Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

Getting consumers a fair deal from regulatory reform

Briefing on the Financial Services Bill

The Financial Services Consumer Panel represents the interests of consumers by advising the Financial Services Authority (FSA) on policy. The Consumer Panel believes that the recent economic crisis and the financial scandals of the last decade have demonstrated beyond all doubt that consumers need to have a strong voice in the regulatory system. However, the Panel is concerned that, as presently drafted, the Financial Services Bill fails to sufficiently enhance consumer protection standards as originally intended.

The key changes the Consumer Panel would like to see are:

- a requirement for the Prudential Regulation Authority (PRA) to respond to representations from the FCA Panels on matters of cooperation with the Financial Conduct Authority (FCA);
- a duty of care for those providing financial services;
- a requirement of access for all consumers to financial services;
- an increase in the transparency of financial services regulation by empowering the PRA and FCA to disclose information about the financial services firms they regulate;
- effective competition powers for the FCA to allow it to deliver its statutory objectives; and
- a requirement for the regulators to undertake full and robust cost benefit analysis when developing new rules.

1 Ensuring a strong consumer voice

The Problem

Consumers are excluded from the decision making process when it comes to prudential matters decided by the PRA. This may be inevitable in a crisis, but it is undesirable and unnecessary under normal circumstances where its actions could have a significant and detrimental impact on ordinary people. It is therefore essential for the PRA to consider the impact its policies could have on consumers by seeking input and insight from the Consumer Panel.

We are concerned that, under current proposals, the only consumer input to the PRA would come from the CEO of the FCA (as a PRA Board member). As the lone voice representing consumers, they are unlikely to successfully influence PRA policy especially when considering it at a late stage in its development. Furthermore, the FCA CEO will base their position on evidence provided by both consumer and industry representatives and will, in effect, present a compromise position based on the different comments it has received from a range of stakeholders.

It will be especially important for the PRA to consider the impact of its actions on consumers in relation to mortgages. For example, the PRA's micro prudential policy will directly influence lenders mortgage forbearance requirements. The Consumer Panel advised the FSA's prudential team when it previously developed guidance in this area, to ensure it fully considered the potential issues for consumers, their options and likely outcomes.

The Solution

It is perverse that the PRA is required to consult practitioners, and potentially a Practitioner Panel, but not consumers when developing new rules and policies. The current arrangements, whereby the FSA has sought advice from the Consumer Panel on the impact of its policies on consumers, has worked well for the last decade. This should therefore be continued for the PRA, as it will be for the FCA.

Amendment

Clause 6, change clauses 2L and 2M to read:

Page 32, line 8 – insert

Arrangements for consulting practitioners and consumers

Add sub-clause to 2M page 32, line 21 to read

(2) The PRA must consider and respond to representations made by the Consumer Panel established by the FCA under Section 1Q.

2 Getting the industry to put consumers first

The Problem

The financial services industry has a hugely disproportionate balance of knowledge when compared to ordinary consumers. This is something the Government recognises in the Bill. However, the Panel does not believe the new requirements for firms to owe consumers an appropriate level of care or to give accurate and timely information go far enough.

We believe those providing financial services should owe their customers the same duty of care as a lawyer or other professions.

The Solution

Like the Joint Committee of the House of Lords and House of Commons, the Panel strongly believes the Financial Services Bill should require firms to have a duty of care towards their customers. This would involve placing a clear responsibility on firms to act honestly, fairly and professionally in the best interest of their customers and to manage conflicts of interest.

The Panel believes including a Duty of Care provision in the Financial Services Bill is a key part of delivering a step change in regulatory approach to protecting consumers. This will ensure providers would be unable to profit unfairly at the expense of their customers, preventing the worst examples of consumer detriment from re-occurring. This includes the numerous industry mis-selling scandals seen most recently with the Payment Protection Insurance (PPI) debacle. This is also an essential tool to help rebuild consumer trust in the financial services industry.

Amendment

Adding two sub-clauses to 3B(1) to read (Clause 6, p34 line 18):

"(g) the principle that, where appropriate, authorised persons should act honestly, fairly and professionally in accordance with the best interests of consumers who are their clients"

"(h) the principle that, where appropriate, authorised persons should manage conflicts of interest fairly, both between itself and its clients and between clients"

and amending 1C(2) to read (Clause 6, p21 line 26):

(e) the general principle that those providing regulated financial services should be expected to provide consumers with a level of care that is appropriate having regard to the degree of

risk involved in relation to the investment or other transaction and the capabilities of the consumer in question, having regard to the general duty to provide those services honestly, fairly and professionally in accordance with the best interests of the consumers in question.

