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

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Financial Conduct Authority
12 Endeavour Square
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By online submission

14 December 2018

Dear Sir/Madam

Financial Services Consumer Panel (The Panel) response to the Treasury Committee Inquiry on Consumers' Access to Financial Services

1. The Financial Conduct Authority (FCA) is required to set up and maintain a panel to represent the consumer interest in financial services. The Panel represents the interests of all financial services consumers and operates independently of the FCA.

2. The Panel welcomes the opportunity to respond to this inquiry.

3. **Summary of Main Points**

4. The European Commission definition of a vulnerable consumer is more complete than the FCA's. In particular, it recognises that the way the market operates may, in itself, cause vulnerability.

   There should be a new duty of care on financial services firms. Some types of firms e.g. financial advisers, are already required to act in their clients' best interests, which is stronger and clearer than the FCA's 'Treating Customers Fairly (TCF)' Principle for Businesses.[1] The FCA should, as a minimum, amend its Principles for Businesses, to require all firms to act in customers' best interests and manage conflicts of interest fairly and so as to avoid consumer harm. This should be backed with a right for an individual to take court action against a breach. However, the best outcome for consumers would be to enshrine a duty of care in the Financial Services and Markets Act (FSMA).

5. The gulf between literacy and numeracy levels in the population and firms' communications with their customers, is an example of how a duty of care could help everyone, including many vulnerable groups, by forcing firms to take account of the needs of their customers.

6. Access issues evolve over time. People who have previously been financially included can find they become marginalised or excluded, because their personal circumstances change, because of a change in the way firms operate (e.g. insurance

[1] Acting in the client's best interests Conduct of Business Rules COB 2.1.1

or credit underwriting) or because of wider trends, such as the digitalisation of financial services.

7. Demutualisation of risk is a growing issue, contributing to exclusion in insurance and credit. It requires public policy intervention to support inclusion and create markets the FCA can regulate effectively. Flood Re proved such interventions can work and we welcome moves to explore a no-interest loan scheme.

8. The FCA often raises concerns about prices, but seldom intervenes on price directly. Price interventions have generally been successful, and this should overcome concerns about the proportionality of such measures.

Yours faithfully

Sue Lewis

Chair, Financial Services Consumer Panel

Comments on specific points in the Inquiry's Terms of Reference

9. ***1a. How should financial service providers define 'vulnerability'?***

   The FCA's definition[2] is a good starting point, but focusing on personal circumstances creates practical issues:

   - It encourages firms to identify customers who exhibit specific characteristics or circumstances. In practice, consumers do not or cannot always disclose difficult issues[3] and identification is unreliable when so many vulnerability factors are invisible, transient, episodic or present in complex combinations. Some vulnerable people risk missing out on additional support that might be available.

   - It risks distracting firms from treating all their customers fairly and avoiding the harm that can arise when their products, information and conduct cause or increase vulnerability.

   The FCA acknowledges both these risks.[4] Firms are improving the way they serve people with particular conditions and circumstances. This merely scratches the surface of all vulnerable circumstances, and leads to vulnerability being a tick-box "compliance" issue rather than one of embedded strategy and culture in the industry. Products and services that work well for vulnerable people will work well for everybody.

   A better starting point would be the European Commission definition of vulnerable consumer[5], which explicitly acknowledges the market environment – and in particular firm behaviour - as a source of vulnerability, alongside personal characteristics and

[2] A vulnerable consumer is 'someone who, due to their personal circumstances, is especially susceptible to detriment, particularly when a firm is not acting with appropriate levels of care.'

[3] '*People often do not disclose mental health problems to advisors as they will not be treated sensitively, or that it will not make any difference to their situation*.' https://www.moneyandmentalhealth.org/wp-content/uploads/2018/11/Vulnerability-the-experience-of-debt-advisers.pdf

[4] Occasional Paper 8, 2015.

