Nationwide Building Society – Written evidence (SCG0019)

Introduction

Nationwide welcomes the opportunity to respond to the Committee's inquiry into the Financial Conduct Authority (FCA) and Prudential Regulation Authority's (PRA) secondary objectives and to comment on how the regulatory landscape can better support growth. As a UK focused organisation, we will not opine in our response on international competitiveness. Instead, we focus on the growth element of the objectives.

Our response covers three areas:

1. Nationwide's perspectives on how regulators have applied the secondary objective and examples of where it is not yet sufficiently embedded.
2. Where the wider regulatory landscape could be better configured to support growth.
3. Specific reforms to better promote growth.

We welcome the Government's emphasis that regulators should be more mindful of growth and the use of metrics and more rigorous cost benefit analyses to measure this. HM Treasury's (HMT) recent remit letters provide strong and practical steers for how regulators can achieve this. There are some examples of the PRA and FCA already working to meet their objectives e.g. Basel 3.1 or the FCA's review of its requirements following the introduction of the Consumer Duty.

Moreover, the Mansion House reforms offer a clear framework for how regulators should support growth. Now that we have that framework, and in the interests of stability, it is important to allow regulators sufficient space to advance their work to support growth. Parliamentary accountability will be important to assess progress. Structured inquiries such as this, which hold regulators accountable to agreed outcomes, are more effective scrutiny than knee jerk pressure in reaction to events.

1. Nationwide's perspectives on how regulators have applied the secondary objective and examples of where it is not yet sufficiently embedded

To help the inquiry and the UK's financial services sector more broadly, we have provided examples of where the secondary objective is not currently sufficiently embedded to promote growth or consistent with the regulators' stated drivers of growth (which are marked in red)

(Innovation) The opportunity cost of a congested regulatory change pipeline

Innovation is a key driver for productivity and growth. However, firms have finite resources to invest to innovate. On a practical level, there are only so many available weekends in a year where major IT change can be implemented. The high volume of regulatory driven change in recent years, particularly in payments, has limited firms' capacity for firm-led innovation to support growth.

For example, UK Finance estimate that the total cost to deliver the payments roadmap over the next five years is between £10bn and £20bn. A survey of their members in 2023 found that over 90% of budgets and resources firms allocate to payments change were consumed by regulator-led projects. In a similar vein, the Garner review on the Future of Payments found that industry had invested an estimated £1.5bn in Open Banking.[1] Each of these projects consumes significant amounts of change resource which could otherwise be devoted to firm-led innovation.

There are also examples of some of these projects being delivered sub-optimally. For example, the New Payments Architecture (designed to upgrade retail payments) ran for eight years, during which time industry spent approximately £150m and invested considerable resources. The project was paused in November 2023 without selecting a vendor.

The Government's new National Payments Vision is a welcome response to this regulatory congestion, and we hope it will lead to a streamlined, better coordinated change pipeline.[2]

(Proportionate regulation) Overly restrictive rules which reduce lenders' ability to support growth and inclusion

The Mansion House speech asked regulators to identify actions to increase the sector's ability to contribute to growth, without reducing financial stability.[3] Its remit letters also asked certain regulators to have regard to "supporting first time buyers (FTBs) who struggle to save for a large deposit."[4]

To that end, there is scope to reform certain rules introduced post financial crisis to expand home ownership and boost economic growth. For example, the Financial Policy Committee (FPC) flow limit on the amount of higher loan to income mortgage lending skews too far towards risk elimination and can limit firms' ability to help FTBs.

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[1] Future_of_Payments_Review_report.pdf
[2] National_Payments_Vision..pdf
[3] Mansion House 2024 speech - GOV.UK
[4] CX_Letter_-_Recommendations_for_the_Financial_Conduct_Authority__FCA__-_Nikhil_Rathi_14112024.pdf

In a similar vein, the FCA's Mortgage Conduct of Business rules (MCOB) can hinder lenders from offering a more innovative mortgage product to meet the needs of today's FTBs. Removing this restriction could reduce payments for FTBs through allowing part repayment/part interest only mortgages. This could enable people to buy a property at a younger age, switching to a full repayment mortgage as their annual earnings increase.

