (together, the "**Scheme Characteristics**").

4. **THE FCA'S ASSESSMENT OF THE SCHEME**

4.1 The FCA has completed its assessment of the Scheme Characteristics and does not support the Scheme. Taken as a whole, the FCA considers that the Scheme Characteristics may not be compatible with the FCA's rules, principles and strategic objectives. In particular, the FCA is concerned that:

- (a) customers with valid redress claims stand to receive significantly less than the value of their claims; and
- (b) the methodology for assessing claims does not produce outcomes with the same high standards of accuracy and fairness as would be available under the FCA's usual framework of complaint handling rules for firms or through recourse to the Financial Ombudsman Service.

4.2 Noting the FCA's integrity objective to protect and enhance the integrity of the UK financial system, the FCA also has significant concerns about schemes of arrangement being used to circumvent paying customers their full redress entitlement. However, the FCA recognises that these are ultimately matters for the FCA to assess and, in a given case, determine whether any action could or should be taken against any regulated entities within the Group as a result and that these concerns need to be balanced against the likely position should the Scheme not go ahead and the proportionality of it taking action in such circumstances.

4.3 As such, while the FCA continues to reserve its position should facts or circumstances change, the FCA confirms, on the basis of the information currently before it, that it does not presently anticipate taking any immediate regulatory action that might specifically prevent the Scheme from having substantial effect (were the Scheme to be agreed by the requisite majority of creditors and sanctioned by the Court). However, the Group should note that the FCA is considering whether the firm continues to meet threshold conditions and may take further action if appropriate.

4.4 Separately, the Company will be aware that in March 2021 the FCA launched an investigation into PPC's conduct, focusing on the consideration of affordability and sustainability of lending to customers, as well as the application of a Financial Ombudsman Service ("**FOS**") decision into the Company's complaint handling process, in the period between February 2020 and February 2021. The start of the investigation period relates to the FOS decision which was taken in February of last year. Although the ongoing investigation is in its early stages all possible outcomes are available to the FCA, including closing the investigation with no further action, a public censure, a penalty, redress, the removal of permissions and/or restriction of activities. It is too early to say how long this investigation will take, but typically investigations take at least 12 to 18 months for the FCA to reach a conclusion.

5. **THE COURT'S ASSESSMENT OF THE SCHEME**

5.1 The FCA has also identified several issues which the FCA considers are relevant, or potentially relevant, to customers if and when they are asked to evaluate and vote on the Scheme, and to the Court when considering whether or not to sanction the Scheme.

A. Contribution of other stakeholders

- 5.2 We note that Provident Financial plc will make available to the Company the Compensation Fund in the amount of £50 million. While the material contribution from the Company's shareholders is welcome, and we understand the amount of funding for the Scheme should take into account the Group's capital adequacy requirements, we believe that there may be scope for the Group to increase the level of funding to the Scheme, in turn increasing the expected return to Scheme Creditors.
- 5.3 This assessment is based on the information, including forecasts provided to the FCA in January/February, with a limited update provided on 16 April. In light of the limited information in the update, and noting the limited time we have had to review it, our considerations include, in particular:
- (a) the FCA understands that the Group intends to increase lending across the Group (by 30%-50% over the next three years) by increasing the size of its credit card business within Vanquis Bank Limited, increasing the size of its Moneybarn motor financing business and by growing the new lending proposition to £55m-£300m (net of impairments). The Group expects to have the capital and wholesale funding required for this growth. The FCA is concerned that the focus is only on new business, with resultant profits generated over time to shareholders, without seeking to address the known liabilities (in particular redress liabilities to consumers) that have arisen from past business;
 - (b) the FCA considers that the Group's anticipated growth in lending over the next three years, and which is factored into its determination of the Compensation Fund amount, could reasonably be reduced, which would in turn reduce the funding requirements of the Group over that period. By way of example, on the information available we note that reducing the lending growth rate from 15% to 10% would reduce funding requirements by £150 million and a reduction to 5% would reduce funding needs by £300 million, a proportion of which may then be available for the Compensation Fund. If strong demand becomes apparent at a lower rate of lending then this could be used as evidence to support additional growth funded via the capital markets; and
 - (c) the FCA has assessed the effect of the assumed impairment rate on overall impairment charges and notes impairment rates in excess of 58% for the new CCD business which may give rise to questions about its future viability. The FCA notes, by comparison, that the impairment rates for Vanquis Bank and MoneyBarn are less than 30%. On the basis that the new CCD business will be lending to customers with a lower risk of default the FCA is concerned that the modelling of future impairment may understate long-term expected collections which will drive the future return to shareholders.
- 5.4 Related to the amount of the Group's contribution to the Compensation Fund, as at the date of this letter, the FCA is continuing to explore with the Group whether executive remuneration is, or could potentially, adversely impact consumer outcomes within the Scheme. The FCA will be considering, for example, whether management remuneration is structured in a way that encourages good conduct and is consistent with our expectations that both variable remuneration and long term incentive plans contain provisions which ensure that there will be appropriate consequences where customers have received poor outcomes and we will continue to review this with the Group.
- 5.5 Separately, in circumstances where the Redress Creditors are anticipated to receive a very small fraction of their Redress Claims under the Scheme, the FCA is concerned that the claims of the other unsecured creditors of PPC and Greenwood Personal Credit Limited will not be similarly compromised (or compromised at all) and indeed are expected to be kept whole.