3 Access to financial services

The Problem

Access to financial services is essential in a 21st Century society. Yet worryingly the Bill makes no mention of it. There is not much point talking about a fairer, more competitive market in financial products if consumers are unable to access financial services because of regulatory or industry actions.

Access to protection insurance and other general insurance products at affordable prices is also an area where many consumers are facing increasing problems as insurance companies impose restrictions on cover to wide swathes of consumers.

A simple competition objective does not in itself guarantee access. For example, consumers in rural areas will have been hit particularly hard by the decision of some banks to close branches or restrict access to cash machines.

The Solution

The Panel believes the FCA, when fulfilling its competition objective, should have regard to the ability of consumers to access financial services. This would ensure the FCA considers the impact of its regulations, as well as the actions of the industry, on consumers' ability to access essential financial services.

Amendment

We support the amendment tabled by Lord Sassoon add a sub-clause to 1E(2) to read (Clause 6, p22 line 9):

"( ) the ease with which consumers who may wish to use those services, including consumers in areas affected by social or economic deprivation, can access them".

4 Using informed consumers to enhance consumer protection

The Problem

There is a crisis of trust in financial services regulation. The Panel believes that more transparent regulation would help restore public trust. We welcome the Bill's increased commitment to transparency, particularly in publishing information about misleading financial promotions.

However, we do not believe this goes far enough; consumers should not be subject to unreasonable delays in receiving information about serious problems with a financial firm. The present Financial Services and Markets Act constrains the FSA and restricts its ability to publish information[1]. The FSA is required to keep regulatory information confidential and, subject to some limited exceptions, it is a criminal offence to publish information relating to the misbehaviour of firms[2]. The Joint Committee recommended that neither the PRA nor FCA should be restricted from disclosing information. However, there is strong industry pressure to bury bad news and delay publication, keeping consumers in the dark, in spite of widespread public belief that the current regulatory system has been weak and ineffective at protecting

[1] ss 348, 349 of FSMA 2000
[2] s 352 of FSMA 2000

consumers. The contrast with the FSA's namesake the Food Standards Agency could not be more stark. The Food Standards Agency may publish such information as it thinks fit[3] under the Food Standards Act 1999, subject to a narrow list of exceptions. This has helped restore consumer confidence in the industry and has supported its recovery from the reputational damage it suffered from the BSE crisis.

Under the new Bill there will also be a requirement for the regulators to consult with firms before publishing warning notices. The Panel is concerned that this will allow lawyers to introduce substantial delays into the process, effectively negating the intention behind the requirement to publish.

The Solution

As part of a drive for greater transparency, we believe both the FCA and PRA should be empowered to publish information about the individuals or firms they regulate where this would help them achieve their objectives. This would ensure consumers are no longer kept in the dark when the FSA identifies failures in a regulated firm and instead would have access to information about their financial services provider to help them make more informed decisions. Greater transparency would also serve as an important catalyst in driving improved firm behaviour.

The Panel also believes consumers should be informed of prosecutions for breach of the regulations. While we support the power given to the FCA to publish warning notices, we do not believe the FCA should be required to consult the firm or individual involved. There is a danger that this creates ambiguity and delays in publishing information which is beneficial to consumers. In this respect, the term used in the Bill of issuing a "Warning Notice" is very misleading. It is in fact equivalent to a "formal charge". The Panel does not think that the reputational damage from a Warning Notice is any different from that experienced by anyone else who is subject to prosecution and subsequently acquitted.

Amendment

To empower the regulators to publish information about the firms they regulate,
Schedule 12, p286 line 6 inset and renumber:

(2) In subsection (1) add a sub-clause (c): [to s349 (1) *Section 348 does not prevent a disclosure of confidential information which is—]*

"(c) by either the PRA or FCA which, subject to applicable Directives, is reasonably necessary for the furtherance of the consumer protection objective."

5 Competition

The Problem

The Panel is pleased that the FCA now has a new competition objective and wider competition powers. However, the Panel does not believe these powers go far enough to enable the FCA to effectively deliver its objectives. As the Bill stands, the FCA will still have to refer cases to the Office of Fair Trading (OFT), or its successor organisation, who would conduct a market analysis before determining whether the issue should be referred to the Competition Commission. The Panel thinks this leads to a slow and unfair regulatory process.