[5] https://ec.europa.eu/info/publications/understanding-consumer-vulnerability-eus-key-markets_en

situations. This is a better way of identifying and addressing vulnerability to harm while at the same time preventing firms focusing on some groups of consumers to the detriment of others who are not badged as 'vulnerable'. It is another way of saying that firms should treat *all* customers fairly, as we explained in our response to the FCA's Approach to Consumers document,[6] as well as in the Panel's response to the Department for Business Energy & Industrial Strategy (BEIS) Consumer Green Paper.[7]

10. As well as looking to the impact of their behaviour on customers, firms should take account of the particular needs of consumers who need additional protection. Vulnerable consumers should be helped and protected but should also be able to participate in the same market as everyone else.[8]

11. ***1c. A 'duty of care' for financial services providers***

The Panel has long argued for a duty of care in financial services as the TCF principle does not go far enough to eliminate conflicts of interest and deter firms from mis-selling products and providing poor service.[9]

12. Our position paper identifies many instances where TCF and other FCA Principles for Businesses have failed to protect consumers adequately.[10]

13. The Panel's proposed new duty is, as set out in its response to the FCA's Discussion Paper,[11] that *firms should act in the best interests of all their customers and manage conflicts of interest fairly and so as to avoid customer harm*.

14. The Panel believes a new duty of care would achieve the following benefits:

- **Better treatment of financial services customers** - there is ample evidence of firms not complying with the Principles for Businesses, while not technically breaching any detailed FCA rules (see Annex A). It is rare for the FCA to enforce against the principles unless rules have also been broken. A new duty should give the FCA more confidence to enforce against a breach of the principles, ensuring that firms took them more seriously. A new duty would improve the position of *all* consumers of financial services, including those who need more support due their vulnerable characteristics or circumstances;
- **Better balance between firm and customer responsibilities** – financial products are complex and the long, impenetrable terms and conditions are non-negotiable. This creates asymmetries of knowledge, understanding and bargaining power between firms and their customers. A new duty would help establish a fair balance of firm and customer responsibilities;
- **Focus on prevention** – a new duty would encourage firms to identify potential customer harm and avoid it, adopting a '*prevention is better than cure' approach*.
- **Change in firm culture** – a new duty would give firms a sharper incentive to improve their organisational culture.

15. The FCA Handbook already contains high-level rules which require firms to act in accordance with the best interests of their customers. These rules apply to certain

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[6] Pages 2-3,https://www.fs-cp.org.uk/sites/default/files/fscp_response_approach_to_consumers.pdf

[7] https://www.fs-cp.org.uk/sites/default/files/fscp_response_modernising_consumer_markets_-_consumer_green_paper.pdf

[8] https://www.fca.org.uk/publication/corporate/approach-to-consumers.pdf

[9] https://www.fs-cp.org.uk/sites/default/files/duty_of_care_briefing_-_jan_2017_2.pdf

[10] See Annex, https://www.fs-cp.org.uk/sites/default/files/duty_of_care_briefing_-_jan_2017_2.pdf

[11] https://www.fs-cp.org.uk/sites/default/files/fscp_response_duty_of_care_dp.docx_.pdf

investment business, mortgage activities and insurance distribution. There is no reason why 'best interests' should not apply across financial services.

16. While we have proposed to the FCA ways to strengthen the Principles for Businesses using its existing powers, we believe the best way of achieving the aims set out above is through legislation explicitly placing the requisite duty on firms. We urge the Committee to follow the FCA's work in this area, and consider a recommendation to the Government that it should bring forward an amendment to FSMA.

17. ***2c. The effectiveness of procedures deployed by financial services providers to ensure that customers, including those with low literacy levels, properly understand the products that they are purchasing.***

18. Consumers can't make informed decisions about financial products and services if charges or fees are unclear[12] or disclosed inadequately or if literature is misleading and confusing.

19. In occasional paper 32,[13] the FCA suggested that the way in which the information is presented can affect how consumers access, assess or act on it. The FCA said firms should take this into account when considering the individual needs of vulnerable consumers, especially those with low literacy levels as they will be excluded from certain products or misled by poorly worded literature. Firms are meant to comply with the principle that communications should be 'fair, clear and not misleading.' Yet standards in the market remain poor. This is another area where a duty of care could be effective. 15% of the UK population is functionally illiterate, so is particularly vulnerable to misunderstanding terms and conditions that often require tertiary level education to understand.[14] Identifying the 15% is an impossible task. Firms should instead design communications that can at least be understood by someone of average reading ability (which is that expected of a 9-year-old), and also recognise that 1 in 20 adults in the UK have a reading age of 5 or less.