B. Claims methodology

- 5.6 The FCA acknowledges that the Company has sought to incorporate in the claims methodology a means of addressing the fact that the Company does not have credit reference agency data for a significant number of customers. However, the FCA remains concerned that the claims methodology does not fully and adequately address this deficiency and therefore a risk remains that a customer for whom no credit reference agency data is held will be treated differently to a customer for whom credit reference agency data is held.

C. Voting on the Scheme

- 5.7 While the FCA understands that the Company will seek to proactively determine the likely validity of creditor claims for voting purposes, it remains unclear to the FCA (i) whether a customer could vote on the Scheme potentially irrespective of whether that customer actually has a Redress Claim, and (ii) whether the weighting applied to a Redress Creditor's vote by reference to a certain percentage of their net compensation is a fair basis on which to calculate voting values. Each of these factors could potentially create an incongruity between Redress Creditors and the customers who in fact voted on the Scheme; in other words, some customers may vote on the Scheme when they are not, in fact, Redress Creditors, and may be given a vote weighting disproportionate to the actual value of their claim.

D. Equitable set-off and Transferred Loans

- 5.8 The FCA is concerned that some customers may be worse off compared to in an insolvency. The FCA remains concerned about customers with outstanding loan balances and valid redress claims who do not engage with the Scheme at all within the requisite time periods, noting in consumer schemes of this nature response rates can be low. Those customers therefore lose their rights in return for no compensation and are potentially worse off than they would be in an immediate insolvency counterfactual. This is because the effect of the Scheme will be to release any right those customers have to assert equitable set off rights in relation to their redress claims in respect of outstanding balances and will therefore be pursued for the full amount of their loan balance in future.
- 5.9 By contrast, in any insolvency counterfactual, we anticipate such rights would be taken into account by any insolvency officeholder when adjudicating claims and applying mandatory insolvency set off as no bar date would exist which would deprive creditors of their rights to set-off. In addition, we anticipate the existence of equitable set off rights would in practice prevent those customers from being pursued for their outstanding loan balances in an insolvency (up to the value of their redress claims) or by any subsequent purchaser of the debt.
- 5.10 Separately, the FCA understands that, under the Scheme, a customer who has a Transferred Loan (i.e. a loan that has been sold to a Debt Purchaser) will not automatically receive a reduction of the balance of such loan by the amount of their Redress Claim unless the Company first enters into a Balance Reduction Agreement with the applicable Debt Purchaser in respect of the relevant loan. To the extent no such agreement is ever entered into by the Company, a customer will continue to owe the full amount of their outstanding balance to the Debt Purchaser – a balance which would otherwise have been reduced in whole or in part had such loan not been sold to the Debt Purchaser. The FCA welcomes the fact the release given by Scheme Creditors under the Scheme carves out any rights of equitable set off that a Scheme Creditor who submits a Scheme Claim by the Claims Submission Deadline may have against the Lenders or any other person (allowing a Scheme Creditor to assert equitable set off as a defence to a debt enforcement claim brought by a Debt Purchaser or person other than the Company or the Lenders). However, the FCA remains concerned that certain customers are nonetheless at risk of being prejudiced in future simply because their loan happens to have been sold to a Debt Purchaser, because (i) such customers would have to assert their rights to equitable set-off, which in practice they may not be aware of; and (ii) as noted above in paragraph 5.8, in the event that such