[3] s 19 Food Standards Act 1999 http://www.legislation.gov.uk/ukpga/1999/28/section/30

The Solution

The Panel supports the view of the Joint Committee[4] that the FCA should have concurrent competition powers, in respect of a Market Investigation Reference (MIR), with the OFT.[5] This would empower the FCA to conduct its own economic analysis and deal with distortions in the market without the need for any delay. This could be achieved by giving the FCA equivalent powers to those granted to the OFT under Section 131 of the Enterprise Act 2002 and we therefore advocate amending the Financial Services Bill to reflect this.

By giving the FCA these powers, a single organisation would tackle significant market issues, such as the PPI debacle, without the substantial delay introduced through referral to another body. This would lead to an earlier response with the faster implementation of remedies and reduced harm to consumers.

Amendment

Clause 42, p134, line 15- leave out from beginning to end of line 38, and insert:

"234H Power of FCA to make request to Competition Commission

The FCA may, subject to subsection (4) of section 131 of the Enterprise Act 2002, make a reference to the Commission if the FCA has reasonable grounds for suspecting that any feature, or combination of features, of a market for financial services in the United Kingdom prevents, restricts or distorts competition in connection with the supply or acquisition of any financial services in the United Kingdom or a part of the United Kingdom."

6 Requiring the regulators to fully assess the impact of their proposals

The problem

The requirement that both the FCA and PRA should undertake a full and robust impact analysis, where an estimate (implying quantification) of both the costs and benefits is undertaken when developing new rules, is an essential accountability safeguard for the new regulators. We have seen how the existing FSMA requirement to estimate costs acted as an important accountability measure during the development of Mortgage Market Review (MMR). This enabled the Consumer Panel to ensure the FSA considered fully the effect of its proposals on creditworthy consumers, which ultimately led to major beneficial changes in the FSA's proposed approach.

We are concerned that the cost benefit requirement, as worded in the Bill, is significantly watered-down compared to the existing FSMA requirement that applies to the FSA. The Bill will only require the regulators to undertake an 'analysis of the costs together with an analysis of the benefits'. The reference to 'analysis' means that the requirement to quantify has been dropped. Sections 138I(8) and 138J(8) also make it too easy for the regulators to claim impracticality as an excuse not to undertake a full and proper cost-benefit analysis.

The FCA's new intrusive regulatory agenda makes the need for careful and informed quantification even more pressing. The full ramifications of new rules need to be carefully assessed to ensure they do not lead to unintended costs for consumers. As the Chairman of the FSA, Lord Turner, outlined in his 2010 Mansion House speech, while the regulator cannot

[4] Paragraph 279, Financial Services Bill Joint Committee First Report

[5] Market Investigation Reference powers would allow the FCA to refer a market to the Competition Commission for further investigation where they have reasonable grounds for suspecting that any feature, or combination of features, of a market is preventing, restricting or distorting competition. The Competition Commission will decide whether competition is indeed prevented, restricted or distorted, and (if so) what, if any, action should be taken to remedy the adverse effect on competition or any detrimental effect on consumers arising from the adverse effect.

continue to accept waves of mis-selling nor should it swing to the other extreme and prevent consumers from exercising free choices.

The solution

We believe the regulators should be required to undertake an estimate of both the costs and benefits when developing rule changes. This should consider not only the costs to the industry, but also the impact on consumers of both introducing, or not introducing, the proposed rule change. This will ensure changes to regulation are proportionate and in the best interests of consumers. This would also ensure that financial regulators are held to the same best practice standard of analysis expected of government departments and executive agencies, as set out in the HMT Green Book.

Amendment

Amending 138I - Consultation by the FCA – to read (Clause 23, p100, line 22):

[…]

(7) "Cost benefit analysis" means -
~~(a)~~ an estimate ~~analysis~~ of the costs together with an estimate ~~analysis~~ of the benefits that will arise.
(i) if the proposed rules are made (or not made), or
(ii) if subsection (5) applies, from the rules that have been made~~, and~~
~~(b) subject to subsection (8), an estimate of those costs and of those benefits.~~
This should consider the costs and benefits for both consumers and the industry.

