

FCA Mission:

Our Approach to Competition

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Introduction

Every day the UK population relies on a range of financial services, from basic bank accounts to car loans, mortgages, pensions and complex investment products.

Consumers need to have confidence in these services and the firms that provide them. They expect the market to be fair, open and competitive. They also have high expectations of those who regulate these firms.

Parliament created the FCA to regulate the conduct of the UK's financial services. The FCA is also the prudential regulator for all firms apart from banks, building societies, credit unions, insurers and large investment firms. These are authorised by the Prudential Regulation Authority (PRA) and regulated by both the PRA and the FCA.

Parliament gave the FCA a single strategic objective – to ensure that relevant markets function well – and three operational objectives to advance:

- protect consumers – to secure an appropriate degree of protection for consumers
- enhance market integrity – to protect and enhance the integrity of the UK financial system
- promote competition – to promote effective competition in consumers' interests

The aim of our regulation is to serve the public interest by improving the way the UK financial system works and how firms conduct their business. By doing this, it benefits individuals, businesses, the economy and so the public as a whole.

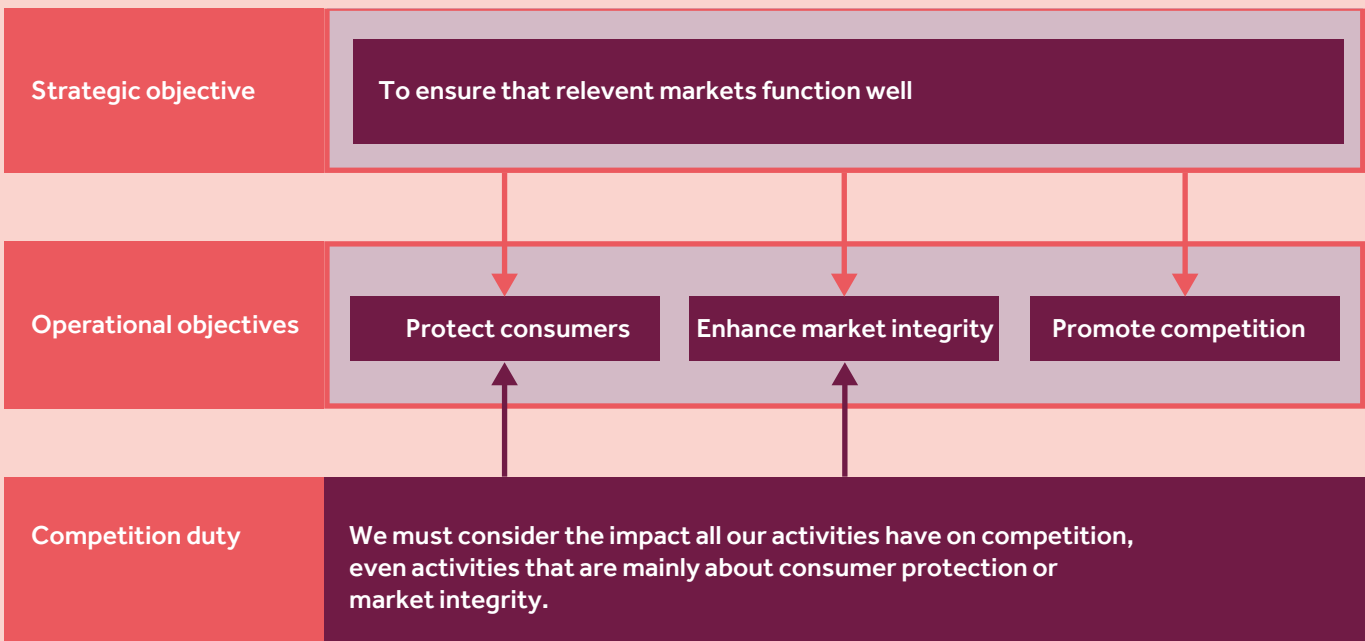
We add public value by: enhancing trust in markets, improving how they operate, delivering benefits through a common approach to regulation, working to prevent harm from occurring and helping to put things right when they go wrong.

To deliver our objectives, Parliament gave us a range of tools, and independent powers to make decisions about how best to use them.

We are one of very few financial regulators in the world with a core objective to promote competition. We also have a duty to promote effective competition in the interests of consumers so far as is compatible with meeting our objectives to protect consumers and enhance market integrity. This means we consider competition across all our work.



Our objectives and competition duty



Our objective is to promote competition in the interests of consumers, not for its own sake. We know that, in some circumstances, increasing competitive pressure in already poorly performing markets can make matters worse. We know also that strengthening competition is not an easy process. Experience in the retail banking sector, for example, has shown this requires a comprehensive approach and persistent effort.

While our Competition and Economics Division spearheads much of the FCA's competition work, this document covers the work we do across our organisation to promote effective competition.

From investment banking to cash savings, our work across both wholesale and retail markets keeps markets open and innovative, and helps consumers understand and buy the right products and services for them.

What is competition?

