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

Telephone: 020 7066 9346
Email: enquiries@fs-cp.org.uk

3 March 2022

By email: appointedreps@hmtreasury.gov.uk

Dear Sir / Madam,

Financial Services Consumer Panel response to HMT's call for evidence on The Appointed Representatives Regime

The Financial Services Consumer Panel (the Panel) is an independent statutory body. We represent the interests of individual and small business consumers in the development of financial services policy and regulation in the UK.

The Panel welcomes the opportunity to respond to the HM Treasury Appointed Representative Regime: Call for Evidence and the similar FCA "Improving the Appointed Representatives regime, Consultation Paper CP21/34", the FCA consultation looking in detail at monitoring, supervision, control, and transparency issues.

The Panel has long advocated for a review of the AR regime and we agree with the TSC Lessons from Greensill Capital inquiry view that, "It appears that the appointed representative's regime may be being used for purposes which are well beyond those for which it was originally designed" and the recommendation that "The FCA and HM Treasury should consider reforms to the appointed representative's regime, with a view to limiting its scope and reducing opportunities for abuse of the system".

The appointed representative's regime dates to the Financial Services Act 1986, but as the scope of FSMA has extended the significance of the appointed representative model has grown. Additionally, the nature of the model, particularly Regulatory Hosting, and the business types transacted by ARs has become far more complex and consequently, the scope for consumer harm has grown. The growth in popularity of the regime is in large part due to it being viewed by ARs, Principles, Product Manufacturers and the Panel as being light touch with reduced supervision.

A number of long-standing concerns have become more significant as the regime and range of AR activities undertaken has developed and become more complex - over and above light touch monitoring, supervision and control, these being that in the current appointed representative's regime and as noted in HM Treasury's Call for Evidence:

- despite use of the terms "principal" and "representative" there is no requirement that an appointed representative in fact represents or acts as agent of its principal.
- because the scope of the appointed representative's appointment is set out in the terms of a private contract, the appointed representative agreement, between the principal and the AR, there is no straightforward way for the FCA or a customer of the AR to know the scope of the AR's right to perform regulated activities, yet if an AR is acting outside the scope of the agreement the customer may be unprotected.
- there is no limit on the amount of business that an appointed representative can carry on in that capacity – indeed, its regulatory income could exceed that of its principal with this increasing risk of conflict and harm.

The ability of ARs to have to have more than one Principal is a key issue with the regime. This requires Principals to have multi–Principal Agreements that set out the respective responsibilities of each Principal. This complicates monitoring, supervision, control for Principals and the FCA and most importantly, exposes the consumer to harm. This is particularly relevant to the final question regarding extending the powers of the FOS to investigate complaints against ARs.

A further concern that the Panel have is the lack of AR regime expertise within the market, HM Treasury and the FCA, particularly in relation to the regulatory hosting model. Whilst the FCA and HMT may be well acquainted with the regime itself, they have little experience of Supervising AR firms, which is where the Panel's concern stems from. The regime has seemed to develop to assist incubator businesses and allowed secondment of individuals from an AR to the principal. This model enables those seconded individuals to conduct regulated activities for which the principal has permissions, but which are not permissible within the scope of section 39 alone, such as discretionary fund management and dealing in investments.

In conclusion and with the increased standards that will be required by the New Consumer Duty in mind, the Panel believe that the FCA should transition from the AR model with all firms moving to being directly regulated. A risk-based approach taken to this with priority of transitioning to direct authorisation starting with AR's providing investment, retirement planning, later life lending and tax planning advice (which is not a regulated activity but is being undertaken by some ARs). In the interim, FCA should tighten the regime, improve transparency, reporting, controls, and Principal firm accountability. Spans of control plus monitoring and supervision levels together with the ability of FOS to investigate complaints should be those that would apply if the Principal firm directly employed the AR. Additionally, capital adequacy levels should increase to reflect the increased risk of harm that a network of AR's presents.

Our responses to the questions posed in the consultation are included at Annex A below. Please note that the Panel have repeated responses in some instance as we believe they are applicable to the question and to ease response analysis.

Yours sincerely,

Wanda Goldwag

Chair, Financial Services Consumer Panel

Annex A – responses to questions

1. For users of the AR regime, whether principals or ARs: do you find the regime effective and beneficial to your business operations? Explaining your answers in the context of your business model would be helpful.

