

## **BBA The Financial Conduct Authority – A Keynote Briefing – 25 January 2012**

### **Title: An effective Consumer Panel Speaker:**

#### **Adam Phillips – Chair of the Financial Services Consumer Panel**

Thank you for the kind introduction Peter<sup>1</sup>.

Some of you here today may think that with all the other problems the industry is facing at the moment, the last thing it needs is an effective Consumer Panel. If that is the case, I hope that in the next twenty minutes or so that I will be able to persuade you to think again.

FSMA established two statutory Panels; a Consumer Panel and a Practitioner Panel. Soon after it started work, the FSA was persuaded that a Smaller Businesses Practitioner Panel was needed and the new Bill will propose that the FCA will have in addition a fourth panel representing markets<sup>2</sup> practitioners. However, the new Bill will not require the PRA to have a similar stakeholder structure, an issue to which I intend to return a little later.

FSMA requires the FSA to consider representations made by its Panels and, if the Authority disagrees with a view expressed or proposal made in the representation, it must give the Panel a statement in writing of its reasons for disagreeing. Like all legislation this basic requirement needs to be operationalised and so each has an MoU with the FSA and agreed Terms of Reference. These are published on the Panel's website and explain how we work together. The key elements of the Consumer Panel's terms of reference are that:

1. The main purpose of the Panel is to provide advice to the FSA. It does not undertake consumer education or take up individual consumer complaints.
2. It is expected to:
  - a. represent the interests of consumers by advising, commenting and making recommendations on existing and developing FSA policy and practices as appropriate;
  - b. speak on behalf of consumers by reviewing, monitoring and reporting to the FSA on the effectiveness of FSA's policies and practices in pursuing its duties;
  - c. keep under review and influence actual and potential developments in financial services to enable it to fulfil its representational role effectively.
3. In addition, it can advise the Government on the scope of financial services regulation.
4. The emphasis of the Panel's work is on activities that are regulated by the FSA, although it may also look at the impact on consumers of activities outside but related to the FSA's remit.
5. The Panel must have regard to the interests of all groups of consumers including those who are particularly disadvantaged in the context of financial services and those who have little or no access to financial services.
6. The Panel can speak out publicly when it wishes to draw attention to matters in the public interest and when it disagrees with the FSA.

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<sup>1</sup> Peter Tyler

<sup>2</sup> Markets Practitioner Panel - to represent the interests of practitioners who are likely to be affected by the exercise by the FCA of its functions relating to markets

The definition of a consumer in FSMA is very broad - essentially anyone who is using or even contemplating using financial services<sup>3</sup>. The definition includes sole traders and small enterprises.

There are thirteen of us who, in addition to being consumers of financial services have a range of experience relevant to the work of the Panel. They include; lawyers, journalists, researchers, ex-regulators, consumer advisers, people who have worked in the financial services industry, economists, academics and business consultants. They are people who are able to discuss and have a view on FSA policy proposals and to raise issues of consumer concern. The Panel Positions itself as a “constructive but nevertheless critical friend” of the FSA.

The whole Panel meets once a month but we also have three working groups dealing with specific areas, including one solely focusing on Europe, which meet monthly two weeks after the Panel meeting and ad-hoc subgroups which are set up to address specific topics. Our meetings are arranged so that we can provide helpful input into the FSA Board’s agenda if appropriate. In addition the chairs of the three panels have a monthly teleconference to discuss topics of common interest, since there are issues on which all the Panels agree and where our cooperation and combined influence is helpful in guiding the regulator.

As well as talking to the sector and policy teams in the FSA the Panel has a regular programme of meetings with the various consumer bodies, governmental organisations and trade associations, whose opinions and actions are relevant to our work. In the last few years we have found ourselves increasingly drawn into the European debate. We are partners of BEUC, the European Consumer organisation, we have a programme of meetings with the Commission and the European Parliament, the Panel’s Vice-chair is also vice-chair of the EIOPA insurance stakeholder group and I am a member of the IPISC stakeholder group which advises ESMA. This is a significant commitment of resource, but there are over twenty<sup>4</sup> major legislative proposals relating to financial services going through the Parliament at the moment and we feel it is necessary to ensure that the UK consumer is well-represented in any discussion that may involve maximum harmonisation. Most European consumer bodies are poorly resourced and have little capacity or the experience needed to deal with the complexities of financial regulation across 27 member states. The experience gained by members of the Panel working with the FSA is extremely useful when dealing with important aspects of proposed legislation, particularly where the objective is to get regulation which achieves its objectives efficiently without loading more cost onto the industry and therefore the consumer than is absolutely necessary.

