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Funding options available to SMEs.

The SME Alliance was formed in September 2014 to support SMEs “battling against fraud, corruption and misconduct in the financial sector” and to lobby for the fair treatment of businesses by their banks and advisors. This submission is based upon the experiences of our members in their dealings with some of the largest and most prominent financial institutions operating in the UK.

The availability and uptake of different sources of funding for SMEs, including banks, peer-to-peer lenders and crowdfunding

It is not easy for SME Alliance members to be considered in the general category of SMEs looking for funding. In the majority of cases our members have legacy issues which means they do not fit the criteria for bank lending. Even where banks have been proven to have abused clients and been heavily penalised, it doesn't follow those clients will have their credit rating restored or that potential lenders will consider the circumstances surrounding legacy issues. Therefore, the experience of our members is possibly not a true reflection of the availability of funding to the SME market and this situation is currently excluding funding to thousands of SMEs.

Understandably those SMEs who have been abused by banks are also nervous of entering into any agreement with lenders because there are no safeguards in place to ensure the same or similar misconduct won't happen again - especially as banks can and frequently do attack personal properties (homes) which are no longer protected by regulatory structures (MCOBS etc) once they are used to secure unregulated commercial lending. All the same, businesses do need funding – especially where owners are trying to rebuild businesses post mis-selling or unethical 'business support units' etc - and, in too many cases, the only funding readily available is 'bridging finance' at crippling interest rates. This has been particularly true for the farming sector where bridging loans (given on the grounds the agents involved would then source mainstream lending) has resulted in tragic results.

The level of competition in the SME lending market and the impact of recent regulatory initiatives

We're not sure what impact regulatory issues or initiatives have had which could improve either competition or lending from major banks? Commercial lending is still unregulated and, other than large fines, we have seen little that has changed – except perhaps the fact lenders seem even more reluctant to lend and are even more keen to ensure terms of lending are onerous and biased in their favour. The introduction of a few challenger banks and the British Business Bank hasn't changed the ethos of lending – which is to maximise bank profits at all costs and even where that gain will obviously damage the client. Despite inspirational advertising campaigns suggesting banks will support small business and even cancer victims or those with mental health issues, the criteria for lending remains largely unchanged. A loan or overdraft facility is still mostly a tick box exercise and nothing to do with the former relationship-based lending where a manager knew his clients and

their potential. We're noticing also that challenger banks, who suggested they would operate new models of lending, are also reverting to the classic corporate model of the big banks.

Trends in SME finance and how potential changes to regulation and redress may affect the market

If the trend before the credit crunch was to lend, lend, lend and with a minimum of security, it does seem the trend now is to lend sparingly and with maximum security – although we note it is frequently reported in the media that SMEs are not applying for bank lending – which we would question. Possibly the introduction of more stringent regulation (although we are unaware of what this is) will make lenders even more reluctant to lend. How will this affect the market? SMEs can't say but business owners, business groups, economists and politicians all say the minimum funding filtering through to SMEs and stifling growth, is affecting GDP.

Any sources of finance which SMEs will not consider or approach and why

It would be good to say SME owners won't use bridging finance from companies with a proven track record of never progressing the loans to main stream despite endless promises. But all too often desperate business owners do resort to this. Similarly, it would be good to say SMEs don't revert to using the equivalent of pay day loans or loan sharks in order to keep paying bank loans or IRHP repayments. Unfortunately, people with their backs to the wall who are trying to save their business, their home, or both, are very often in a position where any loan is better than no loan.

The ability of SMEs to resolve disputes and access fair and reasonable compensation when they borrow money.

Please see next point below.

The effectiveness of existing arrangements for dispute arbitration and settlement

Unfortunately, the existing arrangements are at best ineffective and at worst non-existent. And this sorry situation is as contributory to the abuse of SMEs as the conduct of the banks themselves. The Financial Ombudsman Service is not only ill equipped to deal with SME complaints in terms of its ability to compensate, it has also been exposed to be totally inefficient, inept and negligent – which is something too many SMEs have already discovered to their cost.

The victims of mis-selling or other bank abuse have three choices for resolving serious disputes. In most cases they are all impossible:

1. The Banks internal complaints procedure - We would suggest that in SME cases or indeed in any case where the Bank might have to pay out more than a few hundred pounds, it is a waste of time expecting any satisfaction from the banks. Additionally, it is extremely time wasting and we have members who are still waiting for a reply from banks internal complaints divisions, several years after they made their complaint. Time is of the essence for business owners who need to keep their businesses going even while dealing with banking disputes. Banks are fully aware of this and we suggest the internal complaints divisions are step one of the banks 3D system of 'delay, deny, dilute.'
2. Resolution via the regulators - as mentioned above the FOS are ill prepared and cannot award suitable compensation and the FCA does not deal with individual cases.
3. The civil courts - with increasingly less (or no) legal aid, ever increasing court costs and legal costs vs Banks who are happy to spend millions of pounds of their shareholders money when sometimes the alternative would be to pay a fraction of that to resolve legitimate complaints, the Civil Courts are not an easy option. For those who get around this by entering into