Competition is a process of rivalry between suppliers. To survive and grow, firms must compete on a range of factors to attract and keep customers. When competition works well, it drives down costs and prices, drives up service standards and quality and increases access to financial services. It also drives innovation, productivity and economic growth. Weak or poorly-functioning competition in financial services can cause harm to consumers, firms and the wider economy.

Effective competition also means that markets are open to new firms which can offer better deals and products, while firms that can't keep up either have to change or go out of business.

Competition is a vital engine of economic growth. By regulating to support competitive markets, our work both adds value to the economy as a whole and helps individual consumers. Our goal is to ensure the UK's financial markets are effective at delivering

benefits to consumers and can be trusted by both consumers and businesses. We do not have a remit to promote the UK's or an individual firm's competitiveness in global financial markets. However, effective competition that increases efficiency and productivity is likely to make UK financial markets and firms an attractive proposition internationally.



Our objective is to promote competition in the interests of consumers, not for its own sake.



Chapter 1

Our role

We do three things to advance our competition objective. We look at market structure and dynamics through our market studies, adjusting the 'rules of the game' where necessary to improve consumer outcomes. We investigate anti-competitive behaviour under the Competition Act 1998 (CA98) and its EU equivalent. And we implement regulation with the aim of supporting, rather than inhibiting, competition in consumers' interests.

Our competition work is not just about lower prices or more switching. One aspect is clearly about supporting consumer choice, including the choice to move from an unsatisfactory supplier to a better one. Importantly, this applies pressure on firms who know that their customers could move easily if their products and services are not good enough. But our work is also about keeping markets open to entry and innovation, tackling anti-competitive conduct and intervening to ensure competitive forces drive good outcomes for consumers. It can also be about protecting consumers when markets fail them.

As a competition regulator our primary role is not to regulate prices or profitability directly. In most instances we look to remedy the underlying market failures or root causes of harm. However, there may be times when we need to intervene directly to protect consumers, such as on product standards or, more rarely, on price.

Our regulatory remit covers thousands of products whose prices are rightly determined by market forces and require no regulatory action. However, there may be some situations where we need to intervene on a specific aspect of

price such as an exit fee or surcharge. More rarely still, we may intervene on overall price. We typically do this in response to acute concerns about the lack of competitive pressure, as we did for default pension scheme charges under auto-enrolment. When we intervene on price, we consider firms' costs and what they need to make a reasonable return. Our role, even when applying a price control, is not to regulate the returns a firm makes. However, we often look at pricing and profitability as important evidence in our market studies, to help us understand market dynamics.

Supporting innovation

An important aspect of our work to promote competition is supporting new and innovative players whose business models may test the boundaries of our current regulations. It is vital that we understand how and when regulation can inhibit new entry and innovation, so that our regulation evolves with financial services rather than holding them back. We do this largely through our Innovate programme, the Regulatory Sandbox, our RegTech work, the Advice Unit and the New Bank Start-up Unit. We describe these initiatives



in more detail in 'Our Approach to Authorisation' paper.

Striking the right balance across our objectives

Consumers need to be able to trust that markets will work well for them. Knowing that firms are well regulated means they can make confident choices about the products they buy. In turn, consumers' choices motivate firms to compete effectively, innovate and grow.

However, regulation that protects consumers, safeguards market integrity and promotes financial stability can stifle competition by raising barriers to entry or limiting innovation. For example, requirements to hold minimum levels of capital make it harder for new firms to enter the market. Our actions need to strike a balance between encouraging competition and innovation and advancing our other operational objectives of consumer protection and market integrity.

The FCA is one of several regulators collectively tasked with managing the balance between competition and financial stability. The PRA and the Bank of England lead on financial stability issues, and the PRA also has a secondary competition objective – 'to act, so far as reasonably possible, in a way that facilitates effective competition in the markets for PRA-authorized firms carrying out regulated activities.'

Often we can take steps to improve competition without affecting consumer protection, market integrity or financial stability – as with our work on Innovate and the New Bank Start-up Unit (described below). But at other times we must strike a balance between allowing new firms to enter and innovate, and preventing harm – as with our work on crowdfunding and peer-to-peer lending.

What does good look like?

Below we set out what a well-functioning market looks like, where we can see competition working in the interests of consumers at all levels of the supply chain. If there is weak competition at any level, it is typically the consumer that ends up paying as firms pass on higher costs. This links with the conditions we want to see when consumers are protected and there is strong market integrity as set out in our other Approach documents.¹

In all markets, we want consumers to be able to buy the products and services they need, sold in a way that is clear, fair and not misleading. We also want good value products and services that meet consumers' needs.

In addition, where competition is working well, we will particularly see:

- Confident consumers able to exercise choice. This requires consumers to have access to the information and professional support they need, and requires firms to present choices in a way that does not unfairly exploit behavioural biases.
- Firms winning business by making the best offer to consumers and delivering it, not by colluding with each other or excluding rivals.
- Firms that can enter and grow without facing undue barriers or costs.
- Firms that have the freedom and flexibility to develop new products and services and a regulatory framework that adapts to keep pace with change.
- Firms treating customers fairly, knowing that unfair treatment will have both commercial and regulatory consequences.