In considering these changes, it is worth noting that the mortgage market has proved highly resilient, and lenders now hold much more capital and loss reserves for mortgage. Despite a series of 'once in a generation shocks' like the financial crisis, the pandemic and cost of living crisis, only 1.08% of homeowner mortgages are in arrears of 2.5% or more of the outstanding balance. Repossessions in Q3 2024 were 87% lower than at the peak of the financial crisis in Q1 2009.[5]

(Operational Efficiency) Disproportionate compliance and supervision burdens which divert resources from being deployed to promote growth.

Research by Oliver Wyman shows that UK ring fenced banks devote 15-20% of their investment budgets to regulation.[6] Responses to the most recent FCA Practitioner Panel Survey found that 28% of firms considered the number of data/information requests received from the FCA to be 'more than necessary' and 50% of firms said that the FCA does not give firms enough time to compile data/information that they request. [7]

This is reflected at Nationwide where we received 4,519 pieces of direct correspondence from our regulators over the past 12 months, in addition to 488 meetings during that period. The FCA alone accounts for 1,950 pieces of correspondence and 106 meetings over that time. Whilst some of this reflects the fact that Nationwide was making an acquisition in the last year, we saw a similar pattern in previous years with 3,687 pieces of correspondence in the same period from 2022-23.

In addition to the high volume of data requests and the significant and sustained level of regulatory interaction, senior individuals at Nationwide have been required to provide 12 personal attestations over the past 12 months. These attestations, formal statements supporting the accountability of these individuals for specific issues or actions, are extremely resource-intensive, and we do not believe such frequent use of this supervisory tool is justified given the clarity of individual accountability already in place under the Senior Manager and Certification Regime.

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[5] Mortgage arrears and possessions Q3 2024 | Insights | UK Finance
[6] Oliver Wyman report: How Banks Can Help to Launch a New Era of Growth
[7] FCA and Practitioner Panel Survey 2023-24 Report

As an example, a recent attestation requested across the industry in relation to account closures required input from 14 teams across Nationwide across a 5-month period to provide the senior management function with appropriate reassurance to give the attestation.

Each of these regulatory interactions requires considerable time and senior management resource. In aggregate, they divert resources and funding from more growth promoting activity.

(Effective competition) Uneven playing field between banks and building societies

Building societies' customer-ownership model allows them to focus on long-term domestic growth, rather than maximising short-term value for external shareholders. Hence, they are well-placed to contribute towards the long-term growth of the UK economy.

However, building societies fall under a different legislative framework to banks.[8] Consequently, they have faced certain arbitrary legislative restrictions which retail banks do not, e.g. building societies are restricted in using derivatives to give customers certainty on costs and lenders confidence on cash flow. Similarly, provisions in the Building Societies Act 1986 (the Act) relating to the funding limit have created challenges for building societies that banks do not face.

Whilst some of these changes have been addressed through the Building Societies Act (Amendment) Act, which updated the original legislation, there is a residual risk that building societies face legislative constraints which banks do not. These can lead to an uneven playing field which reduce their ability to compete. To mitigate this, we would recommend that Parliament undertakes an annual review of the legislative and regulatory framework for building societies, to assess how it compares to bank legislation.

We also welcome the Government's call on the FCA and PRA to produce a report on the mutuals sector landscape and look forward to working with the regulators as they carry out their work. [9]

2. Where the wider regulatory landscape could be better configured to support growth

One of the drivers of growth is proportionate regulation. Compared with other comparable jurisdictions, the UK has a crowded regulatory landscape with eight financial regulators and multiple public bodies, some of which act as quasi-regulators. This is in addition to numerous global

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[8] Building Societies are governed by the Building Societies Act 1986