Conditional Fee Agreements (CFA) with legal firms, or No Win No fee agreements, the outcomes are not always the best. Very often it is written into these agreements is the fact the firms can compel the client to accept an offer from the lender – which is sometimes little more than the cost of the legal fees. Also, many SME owners who have genuine claims have been hampered because it has taken an inordinate amount of time to obtain information from the Banks – with some SMEs not even aware of the actions that forced them into difficulty – and so have been prevented from taking legal redress because of the statute of limitations on civil actions which prevent claims for activity more than six years old.

At present there isn't any other route available to most SMEs which is ridiculous given how many cases have been proven collectively against the banks. Recently, Lloyds Banking Group has successfully used mediation to resolve some of the HBOS Reading cases but such opportunities are few and far between and most victims of recognised systemic abuse are forced into wholly inappropriate review schemes set up and run by the Banks themselves. These schemes (such as the Griggs Review for HBOS Reading and the RBS GRG Review) are, if not sanctioned by the FCA, are generally approved by the regulator. Again, we feel the Banks, with the agreement of the regulators are using these schemes as little more than a silk glove to hide yet another steel fist. The very fact some banks can pay minimum compensation for years of financial loss and distress to their customers and then get away with paying a mere 8% for consequential loss, is just one more example of how bad the current 'arrangements' are. It has now become standard and acceptable (by regulators) that the actual consequences of Banks first, deliberately ruining a business, and then spending years denying this has happened, can be ignored. Over and above the actual losses to the businesses, it is rarely the case the level of compensation will go anyway to mitigating years of stress and anguish or the personal losses to the business owners. While senior bankers continue to be paid huge fees and bonuses for overseeing and allowing so much misconduct to exist and continue, we have seen compensation equivalent to a few weeks or even a few days of a senior banker's fees offered as compensation for years of abuse and denial to business people.

The merits of the Financial Conduct Authority's proposals for expanding SME access to the Financial Ombudsman Service

In 2017 at a Committee on Regulation in Westminster which SME Alliance was able to participate in, we asked two representatives of the FOS the following questions:

1. What qualification do you need to be an adjudicator for the FOS?
2. Of the 2000 employees at the FOS, how many people fully understand complex financial products like IRHP or TBL's?

The answer to the first question was "none". No specific qualifications are needed. The answer to the second question was "five". And even then, this wasn't a definitive answer.

These people make decisions every single day that could and sometimes do ruin lives. While many of us have long known this was the case, the Dispatches programme (13th March 2018) has now exposed publicly exactly how unsatisfactory the whole FOS is. We have attached a transcript of the programme to our submission and we would ask how anyone could suggest this organisation should have additional powers or indeed any powers? Please note, our comments are not a criticism of the adjudicators per se as they obviously cannot be expected to do a good job without the training, knowledge or experience necessary to do a good job and we noted the frustration many expressed in the Channel 4 documentary. Our comments are a definite criticism of both the senior management of FOS (and the FCA) who have allowed such an inadequate and inappropriate system to exist for so long.

The case for establishing a new “tribunal” body for settling SME banking disputes and the means by which such a body could be created

SME Alliance has been asking for an alternative to the FOS. In March 2015 at the request of Andrea Leadsom MP, we documented how we thought an alternative would work and we submit that document with this submission. We know that since then the APPG on Fair Business Banking has been collaborating with various people and organisations like SME Alliance and the barrister Richard Samuels.

The design, governance and operation of such a tribunal body, and the potential relationship between it, the Financial Ombudsman Service, and the Financial Conduct Authority

Without doubt who ever is given the governance of such an organisation, it absolutely should include the voices of those who have been most affected by banking disputes and also those who have had direct dealings with victims of bank abuse. While the recent involvement of more MPs, Lords and Ministers in raising the issues of dispute between the financial sector and SMEs is much appreciated and is definitely having an impact, we still have a situation whereby committees are formed and important discussions take place – about other people (victims). But many of the victims are very eloquent, rational people whose explanations and experience would be of enormous assistance to those trying to find resolutions. We give the example of the Treasury Select Committee who regularly pose questions to bankers, regulators, auditors etc but, to the best of our knowledge, they do not pose questions to those business people who might be able to legitimately challenge what others have had. Were that the case, situations where senior bankers from RBS stated adamantly to the TSC that GRG was not a profit-making division of the bank, could have been disproven immediately.

The impact of additional avenues for redress on (i) the balance of power between SMEs and lenders; and (ii) the supply of, and demand for, credit

It cannot be the case banks do not want an ADR system to compensate SMEs purely for economic reasons. Possibly the so called ‘professional’ services associated to banks would have that objection because the very lucrative flow of monies to Magic Circle solicitors, auditors and IPs would be considerably less if SMEs could resolve their issues quickly, cheaply and easily (or fairly easily) via a Tribunal system. Banks would undoubtedly save multiple millions if not billions if such a system were to exist.