If there is weak competition, it is typically the consumer that ends up paying.



¹ Our Future Approach to Consumers and Our Approach to Authorisation have been published. Our Approach to Market Integrity, Our Approach to Supervision and Our Approach to Enforcement will be published in 2018.



Encouraging competition in retail banking

Retail banks face some important regulatory barriers to entry because consumers need to trust the firms that are holding their savings. However, the Independent Commission on Banking identified weak competition in retail banking, which could be limiting choice for consumers.² So the PRA and the FCA have worked together to identify ways of encouraging competition in this sector, for example, by amending capital requirements and creating the New Bank Start-up Unit.

In March 2013, the Bank of England and the FCA's predecessor, the Financial Services Authority, introduced changes at authorisation that reduced capital requirements for new entrant banks that are smaller and less systemically important.³ This proportionate approach reduced barriers to entry without adding unnecessary risks to the safety and soundness of the UK financial system.

By offering assistance to prospective banking applicants and newly authorised banks, the New Bank Start-up Unit helps stimulate competition and drive innovation to promote better outcomes for consumers. The Unit gives these firms the information and materials they need to navigate the process of becoming a bank, as well as focused supervisory resource during the early years post-authorisation. We are taking a similar approach with our new Asset Management Hub, which we launched earlier this year.

Our powers

To date, the majority of our competition work has been carried out under the Financial Services and Markets Act 2000 (FSMA). We can investigate markets where competition may not be working well for consumers, and intervene where appropriate, for example, by making rules. We can only use these powers for the firms and activities we regulate.

However, we have also been given concurrent competition powers with the Competition and Markets Authority (CMA) for financial services. This brings us into line with other sector regulators such as Ofcom. This means we also have powers under the Enterprise Act 2002 to investigate whether any market for financial services is working well, expanding our powers of investigation beyond those firms and activities that we currently regulate. We can also make a market investigation reference (MIR) to the CMA to investigate a particular market or sector in more depth. Only the CMA has powers to decide whether mergers should be

prohibited on competition grounds, but we may give them information about the firms or markets affected by a proposed merger.

Under our concurrent powers we also have powers to investigate and enforce against any breach of the Competition Act 1998 (CA98) in financial services. Only one authority can formally investigate or take enforcement action on a specific case at any one time. We discuss with the CMA who is best placed to do so and seek to reach agreement as to which authority the case should be allocated to, but ultimately the decision rests with them.

In certain circumstances, the European Commission (EC) may take a competition law case involving financial services in the UK, and we cannot exercise our competition law powers for that case. The EC would consult with us before this happens. We expect this to change when the UK leaves the EU.

Q1.

Do you have a clear understanding of the FCA's statutory remit, competition powers and aims in advancing its competition objective? If no, what more could we do to explain our competition remit and powers?

² Independent Commission on Banking, Final Report: Recommendations, September 2011.

³ Bank of England and Financial Services Authority, A review of requirements for firms entering or expanding in the banking sector, March 2013, page 9.