The Panel is supported by a secretariat employed by the FSA. It has a budget for commissioning research and consultancy independently of the FSA. The secretariats for all three panels are part of the Corporate Services department which is responsible for managing the FSA’s secretariat for the Board and its sub-committees. As a result we are effectively integrated into the agenda management of the FSA. This is a great improvement

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<sup>3</sup> s404e of FSMA 2000 *Meaning of “consumers”* defines it as anyone who has used or even contemplated using services provided by authorised persons, appointed representatives, payment service providers or electronic money issuers. Subsection 1(b) further defines those with a relevant right or interest if that interest is derived from or attributable to the use of services or has their rights affected by those acting on their behalf.

<sup>4</sup> [http://ec.europa.eu/internal\\_market/finances/docs/110209\\_progress\\_report\\_financial\\_issues\\_en.pdf](http://ec.europa.eu/internal_market/finances/docs/110209_progress_report_financial_issues_en.pdf)

on the situation four years ago when we were not joined up with central management. That made it much more difficult to contribute effectively to the policy debate at the most senior level. It's clearly not very helpful to arrive with a well-evidenced argument for a particular approach to policy the month after the decision has been taken but, given the confidential nature of some of the issues being discussed, it is not always evident what kind of input is needed and when would be most helpful time to deliver it.

Some of you may wonder why the FSA needs to have advisory groups like this when the Board has a majority of non-executive directors. You should to ask Adair Turner and Hector Sants for their opinion, but I think that it is often difficult for non-executive directors to question regulatory policy at the level of detail needed to ensure that the final decision is the best possible, not just the best of the options that were considered by the management team. The adversarial nature of the external regulatory debate and the promotion of sectoral interests by trade associations and lobbying bodies inevitably encourages a defensive attitude in the regulator. This makes it difficult to discuss policy alternatives. One of the strengths of the Panel approach is that the individual panels work through consensus, so the regulator has access to an environment where it can test assumptions which, if they are accepted are likely to work in the outside world. Of course the three Panels don't agree about a lot of issues, but disagreement is more likely to relate to issues of specific application than to principle. The occasional issues where all three Panels agree, but the FSA disagrees are ones which are particularly helpful to the Board when coming to a view about policy.

I have talked at some length about the Panel's relationship with the Board, because the quality of governance of the FSA is important, but that is only one relatively minor aspect of the work of the Consumer Panel. By far the largest part of our work falls into two categories:

- the Panel's strategic priorities; and
- responding to the FSA's requests for comment and advice.

The Panel aims to spend about half its time working on areas where we think there is an issue which falls within our scope, where we think we can make a difference and which is unlikely to be effectively addressed by other organisations. Our current priority areas are:

- The shape of future regulation
- EU regulatory and legislative issues;
- The future regulation of consumer credit;
- The Mortgage Market Review;
- The advice gap; and
- The effective regulation of business conduct

The reason most of these topics are priorities is obvious and most of them will continue to be priority areas when the FCA takes over, with the possible change that insurance will replace the MMR. The advice gap is not currently a focus of much attention in the FSA, their last piece of published work being the guidance consultation on simplified advice. This was the result of several years of lobbying by the Consumer Panel. We are continuing to research the topic; we published a report on what we call "Straightforward Outcome Products" last autumn and will be publishing research on the various forms of advice option this spring. We

hope that this work will stimulate a constructive debate which will encourage the regulator to think more creatively about what can be done to ensure that people with moderate savings can get access to appropriate advice and suitable products at reasonable cost. This is a good example of the pro-active work of the Panel on a topic which is not of much current concern to the regulator

I have explained how all three panels work with the FSA. However, there is a significant difference between the Consumer Panel and the Practitioners. The industry has the resources to provide effective and well researched responses to consultations issued by the FSA. As a result the practitioner panels do not usually respond to CP's or DP's. However, this is not the case with consumer groups. Most of consumer groups have limited funds for policy analysis and research. Their work is necessarily focused on their particular sectoral interests. As a result, the Panel not only advises the FSA in policy discussions before a consultation is issued, but it also needs to respond to consultations and discussion papers. In the last consultation on platforms we were the only consumer group to respond and we have regularly been the only consumer group to engage with the more technical aspects of the Retail Distribution Review and MMR. Without a consumer panel the FSA would have been even more reliant on policy advice from the industry than it already is.

