THE DEPUTY LEADER OF THE HOUSE OF LORDS

The Baroness Neville-Rolfe
House of Lords
London
SW1A 0PW

2 March 2021

Dear Lady Neville-Rolfe,

Thank you for your ongoing engagement with the Financial Services Bill. During the Grand Committee debate on Monday 22 February, you asked what the Government is doing to support smaller financial services firms. I committed to write to you to set this out.

The Government is committed to ensuring that the financial services sector supports competition, allowing new firms to compete and grow. As you know, both the FCA and the PRA have a statutory objective to promote effective competition.

The Government has taken action to improve competition in banking by assisting smaller lenders, making it easier for new providers to compete effectively. The Small Business, Enterprise and Employment Act 2015 contained two policies achieve this goal.

The first requires the major banks to refer small and medium-sized enterprises (SMEs) they reject for finance, with the SME's permission, to 'finance platforms' that can match SMEs with alternative finance providers. This enables businesses that are viable, but do not fit the risk appetite of the traditional banks, to access the finance from alternative lenders like challenger banks and peer-to-peer platforms.

The second policy improves access to SME credit information by requiring that the same banks share information on their SME customers with other lenders through designated Credit Reference Agencies. This has improved the ability of challenger banks and alternative finance providers to conduct accurate risk assessments and, by levelling the playing field between providers, makes it easier for SMEs to seek a loan from a lender other than their bank.

And the Government is committed to ensuring that smaller innovative firms can grow to their true potential. The FCA launched its regulatory sandbox in 2015, for example, the first of its kind globally. This sandbox enables businesses to test innovative propositions with customers, improving the range of services and products available to UK consumers. The FCA also recently launched a new Digital Sandbox to allow early stage firms to access data that enables them to further develop their innovative ideas.

Finally, in February this year, the Kalifa Review of UK FinTech presented a wide-ranging strategy and delivery model to build on its existing attractiveness to start-up firms and become the best place for a fintech business to reach global scale.

The Government is also committed to a proportionate approach to regulation, and to only regulating where there is a clear case for doing so, in order to avoid putting additional costs on financial services firms. This is particularly true in the case of smaller financial firms, where the Government recognises that unnecessary regulatory burdens would inevitably lead to higher costs for their customers.

One good example of our commitment to proportionality is the Investment Firms Prudential Regime that will be introduced by the Bill. It will a introduce a more proportionate regime for non-systemic investment firms, which are currently regulated under rules designed for banks. The new regime will ensure that prudential requirements for investment firms are proportionate to the risks they pose to the financial system, thereby facilitating healthy competition across the industry and allowing the UK to remain competitive outside of the EU.

In prudential policy, since leaving the EU and gaining the opportunity to tailor our approach to the UK market, we are already seeing the PRA make decisions that do this, while ensuring that we maintain high standards. This includes, for example, the changes that the PRA has made to its regulation of maximum distributable amounts to improve the usability of capital buffers, and not implementing requirements for Intermediate Parent Undertakings in our transposition of the EU's Fifth Capital Requirements Directive (CRDV).

Over a slightly longer timeframe, the PRA will be able to consider how best to set more proportional requirements for smaller lenders. This should take the form of a holistic, consistent and well consulted approach. The PRA's 'strong and simple' approach to future regulation represents the best opportunity to fulfil these criteria.

With these actions to support smaller firms, it should come as no surprise that under this Government, smaller UK financial services firms have grown the fastest of any firms within the sector – significantly increasing their market share over the past 5 years.

I hope that you will find this information useful. I am copying this letter to all those who spoke in the committee debate on Monday, and I am placing a copy of this letter in the Library.

Yours sincerely,

Yours sincerely,
Frederick Howe

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