However, it is questionable whether banks would be happy to relinquish the power they’ve had over the last twenty years quite so easily. A level playing field wouldn’t just bring about resolutions for misconduct done, equally importantly, it would also challenge Banks ability to continue abusing customers.

It is a fact many business owners have not only been subject to misselling or fraudulent conduct, they’ve also been subjected to bullying, intimidation and harassment. This kind of behaviour has been particularly successful in allowing the theft of assets. While some SME owners will not be bullied it’s a sad fact many are because they’re over a barrel. “Do what we say or we call in your loan”. “Do that or we call in your personal guarantees.” In many cases it really is as blatant as that and these threats are enforced. They use the good guy bad guy tactic but usually with the intention the bad guy wins on the instruction of the more senior good guy. Again we use the example of HBOS Reading where a very senior banker re-opened a victims account and gave the client a new facility. But at the same time the banker instructed his colleague who would be running the account, to give it four weeks and then ‘wrap it’ – in other words, close the business down which he did – in the most unpleasant way possible.

We would suggest some banks have been deliberately employing people who were capable of such conduct because only they would ruthlessly behave in this way in order to achieve bank targets and also to achieve

bonuses. Such conduct, where established, would not go down well in a Tribunal setting, although having said that, it has been materially ignored in the civil courts for a very long time.

The regulation of SME lending.

The level of protection currently afforded to SMEs when they borrow money

At present there is no protection for SMEs. Commercial lending, as the FCA repeatedly remind us, is mostly unregulated. More unfortunate still is the fact most SME owners don't realise they have no protection until it's too late. In almost every case SME Alliance has seen, the business owners have written to the Financial Ombudsman or the FCA in the belief these organisations would actively be able to help them. In almost every case this hasn't happened.

The Banks frequently require personal guarantees from SME owners as a pre-condition to advancing funds to the business, often in addition to other security. At present these arrangements are considered commercial lending and are outside the scope of the FCAs powers, but we would argue that, as the SME owner is putting his or her personal wealth, and often family home, at risk, this is an extreme version of personal finance and should be regulated as such.

The use of personal guarantees should be investigated and, at the very least, a code of conduct should be drawn up around their suitability and application.

The case for bringing lending to SMEs within the regulatory perimeter, including (i) the likely impact on the supply of, and demand for, credit; and (ii) lessons learned from past misconduct.

It's certainly true many SMEs are now nervous of getting funding from banks but on the other hand, SMEs do need funding and the option of not applying for it is stifling growth in the sector. While in theory SMEs may be more comfortable with Bank funding if it was regulated, the issue still remains that many SMEs don't trust the regulators to deal effectively with bank abuse and misconduct. Additionally, what would change about the fact the FCA doesn't deal with individual cases? Would this still apply if the lending was regulated or would it still be the case the only people able to deal with individual cases is the FOS? If an organisation like SME Alliance went to the FCA with 20 or 30 similar fact cases, what difference would it realistically make to the present long winded system of initial complaints potentially leading to a Section 166 review, leading to a possible Section 168 review and an eventual decision that may, or may not be published?

An example of this is the HBOS Reading case which was reported by the victims in 2007 and led to a Section 166 skilled persons review on 19th October 2009 (the same day some of the victims delivered a comprehensive report to the FSA and over three years after HBOS started its internal investigations of the fraud). The section 168 review was started on 28th June 2010 – there has been no outcome almost eight years later even although six people have been jailed for a total of 47.5 years.

Would the time scales of these regulatory investigations have been shortened because the lending from HBOS Reading was regulated?

All the same, it would obviously be advantageous for SME lending to be regulated but only if the regulator was inclined to enforce those regulations.

Other non-regulatory or quasi-regulatory options for policing SME lending, such as the establishment of industry codes and standards

We have codes – the FCA Principles for Business – the BBA codes – the banks own voluntary codes. We also have codes for all the 'professional' industries who work with the Banks like lawyers, accountants, auditors, Insolvency Practitioners, estate agents, surveyors.... They all have regulators, they all have codes and some of them have enabled a massive fraud against the public and SMEs. Again, the problem isn't necessarily just the

misconduct of the bankers but rather all of those who make large amounts of money by enabling bank misconduct. Bankers and associated 'professionals' have got used to the huge rewards they get and many seem to feel an unhealthy entitlement to keep getting the rewards by hook or by crook. All the codes in the world are not going to change a culture that values the accumulation of wealth above all else. Until funds are in place to allow police forces to deal with economic crime and until bankers have to consider how much the value their freedom vs how much money they can make by manipulating existing codes and standards for financial gain, it seems pointless to introduce more.

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