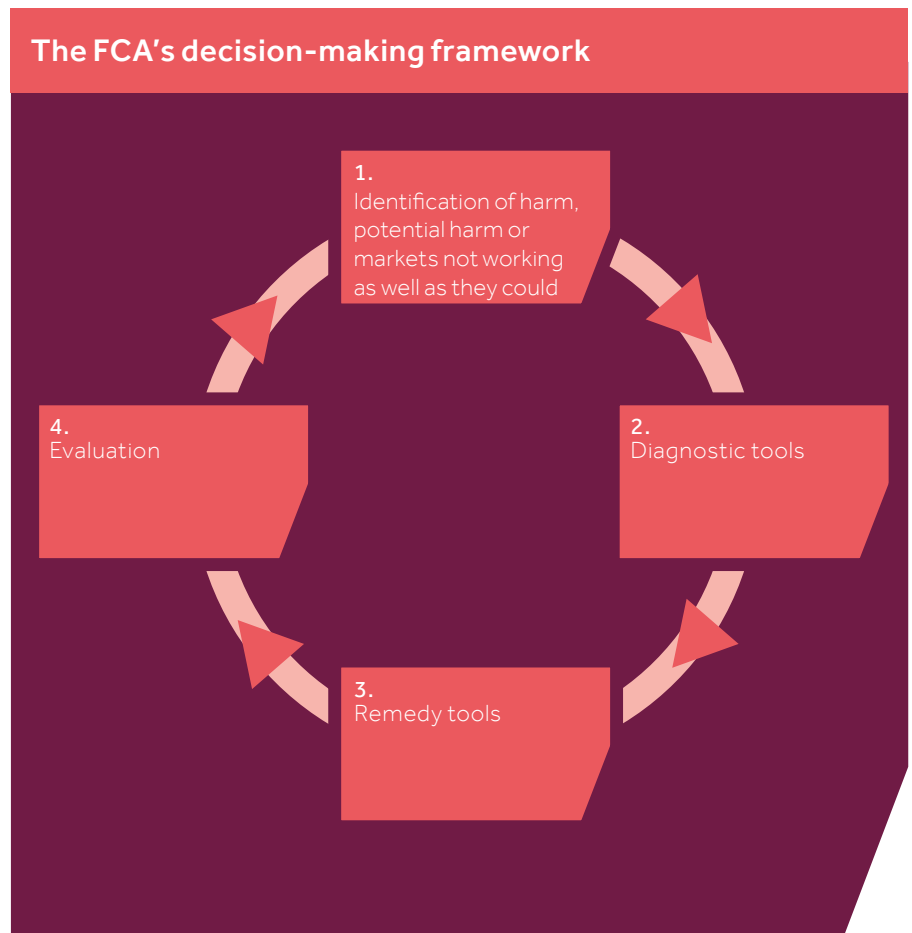
Chapter 2

Our decision-making framework

In our Mission, we explain our four step decision-making framework. This illustrates how we identify potential harm, diagnose and remedy features of a market that do not work well for consumers, and evaluate the success of those remedies to inform our future decisions.

We use this framework across the FCA to diagnose a wide range of harms, their impact, who is affected and which remedies will deliver the greatest public value. It also ensures we apply a consistent approach to balancing competing priorities in our work and make decisions about how our individual functions, such as policy, authorisation, competition, supervision and enforcement, operate.

While this document looks specifically at our approach to competition, this framework also covers our consumer protection and market integrity objectives. It enables us to choose the most appropriate diagnostic and remedy tools to tackle the actual or potential harm we identify in all areas of our work.





Identifying potential harm

Competition is complex and no single benchmark can measure how effectively it is working. However there are a range of market characteristics which can indicate weak competition. These include:

Concentration – Markets with only a few suppliers can give these firms market power, meaning they no longer need to compete hard to attract and retain customers. A firm with significant market power may be able to exploit its customers or exclude rivals. Highly concentrated markets can also make it easier for firms to co-ordinate their actions.

Barriers to entry and growth – Challenger firms are an important source of competitive pressure for established businesses, as well as bringing new ideas and innovation. In markets where challengers cannot enter or grow, established firms tend to be less responsive to customers, less efficient and less innovative.

Integrated supply chain – A firm can be involved in several different stages of a supply chain ('vertical integration'). This can make a market more efficient by creating efficiencies in the supply chain. However, vertical integration can sometimes create conflicts of interest or allow firms to exclude rivals and so avoid competitive pressure.

Barriers to switching – Consumers who cannot freely move to the best value firm are harmed directly because they cannot access the product that best suits their needs. Additionally, if firms cannot win business by offering better value, they have less reason to cut prices, improve quality or innovate. Barriers to switching, such as exit fees, unwieldy or time-consuming processes, will prevent or deter consumers from taking their business elsewhere.

Price discrimination – In markets where firms broadly charge the same price to all customers, switching by a minority of informed and engaged consumers can drive price down and quality up for everyone. However, where firms can discriminate then only those who switch may get the benefits, possibly at the expense of those who are less engaged.

Lack of access to information – Where information is hard to find or understand and compare, it can be difficult for consumers to understand and compare products. This can both directly harm consumers and reduce the competitive pressure on firms.

Sustained excessive profitability – When a firm or group of firms compete successfully we might expect their profitability to be high, while less successful firms will make less money. This is part of the competitive process. However where an entire industry is making high returns for sustained periods of time then this may indicate weak competitive pressure.

Complexity – Complex products can make consumers feel that financial decisions are 'beyond them' and so follow a path of least resistance rather than make active choices. In this case, consumers are more likely to end up with products poorly suited to their needs, or be overcharged.

In identifying these market characteristics, we use information from a range of data sources and from across the organisation. We publish summaries in our Sector Views. Markets which show some or all of these characteristics are likely to raise concerns for us that competition may not be working well for consumers.

These types of indicators or characteristics are not necessarily associated with rule breaches or poor conduct by individual firms. So when we look at whether a market is working well we are not necessarily looking only or primarily at conduct or compliance issues. However, there are conduct issues that can concern us from a competition point of view

Q2.

Are there other indicators of potential harm that we should consider in our preliminary assessments of competition?



Anti-competitive conduct

Anti-competitive behaviour can include directly exploiting customers, for example, by charging far too high a price. Or it can involve deliberately reducing competitive pressure, for example, by seeking to unlawfully co-operate with or exclude rivals. These actions are prohibited by CA98 and enforcing this legislation is an important part of our competition remit.

There are two broad prohibitions in competition law. First, firms must not enter into anti-competitive agreements. Cartels and related anti-competitive behaviour can lead to higher prices, lower quality and generally poorer outcomes for consumers – often on a very significant scale. In 2010 the EC estimated that the removal of overcharges by cartels resulted in approximately €7.2 billion in benefits for consumers.⁴

Second, a firm with substantial market power (a firm that is 'dominant' in a market) must not abuse that position by behaving in a way that exploits its customers or excludes its rivals. Most financial services markets have many firms in them, so dominance is not an issue. However, there are some where there may be one dominant supplier (which is not in itself a problem) who may abuse that position (which is).