~~(8) If, in the opinion of the FCA~~
~~(a) the costs or benefits referred to in subsection (7) cannot reasonably be estimated, or~~
~~(b) it is not reasonably practicable to produce an estimate,~~
~~the cost benefit analysis need not estimate them, but must include a statement of the FCA's opinion and an explanation of it.~~

Amending 138J - Consultation by the PRA – to read (Clause 23, p.101, line 36):

[…]

(7) "Cost benefit analysis" means -
~~(a)~~an estimate ~~analysis~~ of the costs together with an estimate ~~analysis~~ of the benefits that will arise.
(i) if the proposed rules are made (or not made), or
(ii) if subsection (5) applies, from the rules that have been made~~, and~~
~~(b) subject to subsection (8), an estimate of those costs and of those benefits.~~
This should consider the costs and benefits for both consumers and the industry.

~~(8) If, in the opinion of the PRA~~
~~(a) the costs or benefits referred to in subsection (7) cannot reasonably be estimated, or~~
~~(b) it is not reasonably practicable to produce an estimate,~~
~~the cost benefit analysis need not estimate them, but must include a statement of the PRA's opinion and an explanation of it.~~

About the Financial Services Consumer Panel

The Financial Services Consumer Panel (the Panel) was established by the Financial Services Authority (FSA) in December 1998 to represent the interests of consumers by advising the FSA on its policy and practices and monitoring its effectiveness. Subsequently, the Financial Services and Markets Act 2000 (FSMA) made it a statutory requirement for the FSA to establish and maintain a Consumer Panel. The relevant sections of the FSMA came into force on 18 June 2001.

The main purpose of the Panel is to provide advice to the FSA. Consequently, the emphasis of the Panel's work is on activities that are regulated by the FSA. The Panel is also responsible for assessing and commenting on the effectiveness of the FSA. In addition the Panel looks at the impact on consumers of activities outside, but related to, the FSA's remit. Examples include European issues and policy proposals by HM Treasury and others. The Panel has regard to the interests of all groups of consumers, including those who are particularly disadvantaged in the context of financial services. The Panel can also advise the Government on the scope of financial services regulation; and consider other matters that assist it in carrying out its primary functions.

Members of the Panel have a wide range of relevant experience such as consumer advice and advocacy, front-line advice, legal expertise, market research, consumer policy and the media. More information on the Panel can be found here: www.fs-cp.org.uk

Consumer Panel achievements

Introduction

The development of regulation in financial services involves extensive debate and consultation. The Consumer Panel has been particularly effective in helping the FSA to develop better regulation in early stage discussions. As a result, it is often difficult to identify the precise role the Panel has played in the final outcome. For this reason we have separated our successes into those where we think the Panel made a unique contribution, without which the outcome would have been very different, and those where we exerted significant influence but were not alone in promoting effective change.

Unique contribution

Retail Distribution Review (RDR) – The elimination of provider bias in the advice process. The Panel has promoted the elimination of the conflict of interest caused by commission since the early 2000's. Following the launch of the FSA's Retail Distribution Review at Gleneagles in 2006, the Panel has actively engaged with the development of policy, including commissioning research to shape the structure of the regulation, to ensure the availability of good quality advice to all those who need it . The FSA's reforms will raise professional standards and tackle the potential biases created by provider commission payments to advisers and other incentives. Our consistent highlighting of weaknesses in the retail advice sector has influenced the Retail Distribution Review as it has progressed. Our work has included evidence based policy advice on the need for generic financial advice, the potential role of platforms in delivering value to the consumer and ensuring that regulation addresses the advice gap in the middle market This is work in progress and we continue to challenge the FSA to ensure consumer needs are properly considered.

RDR - Platforms – Better value for consumers. As the RDR progressed it became apparent that platforms would play a significant role in the new post RDR world. The Panel has lobbied to ensure platforms conform to the principles of the RDR. As part of this, we commissioned research which demonstrated that it should be possible for the providers of these services to change their business model, given a reasonable amount of time, and therefore ensure a more transparent and competitive market. The FSA is now in the process of undertaking detailed work

which we hope will result in a more economically efficient platform industry that delivers better outcomes for consumers and is free from opaque payments between fund managers, platform operators, advisers and consumers. No other consumer group responded to the platform consultations.

RDR – Advice for the middle market – As more responsibility for saving for later life is passed to the individual from the employer and the state, there is a need for regulated advice at lower cost for the less well off. The RDR has emphasised this need. The Panel has campaigned since 2007 for the investigation of more cost effective ways of delivering advice. This has included calling for the FSA to examine the need for "simplified advice" and commissioning research into lower cost advice models and straightforward outcome products. Our ideas have been gaining traction and we are optimistic that, together with our campaigning in Europe, the British public will have much better value and more suitable savings vehicles in the future.

