The LSB's Information for Practitioners

The Standards of Lending Practice for business customers – Asset Finance

Governance and oversight

May 2020

This document has been produced by the LSB and provides non-exhaustive examples of the approach Registered Firms (Firms) may wish to take into consideration when seeking to adhere to the Standards of Lending Practice for business customers (the Standards) on governance and oversight.

Registered Firms must be able to demonstrate to the LSB that they are adhering to the Standards of Lending Practice; however the LSB does not monitor compliance with the content of this document and as such, it is not intended to be prescriptive nor binding on Registered Firms. The LSB acknowledges that each Firm will have its own way of demonstrating that it is adhering to the Standards without the need to refer to, or take account of, the content of this document.

Where a reference to made to the Consumer Credit Act 1974, as amended (the CCA), the Consumer Credit Sourcebook (CONC), other Financial Conduct Authority (FCA) requirement or wider legislation, the examples or suggestions which follow represents the LSB's view on how the Standard could be achieved.

Customer outcome: business customers will receive a fair outcome when taking out a credit product and throughout the whole customer lifecycle, wherever the interaction with the customer takes place.

Firms will achieve this: with processes, controls and governance arrangements that ensure that there is effective senior management oversight of the Firm's achievement of the customer outcomes contained in the Standards of Lending Practice for business customers.

1. Firms should have adequate governance, policies, processes, management information and controls to enable effective oversight of adherence to standards and delivery of fair customer outcomes.

Typical areas for Firms to consider are:

- Is the fair treatment of customers embedded within the culture of the Firm?
- Is there executive accountability for conduct/customer?
- Is there clear accountability for the achievement of the Standards and outcomes at an executive level, and is their effective oversight to ensure that any delegation of responsibility remains effective?
- Do the Board/senior management have a clear line of sight of risks and issues relating to adherence to the Standards and outcomes?
- Is adherence to the Standards and achievement of outcomes subject to committee oversight and challenge?
- Are there policies in place for areas covered by the Standards of Lending Practice that are subject to effective oversight?
- Where responsibilities have been assigned for the achievement of the Standards and outcomes, are these clear and understood?
- Are there processes in place covering all aspects of the Standards with process owners?
- Are there controls to ensure the Standards of Lending Practice are being achieved, and are these tested for design and operational effectiveness?
- Are control owners defined?
- Is there a mechanism for assessing the Firm's adherence to the high level principles?
- Is there adequate management information relating to areas covered by the Standards available to senior management:
    - To enable the right decisions to be made;
    - To enable any issues to be identified or risks mitigated; and
    - To ensure that achievement of outcomes is effectively monitored and measured?

2. Firms should have an effective risk management framework appropriate to the size of the Firm to ensure that the Standards of Lending Practice are achieved.

Typical areas for Firms to consider are:

- Is there a clear separation between first, second and third lines of defence, albeit proportionate to the Firm's size and complexity, with clearly defined roles, responsibilities and accountabilities?
- Are the plans across all three lines of defence appropriately aligned to minimise the risk of gaps and duplication?
- For smaller Firms, is the split between first line monitoring, second line oversight and third line assurance sufficiently split to enable senior management to obtain an independent view on the design and operational effectiveness of the controls relating to processes and systems covered by the Standards of Lending Practice?
- If assurance work is outsourced, is there management of the outsourced activity from within the Firm?
- Is this separation clearly articulated in risk management policies and understood by the senior committee representatives and senior management?
- Is there clear reporting from each line into a senior level risk or audit committee, which covers risks, controls and issues relating to the Standards of Lending Practice?
- Is there a control risk self-assessment process in place, with an effective challenge process in place, and results escalated?
- Where risks or issues are flagged, is there a process for assessing them against defined criteria, prioritising them, reporting them and escalating them in accordance with the risk profile to a senior committee for oversight and actions assigned?
- Where actions are raised to mitigate risks or address issues, is there a process for assigning actions, prioritising them and tracking them through to completion?
- Is an assessment undertaken, once an action is complete, to ensure that the action has mitigated the risk or addressed the issue and whether any further activity is needed?

3. Firms should ensure that their employees are adequately trained to deliver the Standards of Lending Practice's customer outcomes, and that any incentive schemes are driving the right behaviours to ensure fair customer outcomes.