Anti-competitive conduct often happens in markets with weak competitive pressure – which can happen when one or more of the characteristics described above are present. Sometimes we also get direct intelligence about this behaviour through sources, such as leniency applications, Principle 11 notifications, complaints and whistleblowing.⁵ We encourage anyone with concerns about anti-

competitive conduct to contact us. We set out how to do this in our guidance on our CA98 powers and procedures.⁶

Prioritising our work

We prioritise our market studies work alongside our other interventions as part of our annual business planning. We are more likely to prioritise market studies where:⁷

- market characteristics indicate low levels of competitive pressure
- the market size or type of customer indicates harm on a significant scale or severity
- vulnerable consumers may be at particular risk
- we have the power to intervene
- our intervention is likely to improve market outcomes

We are less likely to prioritise work in markets where:

- market or regulatory changes are already likely to address competition concerns in the near future
- another organisation can better address specific competition issues

Indicators of potential harm can help us prioritise. However, we need to do more in-depth work to investigate the extent of actual harm, and diagnose the cause.



In 2010 the EC estimated that the removal of overcharges by cartels resulted in approximately €7.2 billion in benefits for consumers.



⁴ Davies, S; Ormosi, P (2014), *The economic impact of cartels and anti-cartel enforcement*, CCP Working Paper.

⁵ See FG15/8: The FCA's concurrent competition enforcement powers for the provision of financial service, : Chapter 3 – www.fca.org.uk/publication/finalised-guidance/fg15-08.pdf

⁶ See FG15/8 – www.fca.org.uk/publication/finalised-guidance/fg15-08.pdf

⁷ Similar but not quite identical factors apply to our competition law enforcement work. See FG15/8, pages 11, 12 – www.fca.org.uk/publication/finalised-guidance/fg15-08.pdf



Diagnosing the cause of harm

Diagnostic Tools

In the second, diagnostic, stage of our decision-making framework, we set out our 'theories of harm' based on indicators of the potential harm we have identified. A theory of harm is a hypothesis of how competition may not be working in consumers' interests, and how consumers may be suffering as a result. Our diagnostic work focuses on gathering and analysing evidence to test these hypotheses.

Such investigation may take the form of a:

- Call for input
- Market study
- CA98 investigation

We also have a range of supervisory tools which we can use in this diagnostic stage. These are discussed in our forthcoming 'Our Approach to Supervision'.

If we consider the issue is a priority, we can start a call for input or market study. We make it clear that this does not imply that there has been misconduct by individual firms or that we will necessarily intervene. However, we can only start a CA98 investigation if we have evidence that firms have behaved in a way that gives us reasonable grounds to suspect a breach of the law. We explain this in more detail in our guidance on CA98.⁸ In this situation we will be looking for conduct that infringes CA98 and its EU equivalent.

Calls for input

Our calls for input are public invitations for views, evidence, examples and suggestions from all interested stakeholders. Rather than requesting specific information or data, we use calls for input as a less prescriptive method for gathering information.

We are more likely to issue a call for input when:

- we are looking at markets where we do not routinely gather the information needed to start a market study
- the scale of potential harm is significant but our theories of harm are less well developed
- we are looking at a number of interrelated markets
- the market is emerging or changing rapidly

Calls for input help us better understand emerging issues in a market and the context, cause, scale and type of the harm we want to prevent. The information we get from a call for input may lead us to launch a market study, to propose remedies or to take no further action.

Market Studies

Market studies are in-depth, evidence-driven investigations, typically taking 12-18 months to complete. Annex 2 contains the

⁸ FG15/8, page 11 – www.fca.org.uk/publication/finalised-guidance/fg15-08.pdf



Big Data – helping or hindering competition?

Firms have always collected and used data about their customers to shape their products, services and business models. However, the relatively swift emergence of 'Big Data' has the potential to alter the way the industry assesses risk, prices products and selects customers.

For example, potential concerns in retail general insurance include whether 'high risk' consumers will be able to get affordable insurance and whether the use of Big Data reduces risk-sharing across consumer groups. There are also potential concerns about factors that have nothing to do with risk and cost becoming more widely used in pricing.

We issued a Call for Input on Big Data in retail general insurance for two types of retail insurance – 'motor' and 'home and contents'. We wanted to better understand whether Big Data affect consumer outcomes and competition in these products and whether our regulatory framework affects developments in Big Data in retail general insurance.

We found that Big Data is delivering a range of benefits for consumers in motor and home insurance, and that the potential concern about 'high risk' consumers has not yet materialised in these markets. We also decided to carry out discovery work looking at pricing practices in retail general insurance firms. We know that both technology and the way firms use it evolve quickly. We will regularly monitor developments in Big Data across financial services when reviewing intelligence that feeds into our annual Sector Views.

market studies, calls for input and other competition reviews we have launched to date.

A market study defines a number of questions to explore or theories of harm (as discussed above) to test. We publish the questions we want to answer in our terms of reference at the start of every market study.⁹ The set of questions or theories of harm will focus primarily on how competition works in a market but – since our objectives are interrelated – may also cover how competitive dynamics affect consumer protection or market integrity.