This leads me on to the topic of regulatory capture. There is no doubt that the siting of the Panel inside the FSA and our involvement in the early stages of policy development exposes the Panel to an element of regulatory capture, compared with an independent consumer voice. Once we have agreed to disagree with the FSA about a particular issue, we have to accept their decision and, although we can argue against it in public, it can be counterproductive for us to mount an extended lobbying campaign if we are to continue to work together on other issues. This is the difference between the Panel and other consumer interest groups. They are able to campaign and mobilise public support to persuade the regulator to act. However, this type of lobbying tends only to be effective once significant consumer detriment has become apparent. The Panel on the other hand has access to the policy teams at the FSA and can, if necessary commission research to evidence its argument. Its position inside the FSA and ability to work with confidential information means that it can be effective at helping the FSA identify possible problems and the root cause of regulatory failure before the problem has become significant. This may seem a rather minor issue to those of you not closely concerned with regulatory policy, but it is at the heart of the debate, which Martin Wheatley touched on, about how to regulate in a way which is not unduly costly or which restricts good innovation. By good innovation I mean product and service developments which deliver real value to the consumer, rather than simply providing a way to extract money from consumers.

As Martin Wheatley has already explained pro-active regulation seeks to deal with problems at an early stage ideally before they have crystallised and certainly before the need for any significant redress. This approach works well for both industry and consumers. It builds consumer confidence and it is less costly for the industry, because significant amounts of redress can be avoided. I hesitate to mention PPI, since it is always used as an example, but it is a particularly good example of a product which could be useful for many consumers that was sold in a way which had the potential to create significant consumer detriment. Because the industry and regulators failed to act swiftly it has created a huge cost for the industry and also for consumers since they will ultimately bear the additional cost.

Before going on to talk about how the Panel will work in the new regulatory structure I would like to give some examples of what we have achieved with the FSA. Given the way that the media reports regulation as a kind of football match with winners or losers, focusing on the strikers, rather than the midfield, you may have missed our work unless you were directly involved.

The Panel has consistently supported the RDR and its attempt to raise professional standards and to remove conflicts of interest from the advice process. As the RDR progressed it became apparent that platforms would play a significant role in the new post RDR world. Platforms are not very profitable at the moment in spite of having assets under management of £140Bn in 2010 but the market potential is over £1,000Bn. The Panel was concerned that platforms should conform to the principles of the RDR. 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 doing further more detailed work which I hope will result in a more economically efficient platform industry and a better outcome for consumers in the medium term. No other consumer group responded to the consultations.

Another example where the Panel has been able to make a unique input is the Mortgage Market Review. Misselling of mortgages during the last housing price boom led to serious consumer detriment. The FSA was concerned to ensure that this should not happen again and, as some of you will know, it came up with a detailed proposal to regulate the sales process and, in particular to propose guidance on the affordability calculations mortgage providers should follow. This was supported by some consumer groups who had a great deal of well-researched evidence about the detriment which had been caused. However, the Panel was not convinced that the FSA's cost benefit and economic analysis was sufficiently robust to justify the proposals being made. The industry reached the same conclusion. The Panel's privileged position inside the FSA meant that we were in a better position than an external organisation to discuss the FSA's analysis and the further work which they carried out during last year. One of the penalties of asking the FSA to think again has been the resulting 400 page consultation which some of you are no doubt wading through at the moment. Our initial reaction is that the new consultation is a great improvement on the original. An unusual aspect of the MMR is that mortgage regulation has prudential aspects. In the present structure where both conduct and prudential issues are regulated by the FSA we were able to discuss some of the issues that relate to the potential interaction of conduct rules and prudential controls. This was possible in the current structure, but will be more difficult in the future when we will have no statutory relationship with the PRA or FPC.

That leads us on to the role of the Panel in the new world. At present Section 11 of FSMA enables the Panel to ask the FSA about any aspect of regulation. In the future we will only have the power to request a response from the FCA. Since the PRA will regulate significant elements of the insurance market and the prudential side of mortgages, we are concerned that the Bank is not well equipped to deal with consumer issues. I am sure that Martin Wheatley will represent the views of the FCA to the PRA and FPC but, as I hope I have made clear, the Panel has been most effective when working lower down the system before policy has hardened, challenging assumptions and relying on the use of independent evidence. I would like to see the Consumer Panel having a formal statutory relationship with

the PRA, copying across sections 10 and 11 of FSMA into the new world of twin peaks. There would be a lot of benefits, especially in the area of ensuring an informed awareness of consumer issues and joined up thinking between the FCA, PRA and FPC. Furthermore the Panel's insight would provide one of the very few checks on the level of effective coordination and cooperation between the authorities; insight which external bodies like Parliament could draw on for advice - possibly the reason why the Bank is so strongly resistant to the proposal. There would be no need to create an entirely new Panel and it is hard to see why the costs would be any different from what they are now, apart from some underground fares to travel to the PRA's offices.