Typical areas for consideration are:

- If the culture is one focused on customer outcomes, does this filter through to the recruitment process and the training and development framework?
- Does the training framework focus on areas covered by the Standards of Lending Practice?
- Is root cause analysis undertaken from issues raised through monitoring, quality assurance work and complaints, including agents?
- Is there a mechanism for feeding in training requirements for employees and agents with prioritisation given for areas impacting customer outcomes?
- Is regular feedback provided to employees on performance, capturing areas covered by the Standards, and identifying areas for improvement?

- If there is an incentive scheme in place, including at third parties, has this been assessed to ensure it drives good customer outcomes and does it have appropriate quality thresholds?
- Are any incentive schemes, including those at third parties, monitored to ensure that it is driving the right behaviours?
- Is the performance of incentive schemes, including those at third parties, overseen by an appropriate committee (rewards/conduct)?

4. Firms should have systems in place to ensure that the Firms' employees and agents are promoting products in a clear and transparent way.

Typical areas for consideration are:

- Is there a consistent approach to training employees, based on the job role and their role requirements?
- Is there an induction programme for new starters, which using a blend of training techniques, encourages a consistent and baseline understanding of products and services offered by the Firm?
- Does the training use a blend of classroom and on the job training to provide hands on experience? This could include a mix of soft and technical skills to support all learning styles and to maximise information retention.
- Are there supporting material or tool-kits to support employees and agents in promoting the products available to a customer, clearly and transparently?
- Is there a formal framework for staff training and competency, setting out the core competencies of the job role and knowledge?
- Are there mechanisms in place to ensure individual competencies are reviewed and attested on an ongoing basis?
- Is there a process for ensuring that employee weaknesses or failings are underpinned by a suitable action plan designed to address them?
- Are there processes in place to ensure employees are supervised on an ongoing basis? Are the outputs of this used to support the implementation of training and the ongoing assessment of competence?
- Is there a cultural focus on delivering fair customer outcomes, and are there mechanisms in place to review and assess the quality and delivery of fair customer outcomes?
- Is there a process for capturing customer feedback?
- Are there metrics or key indicators in place which may highlight instances where products have not been promoted in a clear and transparent way such as data on product retention rates, customer complaints or account dormancy?

5. Firms should have systems in place to ensure that any failure to adhere to the Standards of Lending Practice are identified and assessed for materiality and root cause. Where the materiality threshold is met, these are reported to the LSB and remediated in a timely manner.

Typical areas for consideration are:

- Is there a system for capturing any failures to meet one of the Standards, or achieve one of the outcomes?
- Are employees and third party agents trained on the elements of the Standards of Lending Practice and how to identify and report a 'failing'?
- Is there a clear escalation process that employees are aware of for reporting any 'failing'?
- Are failings assessed for materiality (refer to the LSB's guide to breach management) and is this assessment reviewed and challenged?
- Is there a process for ensuring that all failings are underpinned by a suitable action plan designed to address them?
- Is there a process for ensuring that any failings that trigger the materiality threshold are reported to the LSB?
- Does second line compliance oversee the materiality assessment?
- Once an action plan has been documented, is there clear accountability for the actions?
- Are overdue items identified promptly, and is there a process for reporting those at an appropriate level? Are extended dates challenged and is there an appropriate level of sign off?
- Where actions have been completed, is there a process of validation to ensure that the actions have fully addressed the failing and is there a sign-off by the first line owner and second line?
- Is there a clear reporting process for any failings at local level, and is root cause analysis undertaken on failings to identify improvements to policy, process, systems or a training need?
- Are failings further assessed to establish whether a series of smaller failings can be aggregated to point to a more systemic and significant failing?
- Is management information produced to identify trends from breaches that have occurred and improve systems and processes, including the prevention of further recurrence?
- Is there a clear escalation process to ensure that appropriate management information and details of failings, actions and progress against due dates are highlighted to conduct/customer committees and then on to the key risk and audit committees?
- Is the breach management process overseen by operational risk/second line and is there additional oversight from second line compliance for those relating to areas such as the Standards?
- Does internal audit periodically review the breach management process?