We then engage in extensive research, data-gathering and consultation with firms, consumers and other stakeholders such as charities and trade bodies. While this demands significant resources from both the FCA and other stakeholders, especially firms, market studies can result in far-reaching changes across markets.

This means it is important that we understand all stakeholder perspectives, that our conclusions are based on robust evidence and that our proposals reflect reality.

Deciding on the best remedy

Once we have gathered our evidence, we will generally publish an interim report. This report outlines our preliminary findings and proposes possible solutions for addressing any concerns we have. Through open consultation, we then seek feedback on both the findings and any of our proposed solutions. After considering this feedback and undertaking any further work it prompts, we publish a final report which sets out our conclusions and the way forward on solutions or 'remedies'.¹⁰

Both market studies and our cross-cutting supervisory work take a cross-market view. However, while

our cross-cutting supervisory work typically focuses on current or emerging risks across a number of firms within a sector, market studies take a holistic view of a market and try to understand the impact of market forces and structures. A market study is likely to consider the behaviour of consumers and potential new entrants, as well as regulated firms. For more information on our cross-cutting supervisory work see our forthcoming 'Our Approach to Supervision'.

⁹ See FG15/9: Market Studies and market investigation references – www.fca.org.uk/publication/finalised-guidance/fg15-09.pdf

¹⁰ See FG15/9, page 18 – www.fca.org.uk/publication/finalised-guidance/fg15-09.pdf



Often we do not need to use our formal information-gathering powers to get the data we need.



Gathering data from firms

As explained, a market study is an analysis of an entire market, not an investigation into the behaviour of specific firms. Since it is usually not cost-effective to ask all firms in a market to supply data, we typically select a sample of firms:

- who, together, provide a representative picture of the market, or
- whose combined market share represents a significant proportion of the market

These samples generally include the largest firms, but we also want to understand the experience of smaller firms so will include some in the sample. We aim to be proportionate in our data requests and can tailor requests according to the size of a firm. Being selected as part of a sample for a market study does not imply a firm has breached our rules or behaved badly.

Often we do not need to use our formal information-gathering powers to get the data we need, though we can use them and have done so in the past at firms' request.

We aim to be as transparent as possible about the basis for our conclusions, to ensure we can have a meaningful dialogue with stakeholders when we publish our interim report. However, we cannot publish certain data (such as personal and commercially sensitive data). We publish data when and as the law allows us to do so.¹¹

CA98 investigations

We have published detailed guidance on our competition law powers and procedures.¹² The stages of an investigation consist of fact-finding and analysis, provisional findings and ultimately a final decision. However, the law and the need to protect parties' rights of defence mean that we can only make limited information public during our CA98 investigations.

We will discuss with the CMA and, where relevant, the European Commission whether we are the authority that should take a case forward. If so, we can use powers to request information, such as documents and data, and can also conduct compelled interviews and site visits. If, after investigation, we come to the provisional view that competition law has been infringed, we will issue a 'statement of objections' to the firm. This sets out the applicable law, evidence, our analysis and our proposed decision. Firms can inspect copies of the relevant documents we disclose and can make both written and oral submissions to our Competition Decisions Committee. This Committee will take a final decision and may impose financial penalties.

Some breaches of competition law may also breach authorised firms' obligations under FSMA or other legislation. In these instances we may take enforcement action under our other powers as well as, or instead of, CA98. We decide which of our powers are most appropriate on a case-by-case basis. We have a statutory duty to consider whether it would be more appropriate to use our CA98 powers before using certain FSMA powers, and we will make a decision depending on the facts of the case.¹³

¹¹ See FG15/9 – www.fca.org.uk/publication/finalised-guidance/fg15-09.pdf

¹² See FG15/8 – www.fca.org.uk/publication/finalised-guidance/fg15-08.pdf

¹³ See FG15/8 – www.fca.org.uk/publication/finalised-guidance/fg15-08.pdf



Remedies

When will we take action?

The type of action we take to respond to competition problems differs between CA98 investigations on the one hand, and market studies on the other. Following a CA98 investigation we may take action to punish individual firms who have breached the law, both to end that behaviour and to deter further breaches from other firms. Following a market study, we typically make rules or take other action to make the market work better in the future, although we will clearly also take steps to address past misconduct if we find it.

CA98 investigations

Under CA98 we can investigate financial services firms when we have reason to believe they have breached competition law. Based on our investigation, we may:

- Issue an infringement decision, which may involve imposing penalties and/or other directions on firms. We will issue an infringement decision after we have issued a statement of objections and received the parties' representations. We publish infringement decisions in redacted form.
- Accept commitments from firms that they agree to change their conduct in a way we think addresses our competition concerns.

- Publish a 'no grounds for action' decision if we have not found sufficient evidence of an infringement.
- Close our investigation on the grounds of administrative priorities at any time.

Market Studies

We will consider taking action if our analysis identifies competition problems or other issues in the market that are leading to harm. However, we will only intervene where we judge this will be beneficial and proportionate to the concerns we have identified.