We are looking forward to the FCA becoming an effective regulator of financial services in the way the FSA has never been. To be fair, the FSA has made a serious attempt recently to engage with outcome focused regulation in the retail market, but the financial crisis has not made that easy and the work they have done has been more about sweeping up what's left behind after the Lord Mayor's show than leading the procession, to paraphrase the words of Howard Davies the first Chairman of the FSA talking about the type of regulator he did not want the FSA to become<sup>5</sup>. The Conduct focused objective of the FCA gives it a better chance of meeting that aspiration. But to do that it will have to be clearer about what it wants and more determined to achieve what it sets out to do. This means:

- better economic and research analysis, looking at root causes rather than symptoms and having sufficient resources to engage effectively with the PRA and FPC on behalf of the consumer;
- a reasoned debate with the industry and consumers about what it is aiming to achieve and the consequences of regulatory intervention;
- less focus on process and the application of rules and more on the intended outcomes and the extent to which they are not being achieved;
- actions which encourage good behaviour by the industry and rebuild consumer confidence – in our view this requires early intervention, regulatory transparency publicising regulatory action such as warnings and OIVoP's;
- An effective European division which represents the interests of the both the consumer and the industry, something which the FSA has done well.

If the FCA can do this there is a good chance that it will be able to deliver better treatment of consumers, particularly if the FCA gets the powers it needs in the new Bill, the Vickers reforms are introduced into retail banking and the regulation of consumer credit is transferred to the FCA. However, a regulator cannot make people or organisations behave better. What it can do is create an environment which encourages good behaviour, make

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<sup>5</sup> 11 December 2000, speech by Howard Davis (then Chairman of the FSA) to the FSA Conference "A Radical Approach to Regulation" at [www.fsa.gov.uk](http://www.fsa.gov.uk) "And most of all, consumers supported the idea of a proactive regulator, one which tried to anticipate and head off consumer problems in advance, rather than has been sadly the case too often in the ancient regime, coming along afterwards to clear up the mess. Being cast permanently as the man who followed the Lord Mayor's show with a shovel and a bucket is not an attractive role."

clear statements about its intentions, allow reasonable time for organisations to adapt and punish those who fail to meet the requirements. The rest is up to the industry.

I was asked to talk about areas where the Panel might be in conflict with the FCA, PRA or FPC. I hope that will not happen. After all, we have good working relationships with the people who are currently in both the FCA and PRA. However, I was a member of the Panel at the peak of light touch regulation when there was pressure from the Government to dissuade the FSA from action which they thought might damage the financial sector. There is no doubt that concerted resistance to change by the industry supported by the Government could bring the Panel into conflict with the FCA. I think we learned some good lessons last time and I hope that we would be able to manage the relationship better. After all there is nothing consumers or politicians want more than a retail system which is stable, provides good service and good value.

The most likely area for conflict is a situation where we do not feel that the FCA has represented the consumer case effectively to the PRA or FPC and decide there is no alternative but to become more adversarial in public debate. That is not a decision the Panel would take lightly, but if it seemed that significant detriment was likely to arise as a result of changes in the regulation of mortgages, by for example introducing LTV or LTI caps in a way which was likely to introduce significant detriment, or failing to ensure reasonable treatment of policyholders in with profits life assurance policies I think we would have little alternative. The absence of Section 11 powers in relation to the PRA would quickly force us into a public dispute. Of course the Bank might regard this as unavoidable and acceptable. However, they were lucky in the last crisis to have avoided the scrutiny the FSA has received. I don't think that would be the case again.

I thought I would finish by setting out what the Panel would like to see a few years from now if the FCA and the proposed changes in regulation have worked:

- First a truly competitive retail banking market. The Panel would like to see more customer-focused banks encouraged to enter the market; a real debate exposing the 'free if in credit' banking myth which arguably defends a lacklustre status quo; and a regulatory push to tackle inappropriate sales and incentives practices.
- Also a respected advice market, genuinely pro-consumer and perceived as good value. The launch of the Money Advice Service and the Retail Distribution Review are a good start, but the Panel would like to see the industry exploring different advice models which provide real value for the majority of customers who are not wealthy, adopting a duty of care to its clients and ensuring customer needs come first by eliminating conflicts of interest.
- Decent, reliable products which deliver what they promise and which will help restore confidence - this is especially the case for savings, protection insurance and retirement.
- A mortgage market which lends responsibly is good value and provides the home loans consumers need; and finally,
- Better consumer protection, with fewer claims on the Ombudsman and less work for claims management firms.

Thank you.