a customer does not submit a claim by the Claims Submission Date, the Scheme purports to release their rights of equitable set-off.

E. The Company as a special purpose vehicle

- 5.11 In order to effect the Scheme, the Group incorporated the Company to assume joint liability (by deed poll) for all liabilities capable of being claimed against each of the Lenders under the Scheme solely for the purpose of proposing the Scheme.
- 5.12 The FCA acknowledges that such a structure (or similar) has been used in other schemes of arrangement that have been sanctioned by the Court and may in this case be considered necessary for the Company in order to overcome other contractual restrictions on the Group. However, the FCA remains concerned by the use of such a structure in this specific case. In particular, the FCA is concerned that customers – whom it should be noted are involuntary creditors of Provident – may be confused by a scheme proposed by a company with which they have never contracted (or even heard of), but which they may now be owed redress by, and through which they will also release their claims against the other Group entities. In the context of the Scheme the FCA considers that the artificiality of the special purpose vehicle structure may unfairly override the legitimate interests of the Group's customers; the fact that the use of a special purpose vehicle may be necessary for the Group does not mean it is appropriate or fair for its customers.

6. CONCLUSION

- 6.1 The FCA's observations and comments above are referable to the position as we understand it to be, as at the close of business on 19 April 2021. To the extent that things have further evolved by the convening hearing on 22 April 2021 we would expect the Company to update the Court accordingly. The FCA will continue to liaise with the Company ahead of the convening hearing as required and, if necessary, will write to the Company again in due course as things develop.

Yours faithfully,

Sheldon Mills
Executive Director of Consumers and Competition

ANNEX 1:

The FCA's statutory objectives under FSMA 2000:

1. The FCA's strategic objective is: ensuring that relevant markets function well (see s.1B(2) FSMA 2000). 'Relevant markets' includes the markets for regulated financial services (see s. 1F FSMA 2000).
2. The FCA's operational objectives are the consumer protection objective; the integrity objective and the competition objective (s.1B(3) FSMA 2000).
3. The FCA's consumer protection objective is securing an appropriate degree of protection for consumers (s.1C FSMA 2000). In considering what degree of protection for consumers may be appropriate the FCA must have regard to:
 - a. the differing degrees of risk involved in different kinds of investment or other transaction;
 - b. the differing degrees of experience and expertise that different consumers may have;
 - c. the needs that consumers may have for the timely provision of information and advice that is accurate and fit for purpose;
 - d. the general principle that consumers should take responsibility for their decisions;
 - e. the general principle that those providing regulated financial services should be expected to provide consumers with a level of care that is appropriate having regard to the degree of risk involved in relation to the investment or other transaction and the capabilities of the consumers in question;
 - f. the differing expectations that consumers may have in relation to different kinds of investment or other transaction;
 - g. any information which the consumer financial education body has provided to the FCA in the exercise of the consumer financial education function;
 - h. any information which the scheme operator of the ombudsman scheme has provided to the FCA pursuant to section 232A.
4. The integrity objective is: protecting and enhancing the integrity of the UK financial system (s.1D FSMA 2000). The integrity of the UK financial system includes:
 - a. its soundness, stability and resilience,
 - b. its not being used for a purpose connected with financial crime,
 - c. its not being affected by behaviour that amounts to market abuse,
 - d. the orderly operation of the financial markets, and
 - e. the transparency of the price formation process in those markets.
5. The competition objective is: promoting effective competition in the interests of consumers including in the markets for regulated financial services or services provided by a recognised investment exchange in carrying on regulated activities in respect of which it is by virtue of section 285(2) exempt from the general prohibition (s.1E FSMA 2000). The matters to which the FCA may have regard in considering the effectiveness of competition in the market for the services mentioned above include:

- a. the needs of different customers who use or may use those services, including their need for information that enables them to make informed choices,
- b. the ease with which consumers who may wish to use those services, including consumers in areas affected by social or economic deprivation, can access them,
- c. the ease with which consumers who obtain those services can change the person from whom they obtain them,
- d. the ease with which new entrants can enter the market, and
- e. how far competition is encouraging innovation.

ANNEX 2:

Background on the Company and the FCA's role

1. The Company is a limited liability company established on 2 November 2020 for the purposes of the Scheme and is a member of the Provident group of companies under (and including) Provident Financial plc. Certain entities in the Group (including Provident Personal Credit Ltd ("**PPC**")) are authorised by The Financial Conduct Authority (the "**FCA**") to engage in certain regulated activities. Greenwood Personal Credit Limited previously traded under interim permissions, which lapsed in 2015. As a result, the FCA is or was the conduct regulator of certain Group entities under the Financial Services and Markets Act 2000 ("**FSMA**").
2. Provident first contacted the FCA in September 2020 to discuss its proposals in relation to the Scheme. Since that time, the FCA and Provident, and their respective legal advisors Ashurst and Clifford Chance, have been engaged in regular discussions regarding the Company's proposals and the key aspects of the Scheme, including importantly, how customers (borrowers and guarantors, past or present) will be affected .

The FCA's approach to considering schemes of arrangement in general:

3. The FCA has a duty (s.1B FSMA 2000) in discharging its general functions, to act, in so far as is reasonably possible, in a way which is compatible with its strategic objective and which advances one or more of its operational objectives (see Annex 1). The FCA's general functions include determining the general policy and principles by reference to which it performs particular functions under FSMA 2000 including the policy and principles by which it will carry out its functions in relation to arrangements for the supervision of the firms which the FCA regulates, and in particular the functions of considering what, if any, representations to make to the Court in relation to arrangements proposed by an FCA-regulated firm, and also the FCA's functions in responding to consultation requests from the PRA.
4. The FCA also has a separate duty to discharge its general functions in a way which promotes effective competition in the interests of consumers, in so far as that is compatible with acting in a way which advances the consumer protection objective or the integrity objective (s1B(4) FSMA 2000).
5. As part of its normal risk-based and judgement-led approach to supervision, the FCA will assess, taking account of all relevant circumstances of a particular case, whether a scheme proposed by an FCA-regulated firm poses any threat to any of the FCA's operational objectives, to its duty to promote competition described in paragraph 4 above, or threatens to be inconsistent with its strategic objective.
6. The FCA will consider whether the scheme proposal is compatible with FCA rules, including the FCA's Principles for Businesses (enclosed at Annex 3). In particular, the FCA assesses the compatibility of schemes of arrangement with Principle 6 (treating customers fairly), Principle 7 (customers' information needs) and Principle 8 (managing conflicts of interest).

ANNEX 3:

FCA Principles for Businesses

1 Integrity	A firm must conduct its business with integrity.
2 Skill, care and diligence	A firm must conduct its business with due skill, care and diligence.
3 Management and control	A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
4 Financial prudence	A firm must maintain adequate financial resources.
5 Market conduct	A firm must observe proper standards of market conduct.
6 Customers' interests	A firm must pay due regard to the interests of its customers and treat them fairly.
7 Communications with clients	A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.
8 Conflicts of interest	A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client.
9 Customers: relationships of trust	A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment.
10 Clients' assets	A firm must arrange adequate protection for clients' assets when it is responsible for them.
11 Relations with regulators	A firm must deal with its regulators in an open and cooperative way, and must disclose to the FCA appropriately anything relating to the firm of which that regulator would reasonably expect notice.