Targeted intervention in the credit card market

Sometimes we find that competition is working well for most consumers, yet there is harm to a smaller population of consumers that justifies our targeted intervention.

In 2014, we took over regulation of consumer credit. The credit card market is a major part of this sector, with around 30 million UK adults having a credit card (60% of the adult population). We wanted a better understanding of this market, to identify levels of problem debt and assess if competition was working well for consumers, so we carried out a market study.

In our final findings report, we said we had found that competition was working fairly well for most credit card consumers.

However, we found significant concerns about the scale, extent and nature of problem credit card debt and firms' limited incentives to reduce this. Our findings included:

- around two million people had carried debt greater than 90% of their credit limit for at least 12 months
- another 1.6 million people were repeatedly making minimum repayments on their credit card debt and many did so for a number of years
- we did not find widespread issues about fees and charges, but we did identify one firm failing to treat customers fairly when it came to penalty fees and charges

We did a number of things to remedy these issues. We took supervisory action to resolve the penalty fees and charges issue. We accepted an industry proposal to give customers greater control over credit limits. We trialled alternative ways to prompt borrowers to repay more than the minimum required. And we consulted on two rules. The first required firms to intervene earlier when customers show signs of struggling with their finances, and the second requires firms to take action once a customer has been in significant debt for a considerable period.



Changing the 'rules of the game' can have a significant impact on how firms compete, and thus on consumer outcomes.



What action will we take?

We design remedies on a case by case basis. If possible, we aim to address the root cause of consumer harm by improving how competition works in the market, and so improve the consumer outcomes it delivers. We may also seek to protect consumers directly. In either case we consider not only the direct impact of our intervention, but also the likely response of both firms and consumers – the market dynamics. The scale and scope of our intervention is proportionate to the harm we have identified.

The package of remedies we implement can include some or all of the following:

Rule changes. Changing the 'rules of the game' can have a significant impact on how firms compete, and thus on consumer outcomes. Depending on the type of issue identified, we may make rules about:

- providing consumers with better information, for example, requiring general insurance firms to clearly and prominently disclose the customer's previous year's premium at each renewal, to increase awareness of premium increases
- how choices are presented to consumers, for example, changing the way firms present repayment options to credit card holders
- governance, for example, requiring fund boards to consider whether the level and structure of their charges are in investors' best interests
- specific actions, for example requiring asset managers to pass on box profits to investors, or requiring credit card firms to take steps to intervene when customers are persistently indebted

As well as writing new rules, we also aim to remove rules that are obsolete or hinder competition,

such as our recent changes to remove ineffective disclosure requirements.¹⁴

When we propose new rules following a market study, we follow the process required by FSMA. So we consult on any proposed rules or rule changes and conduct a cost-benefit analysis of the expected impact. This allows our stakeholders to see the evidence and reasoning behind our proposals and to feed in views.

Publishing guidance. We can also provide new or revised guidance on existing rules to achieve similar, direct changes to a market. While we cannot enforce guidance, it sets a standard for best practice which many firms follow when implementing our rules.

Supervision or enforcement activity. Where we are concerned about harm due to behaviour by a sub-set of specific firms – as opposed to a market-wide issue – we can use targeted supervisory or enforcement work. This is a more proportionate response than market-wide remedies for behaviour that is confined to a small number of firms. For example, we undertook supervisory work with firms as a part of the investment and corporate banking market study to examine the policies and practices for Initial Public Offerings' allocations to shareholders.

Voluntary solutions. We encourage industry to propose voluntary solutions to the problems we have identified. For example, our work in the credit card market led to the industry developing tools to give consumers greater control over their finances by providing timely information on their borrowing.

If a remedy needs to change over time in response to changing market conditions then an industry solution may be the most effective and cost efficient choice.

¹⁴ See PS16/23: Smarter Consumer Communications: Removing ineffective disclosure requirements in our Handbook – www.fca.org.uk/publication/policy/ps16-23.pdf



Publishing data. Publishing data on key market indicators (so-called 'sunlight' remedies) can help consumer groups, market commentators and other users assess products and make comparisons. For example, we published the interest rates offered by retail banks for cash savings accounts and claims data for general insurance. By making this information public, we aim to improve transparency, influence consumer and firm behaviour and give firms an incentive to improve the value of their products.

Market Investigation References. We can also make a MIR to the CMA. We are more likely to do this when we are concerned about firms or activities that are outside our regulatory perimeter. For example, we made an MIR about investment consulting after our Asset Management Market Study found concerns about that market, much of which is outside FCA regulation.

Engaging with other agencies. Where another government department or agency is better placed to act we will share our findings and provide any support they need.

Not taking action. Lastly, we may decide to take no action. We are most likely to do this if we do not have clear evidence of significant consumer harm or we are unable to identify an intervention that would successfully address the issue.