[9] 20241114_EST_Letter_FCA_Mutuals_Reporting.pdf

standard setters like the Financial Stability Board or SWIFT (the international payments network). Often their remits overlap e.g. CMA, FCA, PSR all had responsibility for Open Banking. Rather than simplify this landscape, the UK has opted for a myriad of memoranda of understanding to manage the complexity.[10]

A prime example of this complexity is the role of the Financial Ombudsman Service (FOS), which has expanded from dispute resolution (as Parliament intended) to quasi-regulation, as its decisions set new standards and policies. These have far-reaching impacts on firms, consumers and the market and aren't subject to proper checks or transparency, given the shortcomings of the Wider Implications Framework, not least the absence of industry involvement in it. This is having a detrimental impact on growth and investment as it creates material uncertainty for firms and can conflict with FCA policies. While we welcome the FCA and FOS' call for input to modernise the redress system we remain concerned about the overall complexity of the system.

The role of the Lending Standards Board (LSB) has been another example of an overcrowded regulatory landscape, with the FCA and other regulators such as the PSR taking on increasing oversight in key areas of the LSB's previously stated scope, such as branch closures and APP scams.

3. Specific reforms to better promote growth

We have set out below several recommended reforms to better embed the growth objective.

A. Increase the Financial Policy Committee limit on higher loan to income lending.

In 2014 the Financial Policy Committee (FPC) introduced a loan to income (LTI) flow limit that stipulates that no more than 15% of a lender's new residential mortgages can have loan to income ratios at or greater than 4.5 times the borrower's income. This limit was intended to mitigate over-indebtedness and, although it has been reviewed, it has not been increased since it was set a decade ago. [11]

There is now a pressing case for at least a modest increase in the limit to reflect changes in the housing market and to reduce the drag on home ownership and growth. Lending above 4.5 times income is essential to help FTBs. With a modest increase in the limit to 20% of new mortgages, we estimate that Nationwide could support around 10,000 more

[10] There are an estimated 13 regulatory MoUs
[11] An FPC Response - Consultation on withdrawal of the affordability test Recommendation | Bank of England

completions per year, the vast majority for FTBs. If the rest of the market took the same approach, this could help an additional 250,000 FTBs to own their own home over the course of a Parliament. With each resale housing transaction producing an average economic benefit of £9,559, this amount of additional activity would stimulate growth.[12]

B. Change the delivery model for UK payments infrastructure

HMT and regulators have a golden opportunity to use the new National Payments Vision to shift the current delivery model to a more streamlined and commercial model. Specifically, this should involve:

a. Rationalising and simplifying the number of change initiatives. We note that the Garner review of payments called for a 10% reduction in 2024.[13]
b. Ensuring that the Open Banking and Open Finance roadmaps transition to a commercial model to incentivise investment in them. Specifically, banks should be able to charge for API related costs which include development costs, liability and any potential margin.
c. Moving to a public-private delivery model for future change initiatives and ensuring that all such initiatives are subject to a rigorous cost benefit analysis.

C. Parliament should undertake an annual review of the legislative framework for building societies to assess to ensure a level playing field with bank legislation

Building Societies operate under a different legal framework to banks and other companies. The Building Societies Act 1986 (the Act) contains the core characteristics of a building society and helps to preserve their unique form. However, there have been examples of the Act falling behind equivalent legislation for banks and imposing arbitrary restrictions on building societies, which can tilt the playing field in favour of banks. These have been rectified by updates to the Act, most recently through the Building Societies Act 1986 (Amendment) Act.[14]

These legislative updates have taken considerable time and effort. For example, the most recent updates where only possible because Julie Elliott, the former MP, was drawn first in the private members bill ballot and took the changes through a private members bill (for which

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[12] knight-frankhbf-economic-benefits-of-housing-market-activity-2020-7616.pdf
[13] Garner Future of Payments Review: Future_of_Payments_Review_report.pdf
[14] Building Societies Act 1986 (Amendment) Act 2024

Nationwide is very grateful). This only passed because it was included in the parliamentary wash up and had the support of Government.