Mystery Shopping – The Panel persuaded the FSA in the early 2000s that it should conduct mystery shopping as part of its regulatory toolkit. The various surveys the FSA conducted in following years highlighted serious deficiencies in the provision of advice, equity relief, lifetime mortgage products, PPI and critical illness insurance. The results encouraged the FSA to overcome industry resistance to a more intrusive approach to regulation.

Communications with consumers – The Panel has pressed the FSA over many years to do more to help consumers engage with the market by giving out clear and unbiased generic information, influencing the development of the FSA's Moneymadeclear website and other consumer information. Much of this has now been transferred to the Money Advice Service, but there remains a need for the FSA to continue to communicate directly with consumers on which the Panel continues to advise.

Mortgage Arrears and Repossessions – Since the FSA took over the regulation of mortgages in 2004, the Panel has continued to push for improvements in this vital area for consumers. Most recently we have pressed the FSA to ensure that mortgage companies comply with FSA requirements to liaise properly with customers to do everything possible to avoid arrears and repossessions. At the same time we promoted this need with the Ministry of Justice which eventually resulted in the mortgage arrears pre-action protocol.

More effective identification of emerging risks – The Panel has collected intelligence from consumer groups on emerging risks for consumers over the last three years. This work has informed the FSA's conduct policy and is now in the process of being embedded in the FSA's consumer engagement and Retail Conduct Risk Outlook report. This will support the more proactive approach to regulation which the FSA is adopting.

Areas where the Panel has had a major impact on policy

Mortgage Market Review (MMR) – Inappropriate mortgage lending during the last housing price boom has led to serious consumer detriment, with some consumers struggling to maintain their mortgage payments. To prevent this happening again, the FSA has developed detailed proposals to regulate the sales process and, in particular, to mandate appropriate affordability assessments for all mortgages. While the Panel welcomed the proposals, we were concerned that the FSA's cost benefit and economic analysis was not sufficiently robust to ensure the proposals did not adversely affect creditworthy consumers. The Panel's privileged position inside the FSA meant that we were in a better position to discuss the FSA's analysis. This has been an important influence helping the FSA to refine their MMR proposals.

Financial Crisis in 2007/2008 – The Panel actively lobbied to achieve the greater compensation offered during the crisis for retail bank deposit holders should their bank collapse. This was successful. We have continued to press for better and more effective compensation in both the UK and at the European level, including cover for temporary high balances. Our consistent position has been that different brands should be covered by separate compensation; since

consumers do not understand that very different sounding brands can be authorised under the same institution and so only qualify for one compensation limit.

Banking regulation - Ineffective self-regulation of the banking sector resulted in consumer detriment from poor business practices. The Consumer Panel and others lobbied for the transfer of regulatory responsibility for conduct of business from the Banking Code Standards Board to the FSA in November 2009. The Panel continues to work with the FSA to improve the effectiveness of consumer protection in this sector.

With profits funds – Research published by the Panel highlighted significant problems in the governance arrangements in with profits funds. The FSA has taken action on some of the issues we raised, although we feel it acted too slowly and considerable work is still needed to protect the interest of with profit policyholders. This is something which the Panel's lack of a statutory relationship with the PRA in the future may make more difficult.

Enforcement - The Panel expressed the view to the Treasury Committee in 2003 that the FSA had relied too much on the reassurances of the industry in its compliance work. The increase in the number and profile of enforcement actions and the doubling of size of the FSA team from 2008/9 onwards was a response in part to pressure from the Consumer Panel. The Panel has always maintained that strong action against firms and individuals is important, not only for better behaviour in the industry, but also for consumers to gain confidence from an industry which is well policed.

Financial Capability - The Consumer Panel had long argued for an impartial generic financial advice service which is not linked to the sale of any financial products. In 2008 we therefore supported the Government's Thoresen Review, which led to the FSA being charged with the development of a money guidance service. This led to the creation of CFEB the Consumer Financial Education Body and ultimately the Money Advice Service.

Payment Protection Insurance The Panel has consistently pressed the FSA to take strong action against firms that have mis-sold Payment Protection Insurance. It has been closely involved in efforts to get effective and timely redress for those consumers who were mis-sold PPI.

Financial Services Consumer Panel
2 November 2012