Q3. **Are there other tools we could consider when designing remedy packages?**

Regulating for the real world

When thinking about remedies we need to recognise the limits of relying on consumer engagement and active choice to drive good outcomes. Successful competition remedies make it easier for consumers to exercise choice and bolster incentives for firms to change because of the threat of switching or wider reputational concerns. In some markets the active choices of the minority benefit the (less active) majority. However, in other markets this is not the case and we may need to act to protect those consumers.

In asset management, for example, with evidence of very low engagement among some investors, we proposed governance changes to strengthen the duty on firms to act in investors' best interests when it comes to value for money.

In 'Our Future Approach to Consumers' paper we set out how behavioural economics informs how we regulate. This is extremely relevant to the way we design remedies in our competition work.

Competition is most effective when consumers are able to judge what products offer the best value and reward firms with their business. This requires us, for example, to make sure that firms supply customers with clear and accurate information. But it also requires us to be realistic about how consumers assess and compare products, to recognise 'behavioural biases' and to ensure our remedies are designed for real world behaviour rather than textbook rationality.

We can use 'nudges' to prompt engagement at crucial moments, for example insurance renewal (described below). We can also regulate how firms present choices to consumers, for example by banning pre-ticked boxes for optional insurance add-ons.

We can also use consumer research, including lab and field trials, to test how our remedies actually influence consumer behaviour in practice.

Switching customers on to better deals

There are over 40 million home and motor insurance customers in the UK. Firms generally increase premiums for existing customers every year, yet only a very small percentage of customers decide to switch to a better deal.

We carried out extensive behavioural trials with over 300,000 customers across three firms to find out what was most likely to help consumers to engage at renewal and switch. As a result, from April 2017, we required firms to include the previous year's premium, along with standard advisory messages, when they sent out renewal notices. We will be monitoring subsequent switching rates to see how effective this has been in encouraging customers to switch to better value products.



Measuring our impact

Our Mission emphasised the importance of evaluating our interventions, particularly looking at the impact of our interventions and the outcomes in markets.

Impact of our interventions

We always aim to design packages of remedies that address consumer harm, that are proportionate and that are realistic in terms of likely response by both firms and consumers. For rule changes and guidance in particular, cost-benefit analysis and stakeholder consultation help with this.

However, we can never be sure that our remedies will work exactly as we expect. So testing the effectiveness of our interventions after the fact is critical. Evaluation helps ensure that:

- we are transparent about the success or failure of our remedies
- we change ineffective remedies
- we demonstrate and, where possible, measure the public value of successful remedies
- we get better at designing remedies in the future

However, post-implementation analysis is rarely straightforward. The dynamism and complexity of financial markets mean it is often difficult to pin down the response of firms or consumers to a particular intervention, or measure the scale of the effects. We therefore conduct detailed evaluations only for certain interventions.

Since we only began competition work in 2013, we have only recently begun to evaluate our initial interventions. Our first evaluations will focus on guaranteed asset protection (GAP) insurance and the New Bank Start-up Unit.

Market outcomes

We will continue to develop our key indicators of competition in markets, and to improve the market data we collect to enable us to monitor this in real time.

These data sets range from traditional measures of competitive pressure, such as market share and profit margin, to our unique data sets, such as data on consumer complaints from our contact centre.

Q4.
Has this document set out the FCA's approach to competition clearly? Are there other issues relating to our approach to competition that could benefit from further clarification?



Annex 1: Questions

Q1.

Do you have a clear understanding of the FCA's statutory remit, competition powers and aims in advancing its competition objective? If no, what more could we do to explain our competition remit and powers?

Q2.

Are there other indicators of potential harm that we should consider in our preliminary assessments of competition?

Q3.

Are there other tools we could consider when designing remedy packages?

Q4.

Has this document set out the FCA's approach to competition clearly? Are there other issues relating to our approach to competition that could benefit from further clarification?

How to respond

We are asking for responses to these questions and comments on the paper by 12 March 2018.

You can send them to us using the form on our website at:
www.fca.org.uk/approach-competition-form

Or in writing to:
Competition and Economics
Division,
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Email:
approachtocompetition@fca.org.uk



Annex 2: Market studies, calls for input and other competition reviews launched by the FCA

	Date launched	Final report published
<u>General insurance add-ons market study</u>	December 2012	July 2014
<u>Cash savings market study</u>	October 2013	January 2015
<u>Retirement Income market study</u>	February 2014	March 2015
<u>Wholesale sector competition review – call for inputs</u>	July 2014	February 2015
<u>Credit cards market study</u>	November 2014	July 2016
<u>Investment and Corporate Banking market study</u>	May 2015	October 2016
<u>Call for inputs on competition in the mortgage sector</u>	October 2015	May 2016
<u>Call for inputs: Big data in retail insurance</u>	November 2015	September 2016
<u>Asset management market study</u>	November 2015	June 2017
<u>Retirement outcomes review</u>	July 2016	Ongoing
<u>Mortgages market study</u>	December 2016	Ongoing
<u>Strategic Review of Retail Banking Business Models (joint work with Supervision)</u>	May 2017	Ongoing
<u>Investment platforms market study</u>	July 2017	Ongoing
<u>Wholesale insurance brokers market study</u>	November 2017	Ongoing



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