This illustrates how challenging it can be to ensure a level playing field between banks and building societies. Given the Government's manifesto aim to double the size of the mutual sector, we recommend closer parliamentary scrutiny of how the legislative and regulatory framework for building societies compares to banks. For example, the Labour Party's Financing Growth report recommended that "regulators and policymakers to report annually to Parliament on how they have considered the specific needs of mutuals and the need for a level playing field with the wider financial services sector."[15] Parliament should consider adopting this recommendation. Alongside this, we would recommend that when the Companies Act or equivalent legislation is amended, there should be a parallel review of the Building Societies Act to assimilate the legislation.

D. Adopt a more joined-up and proportionate approach to data requests from the regulators and placing supervision in scope of the secondary objective.

As outlined in this submission, regulatory requests for data and information are consuming significant amounts of finite management resource, which could be better directed towards more growth promoting activities like investment and innovation.

We fully understand the importance of data collection but see considerable scope for a more joined up and efficient approach to reduce duplication. Consideration could also be given to including supervision in the scope of the secondary objectives and for regulators to provide more timely feedback on these data submissions.

E. Use the FCA's work on modernising consumer redress to clarify the remit of the FOS to avoid it becoming a quasi-regulator

Certainty and predictability are crucial enablers of growth and innovation, however the material uncertainly caused by the FOS creates uncertainty around regulatory expectations and steers firms towards a zero-risk approach. This stems largely from the nature of FOS's 'fair & reasonable' jurisdiction, which unlike the courts and their system of precedent, is highly unpredictable; and the obligations on firms to apply FOS decisions to non-complainants (giving rise to read across impacts).

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[15] Financing-Growth.pdf

A recent example of this is how the FOS is considering its approach to the Consumer Duty in the context of packaged bank accounts. The FOS thinks that the duty may require personal bank account (PBA) providers to look at whether the customer had used any of the PBA benefits in the preceding year and if not, to prompt them that this may not be the right account for them.

Leaving aside its merits and practicality, this suggestion would go some way beyond the FCA's current guidance in this area. FOS isn't set up to drive such expectations because it only sees complaints and therefore will inevitably have a much narrower and more specific focus than the FCA's 'whole of market' remit. Crucially, FOS also isn't subject to the secondary objectives, nor does it have the same accountability the FCA does.

HMT and the FCA should use the current work, including the recently announced call for input, to modernise consumer redress and to clarify the FOS's role to focus on resolving individual complaints while the FCA handles matters with wider implications. [16]

F. A prevention-based model for fraud and scams

Fraud and scams ruin lives and are a material drag on competitiveness and growth. The latest UK Finance data shows that £570 million was stolen in payment fraud in 2024 alone with the total number of cases rising by 16% in the same period.[17]

The steps outlined by Government, and the Online Safety Act, will help to reduce fraud further but there is an urgency to do more. Everyday thousands more people are falling victim to criminal gangs, and we must implement a preventative model which stops fraud and scams at source.

The Government's pressure on tech and telcos is welcome, but more is needed to prevent harm. Nationwide has called for a National Anti-Fraud and Scams Centre to be established. The Centre will bring together all the relevant actors including those in the financial services, tech and telco sectors. The Centre will be the driving force and focal point for all the activity taking place. By collaborating at an industrial scale, we can act in real-time to prevent fraud and scams.

We also need to look downstream of banks. One trend we have seen recently is an increase in people being tricked into sending funds to crypto wallets that have been setup in their name and then sending the onward

[16] Call for Input Modernising the Redress System
[17] Half Year Fraud Report 2024 | Policy and Guidance | UK Finance

payments to the fraudster from the crypto wallet. Despite the PSR's recent efforts to extend reimbursement coverage, crypto firms typically aren't in scope of its scheme. If they aren't providing a regulated payment service, these firms are also likely to be outside the scope of the FOS complaints scheme.

Conclusion

Nationwide welcomes the chance to respond to the committee's inquiry. We hope this sets out some areas where the secondary objectives could be better embedded and where the focus on growth could be extended to other regulatory actors. We look forward to discussing this with the committee.

29 November 2024