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Sam Beckett
Permanent Secretary
Department of Business, Energy and Industrial Strategy
1 Victoria Street
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Dear Sam

CSBILS

My team have been discussing the new 'CSBILS' loan scheme with BEIS and HMT officials in the past couple of days. We have rapidly pulled together the outlines of how a new scheme might work, taking into account the design parameters outlined by the Chancellor, and have discussed them informally with some of the larger banks. I am writing to record a number of risks that we believe need further consideration before any scheme could be launched. Our view is that if not properly mitigated these could have profound and long-term impacts on the market.

In putting forward these comments, I should say at the outset that the policy objectives behind CSBILS have not been clearly articulated to the Bank, which has made proper options analysis difficult. We understand the prime motive behind the proposal is rapidly and substantially to increase the volume of loans being delivered at the lower end of the market. We have been working with BEIS to flesh out the potential target market, but we have not seen articulated a target number, value or penetration rate of the SME sector. We also gather that the speed of approval once an application has been submitted is a key consideration, with HM Treasury seeking ways to ensure loans are swiftly delivered, ideally within 24 hours.

Based on that understanding, and following a detailed conversation with the major banks this afternoon, our central concerns are as follows:

1) ***Significant risk of fraud and abuse***. Applying only basic checks and allowing self-certification by businesses in the desire to speed up loans opens up the risk of significant fraud and abuse, as anyone with a business current account or HMRC self-employment registration could borrow, possibly through multiple business entities. We would not be able to track the use to which borrowing might be put. At the low interest rates being suggested, a loan could be used to pay off existing more expensive business debt by those businesses who had no prior need for finance, creating significant deadweight costs. And with a significant blurring between personal and business activities at this end of the market, the loans could be viewed simply as a very attractive way to borrow for personal and not business purposes. Furthermore, with a 100% guarantee and a standard rate of interest, there is no direct incentive for banks to assess a borrower's creditworthiness or, indeed, to seek to recover the debt in the event of default.

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2) ***The UK's alternative finance sector could be negatively impacted, and competition in the SME finance market distorted***. We have not consulted with the alternative finance sector and it could be difficult for many alternative finance providers to compete with these loans as currently proposed. If this was the consequence, it would reverse the UK's hard work over the last decade to build a world-leading alternative finance sector, in no small part to reduce its ongoing reliance on the large banks following the financial crisis. That could leave SMEs reliant, once again, on the large banks in the forthcoming recovery.

3) ***Setting up a standardised product will be an additional implementation challenge for lenders above and beyond the implementation of CBILS.*** We understand that the large banks have suggested that they could deliver by May 4th. However, even with a standardised loan product and application form, the proposal risks creating fundamental process and systems configuration issues in these institutions. Even after six weeks, some banks have ongoing issues to resolve in standing up their systems to deliver CBILS. Overlaying a new standardised product and application form simply increases the challenge.

We have flagged to officials that there are still alternative options for Ministers that would address many of the remaining obstacles to the swifter delivery of lower value loans through the current CBILS. Part of the issue lies with the lenders themselves, whose systems addressing this area of the market are not flexible, and in the case of some substantial CBILS lenders progress remains slow. On our side, work is already well progressed to remove obstacles, and we understand Ministers are considering further modifications and reassurances for providers to facilitate take-up of the scheme. We are also working with your officials on complementary ideas to support the funding of alternative lenders. If completed, this work could rapidly deliver many of the benefits sought in this area of the market while still encouraging a diversity of supply.

However, I recognise that given the widespread market disruption there is also an argument that could be made that we cannot afford to take an incremental approach as this risks doing too little too late. It is clear that thousands of SMEs are facing a very real cash crunch. Given the gravity of the situation you and Ministers will need to weigh up the risks of action highlighted above against the risk of not taking sufficient action.

We stand ready, of course, to support the Government in delivering against your chosen policy objectives at pace. As set out here, however, there are a range of significant risks in the present direction of travel that need to be taken into account (and there may be others we have not fully worked through, for instance around State Aid) and as such, if Ministers reach the view action is required now through a CSBIL Scheme, an instruction will be needed before any scheme can go live.

Yours sincerely

PD

Keith Morgan CBE
Chief Executive Officer & Accounting Officer