The Financial Services Consumer Panel are concerned that AR model as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control are in many cases lower than would be the case had the AR been directly employed by the Principal or product manufacturer, as a consequence consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions. The New Consumer Duty is seeking to deliver higher standards in relation to foreseeable harm through supporting retail consumers by firms acting in good faith to deliver better outcomes. The Panel is concerned that the current level of Supervision for ARs is limited and therefore questions how firms can ensure they are adhering to the New Consumer Duty.

2. Are there any other types of use of the AR regime we have not described above? In this case, please describe the business model and the types of firms (or groups, where relevant) that use the AR regime.

No.

3. For multinational firms that use the regime to access UK financial services markets – how do you access these markets in other countries?

No comment.

4. Do you think the diverse use of ARs across different sub-sectors and business models has been a beneficial evolution of the regime? Do you have any concerns with any of the ways in which the AR regime is currently used?

The Financial Services Consumer Panel are concerned that AR model as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control in many cases lower than would be the case had the AR been directly employed by the Principal or product manufacturer, as a consequence consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based

transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

5. Do you think the above discussion provides an accurate explanation of the current AR regulatory regime? Are there any other elements to the regulatory regime which are important to consider?

Yes, the Panel agree that the discussion reflects the current AR regulatory regime.

In terms of other elements of the regulatory regime that are important to consider, the Panel highlight that the Senior Managers and Certification Regime does not extend to AR's and has long standing concerns regarding the regime as it currently stands in relation to standards of AR regime oversight, supervision, spans of controls and capital adequacy. The Panel are of the opinion that unless and until our concerns are addressed, with the Principal at arm's length from the consumer, it will be difficult to deliver the increased standards and customer outcomes required by the New Consumer Duty.

6. Do you think these policy aims are the right ones for the AR regime?

Yes, however we suggest point 3.18 bullet one within the consultation should include improving consumer inclusion and outcomes. Point 3 is not strong enough and should reference proactive mitigation of risk.

The Panel also suggest a fourth point, the AR regime should not be lighter touch or lower cost regulation, control and supervision than would be the case had the AR been directly employed by the Principal or authorised firm. The Panel believe the AR regime requires urgent review and simplification with consumers better served by a risk-based transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

7. How appropriate and effective do you think the current regulatory approach is at ensuring the safe operation of IARs?

The Panel has less of an issue with IAR's and if the AR regime was phased out there would still be a role for IARs and they could continue to operate. We view clarity and transparency of the IAR role and status as essential with disclosure of renumeration and their being prohibited from influencing the consumer purchase decision.

8. How appropriate and effective do you think the current regulatory approach is at ensuring the safe operation of smaller ARs?

The Financial Services Consumer Panel are concerned that AR model as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control in many cases lower than would be the case had the AR been directly employed by the Principal or product manufacturer, as a consequence, consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based

transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

9. How appropriate and effective do you think the current regulatory approach is at ensuring the safe operation of larger, more complex ARs?

The Financial Services Consumer Panel are concerned that AR model as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control in many cases lower than would be the case had the AR been directly employed by the Principal or product manufacturer, as a consequence consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

10. How appropriate and effective do you think the current regulatory approach is at ensuring the safe operation of the regulatory host model?

The Financial Services Consumer Panel are concerned that AR model, particularly the Regulatory Hosting Model, as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control in many cases lower than would be the case had the AR been directly employed by the Principal or product manufacturer, as a consequence consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

A further concern that the Panel have is the lack of AR regime expertise in the market HM Treasury and FCA, particularly in relation to the regulatory hosting model, this developed to assist incubator businesses and allowing secondment of individuals from an AR to the principal. This model enables those seconded individuals to conduct regulated activities for which the principal has permissions, but which are not permissible within the scope of section 39 alone, such as discretionary fund management and dealing in investments. In addition to our previous comment, the significant growth of the Regulatory Hosting recent years is a further concern and reason why the Panel are of the firm view that AR firms using this model should be transferred to directly authorised status at the earliest opportunity.

11. Do you think the above discussion is an accurate reflection of the challenges to effective operation of the current AR regime? Are there other challenges to fair and effective operation of the regime which have not been identified here? Do you think these challenges are manageable under the current approach? Do you think the range of regulated activities an AR may carry on is appropriate?