20. This would benefit all consumers, as well as being inclusive to those who are vulnerable. It would help combat some of the issues flagged by our research into data and consent:[15]
    - even when people read terms and conditions, they are usually none the wiser. They rely on reviews, or a vague feeling that government and regulators are looking after their interests
    - people value privacy, but not as much as speed, when they want goods or services
    - research published by Visible Thread[16] showed the need for asset management firms to improve the clarity of fund disclosures on their webpages.

21. ***2i. Evaluate how fintech and technological innovation could help those who cannot easily access physical financial services branches.***

[12] https://www.fca.org.uk/publication/consultation/cp18-13.pdf
[13] https://www.fca.org.uk/publication/occasional-papers/occasional-paper-32.pdf
[14] https://literacytrust.org.uk/parents-and-families/adult-literacy/
[15] https://www.fs-cp.org.uk/sites/default/files/final_position_paper_-_consenting_adults_-_20180419_0.pdf
[16] *98% of the 69 asset management firms tested failed to meet "basic standards of readability.*
https://www.visiblethread.com/company/published-reports/

22. In the new digital age, digital capability is likely to be as important as financial capability. [17] Both Lloyds and Barclays are developing new indices to measure digital capability and financial capability.

23. The implementation of Open Banking has widened access to financial services but disadvantages to those who are digitally excluded, who are often, the elderly.

    Whilst Fintech has a part to play in increasing choice, competition and convenience for consumers, especially those who cannot access physical branches, this must be coupled with adaptations and support for those consumers who are left with no choice but to use online services that are not designed around their needs.

24. It should also be borne in mind that technology imposes significant costs on consumers. In particular, apps will often only work with the latest hardware, so consumers may have to upgrade their phone or tablet every 2-3 years. This will be unaffordable for many.

25. Banks can sometimes ask customers about their communication needs (often with a limited range of options such as braille) but rarely ask about their communication preferences. If a wider range of options was available to all customers (including email), this would enable vulnerable customers to choose their preferred communications channel without stigma.

26. Those with mental health difficulties have specific communication needs ranging from the need to see a financial professional face-to-face, to not being able to speak to someone in person at all. [18] With the increase of bank branch closures, clearly some of the most vulnerable will struggle to access financial services independently.

27. The closure of branches has meant that banks are more likely to contact customers by telephone. However, not all consumers are willing to be contacted by people calling from unfamiliar numbers, and many are wary of unsolicited calls due to anti-scam campaigns warning against fake callers purporting to be from banks. While consumers are expected to go through lengthy security questions before they can discuss their bank account, there is no requirement on banks to prove their identity to customers they telephone.

28. Moreover, bank staff will not know if the customer struggles to hear, and cannot be certain that the customer has understood the conversation fully. Consumers who ask for copies of recordings of telephone conversations often find banks unhelpful. It would be better for all consumers to be asked for their preferences as regards telephone contact.

29. Fintech and technological innovation may be the way forward for those forced to use online services as a result of branch closure, but it should be designed in a way to ensure that those who are vulnerable can give genuinely informed consent to their data being shared.[19] Consumers who do not wish to share their data should not be discriminated against.[20]

30. ***3. Do vulnerable consumers pay prohibitively more for certain financial services products, including travel and home insurance.***

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[17] https://www.fs-cp.org.uk/sites/default/files/fscp_response_house_of_lords_select_committee_on_financial_exclusion_1.pdf

[18] http://www.moneyandmentalhealth.org/wp-content/uploads/2017/02/Seeing-through-the-fog-Final-report-1.pdf

[19] https://www.openbanking.org.uk/wp-content/uploads/Open-Banking-A-Consumer-Perspective.pdf

[20] For more on these issues, see the Panel's response to the Government's Consumer Green Paper [link]

It is clear from Citizens Advice's '*loyalty penalty*' super-complaint to the CMA, the FCA's announcement of a market study into pricing practices in motor and home insurance, and the FCA's Call for Input on Access to Insurance,[21] that consumers are not being treated fairly, with vulnerable consumers often being hardest hit.

31. Travel insurance

32. The FCA's research[22] concludes that consumers whose circumstances or pre-existing medical conditions fall outside the parameters of automated algorithms are often not able to find insurance at all. At best, they are offered cover at an inflated price with incomprehensible conditions and exclusions. Many consumers are disappointed when they try to claim. Price comparison websites do not help 'non-standard' consumers because firms promote policies on headline price. Suitable policies for non-standard risks may not feature at all. Important features such as exclusions and excess fees are hard to find. Moreover, price comparison websites rarely display information about exclusions based on age or medical conditions until a consumer has filled in all their information and been refused cover.