6. Firms should have processes in place to identify when changes to the Standards of Lending Practice are made and to ensure that these are effectively incorporated within policies, processes and systems.

Typical areas for Firms to consider are:

- Does horizon scanning take place to ensure that changes in regulation are taken into account and assessed for impact on policies, processes and systems?
- Is there a process for communicating regulatory change to relevant parts of the business, and are there business owners who have responsibility for taking necessary action?
- Is a materiality assessment undertaken with sufficient priority afforded to those items required to meet the Standards?
- Is there a change management process in place to enable the change to be implemented in a timely manner?
- Is there a process for ensuring that the required change has been implemented satisfactorily?
- Is there a post implementation review to ensure that the change has been embedded and is operating as expected?
- Is there a level of second line oversight of the change process and independent third line assurance?

7. Firms should ensure that when systems or processes are changed, or products are introduced or changed, the impact on meeting the Standards of Lending Practice is adequately assessed.

Typical areas for Firms to consider are:

- Where products, systems or processes are changed, or a new product is developed, is there a formal change management framework in place that ensures that the change takes full account of any impact on compliance with the Standards, across all business areas, with appropriate prioritisation based on a full materiality assessment?
- Is there a sign-off process at key stages to ensure that the work is satisfactorily completed before moving to the next phase of development?
- Is there a process for communicating change promptly within the Firm and to relevant third parties?
- Is there clear accountability for managing the change including implementation, staff training, testing and reporting at the Firm and, where applicable, the third party?
- Is there second line oversight and challenge of projects in transit and third line independent assurance?
- Post change implementation, does training take place for staff members at the Firm and, where applicable, at the third party to understand the changes?
- Before go live and post change implementation, is there adequate testing to ensure that the changes have been successful and that regulatory requirements have been met, including the right customer outcomes, both at the Firm and, where relevant, at the third party?

- Is regular reporting produced and reviewed by all relevant people to ensure any potential weaknesses in the new process are identified and dealt with promptly either at the Firm or, where relevant, at the third party?

8. Firms should ensure that the product design stage takes into account internal and external risks which could impact upon a customer's ability to maintain their repayments so that new products do not lead to unsustainable borrowing.

Update to take account of measures introduced by the Government to support lending to SMEs impacted by the Covid-19 pandemic.

HM Government has established the Coronavirus Business Interruption Loan Scheme (CBILS) to support the continued provision of finance to SMEs throughout the Covid-19 pandemic. It is recognised that registered firms are prepared to support business customers experiencing disruption caused by the coronavirus pandemic, and in doing so may be prepared to offer products, including asset finance products, under CBILS in reliance on the Government guarantee under the scheme.

It is recognised that by participating in the Government scheme firms may not be able to apply in full effect all provisions within this section of the Standards as certain aspects of the products are determined by the Government, and as such firms have a limited or no role in the design of products.

Given this firms cannot reasonably be expected to apply the provisions of paragraph 8. to the design of products offered under CBILS as the parameters of the products are set out by the Government.

Typical areas for Firms to consider are:

- Are all key stakeholders involved in the product review process (e.g. product, channels, marketing, customer operations (including collections), customer experience, second line risk functions (operational, credit and compliance), finance)?
- Is there an appropriate level of oversight and challenge, proportionate to the organisation, of the product design and review cycles?
- Is there an assessment of internal and external risks which may impact on the customer's ability to maintain product repayments to help ensure that new products do not lead to unsustainable borrowing?
- Is the target market identified and is this monitored post-launch?
- Are product features, and their operation, reviewed both pre- and post-launch to ensure they are, and remain, fit for purpose?
- Is product performance data taken into account as part of the design and review stage, for example:
    - accounts which operate within the terms of the product versus those that breach them, and any identifiable trends, such as accounts falling into arrears at an early stage?
    - evaluation of the ease of access for customers via the relevant sales channels?
    - customer research to test the understanding and usefulness of the proposed product and features?

