

New rules to give SMEs extra rights in respect of financial services

Regulations designed to afford additional "consumer-style" protection to SMEs could also mean a big increase in the potential liability of regulated entities, write Conor Houlihan and Kate Curneen.

The important role of small and medium enterprises in a globally changing economic landscape characterised by continuous structural changes and enhanced competitive pressures is well recognised, both nationally and at an EU level. As providers of employment opportunities and as key players in the wellbeing of local and regional communities, SMEs play an essential role in ongoing economic growth.

Ensuring that an adequate pool of credit is available to fund SMEs in the real economy is one of the key priorities of the current Irish Programme for Government. There have been numerous recent government initiatives to support SMEs, the most notable of late being the establishment of the Strategic Banking Corporation for Ireland by the Department of Finance in an effort to ensure the availability for SMEs of competitive and innovative financial products.

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The Central Bank of Ireland has repeatedly emphasised that it sees the SME sector as a vital contributor to ongoing sustainable economic and employment recovery in Ireland. In addition, it recognises that the SME sector is largely indigenous and employment-intensive, relying primarily on domestic demand and domestically-provided bank credit and, as such, is

particularly responsive to changes in domestic policy.

Recently the Central Bank of Ireland has focused its attention on broadening the ambit of substantial customer protection regulation beyond traditional "consumers" (i.e. natural persons acting outside their business, trade or profession) to SMEs.

Section 48

The tool utilised by the Central Bank of Ireland for this task is Section 48 of the Central Bank (Supervision and Enforcement) Act 2013. This section gives the Bank the power to make regulations concerning a broad range of financial services activities in connection with the proper and effective regulation of financial institutions.

The Act allows it to transfer the legal basis of much of its supervisory function as regards financial services providers from an informal footing, such as regulatory codes, to a formal statutory footing, in the form of regulations.

Section 44

The Act has a broad remit. Pursuant to Section 44, a breach of any provision of financial services legislation by a financial services provider will give an affected customer the power to sue that provider for damages where they can prove that they have suffered loss or damage as a result of the breach. The new private right of action represents a substantial extension of potential liability for regulated entities.

On 11th January, 2015 the Central Bank of Ireland published the consultation paper and draft regulations on the amendment of the Code of Conduct for Business Lending to Small and Medium Enterprises.

The Draft Regulations propose to give SMEs additional significant rights in connection with their relationship with

lenders authorised by the Central Bank of Ireland.

The current SME Code was introduced in 2009 and, following a limited review, was amended with effect from 1st January, 2012. While the current SME Code is issued under Section 117 of the Central Bank Act 1989, the Central Bank of Ireland intends to make regulations under Section 48 to both replace the existing SME Code and introduce the reforms described in the Draft Regulations.

Lender requirements

The Draft Regulations would strengthen the protections available to SMEs in a number of significant ways, including by introducing requirements for lenders to:

- provide information on the application process for credit and associated timelines;
- assess the affordability of credit;
- provide reasons in writing for declining credit that are specific to the application (or part thereof) that was declined;
- provide increased information to borrowers about their policies for dealing with financial difficulties, including the implications for borrowers who are not co-operating. In this regard, the Central Bank of Ireland is considering the introduction of the concept of "not co-operating" similar to that contained in the Code of

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Conduct on Mortgage Arrears 2013;

- provide detailed information to borrowers in financial difficulties about the offer of an alternative arrangement;
- expand the appeals provisions to include decisions on declining or withdrawing credit and decisions regarding terms and conditions; and



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- provide information to the customer about:
 - government supports available from or through the lender;
 - the lender’s appeals process and the role of the Credit Review Office (where relevant); and
 - the complaints process including, where relevant, to the Financial Services Ombudsman.

It is to be hoped that, following the consultation process, a balance will ultimately be struck between ensuring the availability of credit and the provision of adequate regulatory protections for SMEs

- Other proposed enhancements involve:
- the extension to all SMEs of certain protections currently only afforded to personal consumers, relating to the

provision of credit contained in the Consumer Protection Code 2012;

- the extension to all SMEs of CPC requirements in relation to the provision of information and advertising (which currently only apply to smaller enterprises); and
- the inclusion of the provision of credit by credit unions to SMEs and of business credit cards within the Draft Regulations’ scope.

However, multi-lender credit and special purpose vehicles are excluded from the scope of the Draft Regulations, as is the position currently under the existing SME Code.

Balance

The Draft Regulations seek to introduce enhanced and additional provisions in an effort to increase support for SME borrowers and to ensure meaningful engagement by lenders. However, if implemented as is, they would have a significant effect on the manner in which financial institutions engage with SMEs in the future.

Given the broad definition of an SME, it is likely that most business borrowers would receive the protections proposed by the revised SME Code.

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It is to be hoped that, following the consultation process, a balance will ultimately be struck between ensuring the availability of credit and the provision of adequate regulatory protections for SMEs, on the one hand, and maintaining a regulatory framework that, from the point of view of financial services providers, is practical and workable, on the other.

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