33. Firms' risk pricing is opaque. There is no independent verification of whether firms use relevant statistics to assess risk. Risk models must be transparent to determine whether consumers are being treated fairly, whether price optimisation models are fair; and whether firms are complying with the Equalities Act 2010.

34. The basis on which firms price risk should be clear to consumers and the Panel welcomes the FCA's continued investigations in this area.

35. The increasing use of individualised risk pricing excludes vulnerable consumers and limits access to vital financial services for many others. This is a public policy issue. It hinders the FCA's achievement of its objectives, but the FCA cannot act alone. Industry cannot easily move away from individualised risk pricing without regulatory and governmental intervention and support. The Government recognised the need for an innovative solution for flood insurance by setting up Flood Re.

36. There are other products for which a degree of mutualisation may be socially desirable in order to enable affordable access to essential financial services.

37. Age

38. Age is a factor in financial exclusion from certain products and services. Older people are less likely to be digitally included[23], although that is changing rapidly, and they prefer accessing services face to face. This means they can struggle in a world where online services are becoming the norm, and banks are withdrawing their high street presence. Older people are likely to find themselves victims of age discrimination.[24]

39. This is not permitted in most service industries, but financial services are exempt. Firms can use age as a risk factor in pricing financial products, or even refuse to provide products to certain age groups. At the other end of the spectrum, young drivers may be unable to get affordable car insurance, for example, which seems unfair if their individual risk profile is much lower than the average for their group.

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[21] https://www.fca.org.uk/publications/feedback-statements/call-input-access-insurance

[22] https://www.fca.org.uk/publication/occasional-papers/occasional-paper-17.pdf
https://www.fs-cp.org.uk/sites/default/files/fscp_response_-_big_data_call_for_input.pdf

[23] An Age UK Digital Inclusion Policy Review document states only 29% of adults aged 75 years and over have used the internet: http://www.ageuk.org.uk/PageFiles/12810/Digital%20Inclusion%20Review.pdf?dtrk=true

[24] https://www.fs-cp.org.uk/sites/default/files/fscp_laterlife0609.pdf

40. Paying for insurance monthly is often costlier than paying for it annually. This may indicate that those who cannot afford to pay the annual cost of a policy upfront, and may be vulnerable, are being penalised by paying more for the same policy each month.

*41. **3c. Consider whether vulnerable consumers have access to appropriate and affordable credit.***

42. Consumer credit

43. The FCA's research into consumer credit and consumers in vulnerable circumstances.[25] showed that consumers who are struggling financially or on lower incomes pay more for financial products.

44. Firms' exploitation of vulnerable consumers' circumstances and behavioural biases in the credit market mean two thirds of low income credit users face additional costs compared to other consumers. [26]The prices paid by low income and vulnerable consumers for consumer credit partly reflect an increased risk of default, but partly represent overcharging consumers who have limited choice.

45. While some low-income consumers are unable to access the credit products they need (and could afford to repay). The borrowing options available to low-income borrowers often come at a high cost and on terms that pitch them into poverty, debt and social exclusion. Recent research shows that, among low-income high-cost credit users, the estimated interest costs ranged from £120 per year for small-sum, short-term payday loans to £540 for larger-sum, longer-term home-collected loans.[27]

46. Overdrafts

47. Consumers living in more deprived areas are more likely to use an unarranged overdraft than those in less deprived areas and pay around twice as much in fees and charges. Overdrafts are a common form of credit for those on low incomes.[28] Excessive charges, a lack of control, and a lack of transparency about how charges are levied is likely to affect vulnerable consumers particularly.[29] The majority of unarranged overdraft fees are paid for by 1.5% of customers, despite 14% of current account customers paying these charges in total.[30]

48. Repeat use of unarranged overdrafts in conjunction with long-term use of arranged overdrafts is a particular problem.

    Following recent increases in the costs of arranged overdrafts, repeat and long-term use of arranged overdrafts could also be seen as creating more harm for vulnerable consumers struggling financially.