Yes, we agree that the discussion is an accurate and fair reflection of the challenges to the effective operation of the current AR regime. This said, the Panel are concerned that the AR model, particularly the Regulatory Hosting Model, as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control in many cases is lower than it would be the case had the AR been directly employed by the Principal or product manufacturer. As a consequence, consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

The FCA and HM Treasury lack of understanding of the Regulatory Hosting Model together with its significant growth in recent years a particular concern and reason why the Panel are of the view that AR firms using this model should be transferred to directly authorised status at the earliest opportunity.

12. Do you think changes to the scope of the section 39 exemption for ARs should be considered? If so, what changes do you think should be made? How might changes to scope affect ARs, principals and their consumers?

The Financial Services Consumer Panel are concerned that AR model, particularly the Regulatory Hosting Model, as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control in many cases lower than would be the case had the AR been directly employed by the Principal or product manufacturer, as a consequence consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

13. Section 4 - What are your views on the FCA having greater ability to prevent poor oversight of ARs through the introduction of a 'principal permission'? Do you have views on other ways of enhancing the FCA's role in the regulation of

principals and their ARs? What do you think would be the benefits and risks of enhancing the FCA's powers to regulate principals or ARs?

The Financial Services Consumer Panel would welcome the FCA having far greater ability to prevent poor oversight of AR's by means of a 'principal permission'. The Panel are concerned that AR model, particularly the Regulatory Hosting Model, as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control in many cases lower than would be the case had the AR been directly employed by the Principal or product manufacturer, as a consequence consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

14. What do you think would be the benefits and risks of applying more regulatory requirements directly to ARs? Are there particular requirements that you think should be applied directly to ARs?

The Financial Services Consumer Panel are concerned that AR model, particularly the Regulatory Hosting Model, as we see it today has evolved far beyond what was originally intended and is perceived as light touch, low burden, cost, and distribution risk regulation by insurers, mortgage lenders, investment houses, Principals and ARs. The levels of Principal and AR monitoring, supervision plus spans of control in many cases lower than would be the case had the AR been directly employed by the Principal or product manufacturer, as a consequence consumers are exposed to risk of harm and we urge HM Treasury to consider the impact of the regime on all stakeholders, not simply Principals and ARs.

We believe that irrespective of the size of the AR firm, monitoring, supervision, and the frequency of checks should be the same. We additionally believe that, especially given the increased standards that will be required by the New Consumer Duty, the AR regime requires urgent review and simplification with consumers better served by risk-based transition to all firms being directly regulated by the FCA - particularly those ARs distributing pension, investment, savings, retirement and tax planning and lifetime mortgage solutions.

15. Do you think there is a case for extending the ability of the Financial Ombudsman Service to investigate complaints involving the activity of ARs? What do you think the benefits and risks of this approach might be? Would this change affect how ARs are used by their principals?

The Panel believe that the very reason that this question is being asked, and the fact that the FOS cannot intervene, illustrates why the AR regime in all its variants should be subject to an orderly and risk-based wind down with AR firms transitioning to be directly authorised and adequately capitalised.

We agree with HM Treasury that there is a strong arguments for this proposed change, this said, the Panel feel greater clarity is required as it:

- It does not take into account the FCA's proposal that the financial services register should show the regulated activities that an appointed representative has authority to carry on – both in the sense that the scope of that authority would then be something that consumers could inform themselves about, and also because if the principal was in fact responsible for a wider range of regulated activities than was shown on the register, that would mean the register was misleading by showing a shorter list of activities against the name of the appointed representative.
- Presumably the liability of the principal in respect of its appointed representatives would still be limited by the permissions of the principal itself – in which case consumers would still be exposed if the appointed representative acted outside that scope.
- It is not clear whether this change is intended to affect only complaints made to the FOS, but any change to section 39 would surely affect the principal's liability as a matter of law more generally. The FOS has to take account of the law in its decision making, so if as matter of law the principal had no liability for the acts or omissions of its AR, that would significantly curtail the ability of the FOS to find against the principal.
- It is also unclear how this change would work where an AR has more than one principal; currently in such cases the principals are required to enter into a multiple principal agreement which sets out the respective responsibilities of each principal. It is also unclear how it would apply in the context of introducer appointed representatives, whose appointment by definition has a more limited scope.