    - application decline rates and the associated rationale for these?
- Are wider economic factors taken into account (for example, changes in regulation within specific markets, potential Bank of England base rate changes, inflation rates) to assess the impact these may have on the ability of customers to service the account?
- Do the product design and cyclical product reviews take into consideration customer feedback from a range of sources such as customer satisfaction surveys and complaints?
- Does the product design framework include regular reviews to ensure the product is being accessed, sold and operated as expected?
- If, following review, the product is not performing as expected, are appropriate actions implemented and monitored?
- Are customer outcomes assessed when the performance of the products is reviewed to identify any new risks, which can inform any enhancement to product features or delivery?

9. Where part of the credit process/life cycle is outsourced, Firms should:

  a. undertake effective and robust due diligence to ensure that the third party or intermediary can meet the requirements of the Standards of Lending Practice and deliver the required customer outcomes; and

  b. exercise effective ongoing oversight of the third party or intermediary to ensure that it is meeting the Standards of Lending Practice and delivering the required customer outcomes.

Typical areas for Firms to consider are:

- Are there policies and processes for third party outsourcing that cover the management of the third party and oversight arrangements, and the requirement that any regulatory obligations, including the Standards of Lending Practice, are met?
- Are governance arrangements in place to monitor both the on-boarding of new third parties and the performance of existing ones?
- Does the due diligence on a third party include an assessment of conduct risk which focuses on the achievement of customer outcomes and the fair treatment of customers?
- Is there an assurance framework in place proportionate to the Firm that encompasses monitoring and quality assurance of transactions and processes, independent oversight, and independent assurance in respect of third party providers?
- Is there a route for escalation, with clear lines of responsibility, that allows for Standards of Lending Practice related matters to be reported in a timely manner?
- Is there complete, accurate and timely management information and reporting at the appropriate management and risk committees to ensure effective oversight of third parties in respect of meeting the Standards and achieving customer outcomes, including areas such as processing capacity, business continuity arrangements and data protection requirements?
- Is due diligence undertaken on new suppliers that includes how the Firm's regulatory obligations will be met by the third party and the resilience of systems to service the Firm's requirements to achieve the right customer outcomes?

- Does the due diligence include the identification and implementation of robust controls where the third party will sub-contract its services, whether partially or fully?
- Is there a formal signoff process at senior management level before a new supplier is taken on?
- Is there an oversight strategy for third parties, which accounts for the risk that the third party presents to the Firm in meeting its regulatory obligations and achieving the right customer outcomes?
- Are regular assessments undertaken of the adequacy of controls at the third party, through quality assurance and monitoring, to ensure customer outcomes are being achieved and regulatory requirements are being met?
- Is data at third parties adequately safeguarded?
- Is there monitoring and testing of third party's system's integrity, performance and resilience to ensure that the supplier can maintain operations at all times?
- Are third parties subject to relationship management with independent oversight and quality assurance?
- Does internal audit conduct independent third line assurance on the oversight and management of third parties by the Firm?

10. Firms should have a robust complaints management process in place to deal with Standards of Lending Practice-related complaints and to undertake root cause analysis [DISP].

The requirements regarding complaint handling are set out in DISP, Firms should ensure that these requirements are applied to complaints relating to the Standards of Lending Practice.

11. Firms should assign an appropriately skilled and senior individual(s) with clear accountability for overseeing that the Standards of Lending Practice are being adhered to and customer outcomes achieved, and for ensuring that remedial action is instigated where this is not happening.

Typical areas for Firms to consider are:

- Is there an individual in the organisation with clear accountability for ensuring the control framework is in place for meeting the Standards of Lending Practice?
- Has the nominated individual been provided with an appropriate degree of authority to be able to fulfil the role?
- Does the nominated individual have sufficient skills, knowledge and experience of products covered by the Standards of Lending Practice?
- Does the nominated individual have sufficient awareness of what the Standards of Lending Practice are trying to achieve?
- Is the nominated individual independent of first line processes and able to provide effective challenge?
- Is the nominated individual of sufficient seniority:

- to ensure that they have the organisational influence to initiate change to achieve the Standards of Lending Practice;
- to hold the business to account where they feel the Standards are not being achieved;
- to oversee progress of actions designed to meet the Standards and challenge first line senior management if they feel that these are either not on track or will not fully address the weaknesses;
- to present an independent view to senior management/committees on the status of risks, issues and mitigating actions?

- Is the nominated individual recognised across the organisation for the role that they have in respect of the Standards of Lending Practice?