[25] https://www.fca.org.uk/publication/research/consumer-credit-customers-vulnerable-circumstances.pdf
[26] Ibid
[27] www.bristol.ac.uk/media-library/sites/geography/pfrc/pfrc1710_making-the-poverty-premium-history.pdf
[28] https://www.fca.org.uk/publication/research/consumer-credit-customers-vulnerable-circumstances.pdf, pg25
[29] Ibid, pg 28
[30] https://www.fca.org.uk/publication/consultation/cp18-13.pdf

49. Remedies which give consumers more information and text messages are likely to not work to reduce the detriment for vulnerable consumers. Research conducted by the FCA[31] and others has found that:

- the transparency remedies proposed by the FCA will make little difference for persistent users of overdrafts or vulnerable consumers lacking access to mobile banking or savings.

- a large number of heavy users of unarranged overdrafts and unpaid items are not helped by automatic enrolment into alerts.

50. Mortgages

51. We note in our response to the CMA's loyalty penalty super-complaint[32] that it is usually the elderly and those on lower incomes who do not switch mortgage provider and end up paying higher prices. Some are unable to switch to a better deal with their existing lender because they have taken a repayment holiday due to ill health or a temporary drop in income. Those in arrears for other reasons, or whose income does not meet current lending criteria, are unable to move to other lenders.

52. This is particularly problematic for those whose loans have been sold to a firm that is outside the FCA's regulatory perimeter. These customers are paying higher rates than those with a wider range of options.

53. As noted above, consumers on low incomes and struggling financially, often turn to high cost credit because it is quick and easy to access,[33] although it is not the most suitable form of credit to them, worsening the debt cycle. This is the same for some experiencing periods of mental ill-health.[34] Charges for overdrafts are concentrated meaning it is likely that vulnerable consumers pay for the majority of fees.[35]

54. The FCA's research showed that those on the lowest incomes found online credit inflexible and impersonal, again restricting access for the most vulnerable.[36]

3e. Evaluate how regulators assess whether financial services providers are providing products to consumers at a fair price.

55. The Panel supports the work of the FCA in this area and will respond to its Discussion Paper on fair pricing practices and the GI market study terms of reference.[37] Fair pricing has been an issue for too long – reflected by the complaints about insurance received by the Financial Ombudsman Service.[38]

56. The FCA rarely intervenes directly on price, favouring demand-side measures such as encouraging consumers to switch products.

[31] https://www.fca.org.uk/publication/occasional-papers/occasional-paper-36.pdf
[32] https://www.fs-cp.org.uk/sites/default/files/fscp_response_to_cma_loyalty_penalty.pdf
[33] https://www.fca.org.uk/publication/research/consumer-credit-customers-vulnerable-circumstances.pdf
[34] http://www.moneyandmentalhealth.org/wp-content/uploads/2017/02/Seeing-through-the-fog-Final-report-1.pdf
[35] https://www.fca.org.uk/publication/consultation/cp18-13.pdf
[36] https://www.fca.org.uk/publication/research/consumer-credit-customers-vulnerable-circumstances.pdf
[37] https://www.fs-cp.org.uk/sites/default/files/fscp_response_to_gi_market_study_terms_of_reference_20181208_v2.pdf
[38] https://www.financial-ombudsman.org.uk/publications/ombudsman-news/144/144.html

57. It seems the FCA is concerned about proportionality and cost benefit analysis. Despite the acknowledgement in its Mission[39], that prices that are too high can cause consumer harm, the FCA seems to only assess the impact of prices when the Government tells it to, notably for payday loans. Price interventions can be effective. Some examples are below:

    1. the payday loan price cap;[40]
    2. cap on the charges within default pension funds – since 6 April 2015, under DWP regulations and FCA rules, providers have to cap the charges within default funds in qualifying workplace pension schemes, to 0.75% per year of funds under management;
    3. stakeholder pension schemes – in stakeholder pension schemes annual management charges are capped at 1.5% per year for the first ten years of scheme membership and then not more than 1% thereafter; and
    4. the CAT standard mortgage which limited SVRs to no more than 2% above base rate and stopped thousands of vulnerable and trapped consumers paying excessive interest rates.

58. As a conduct regulator, if the conduct of businesses using certain pricing/risk models harms consumers, then the FCA should intervene. Equally, the Government must step in where it can to support or supplement the FCA's actions from a policy perspective, to ensure consumers are not continuously losing out.

[39] https://www.fca.org.uk/publication/corporate/our-mission-2017.pdf
[40] https://www.fca.org.uk/publications/policy-statements/ps14-16-detailed-rules-price-cap-high-cost-short-term-credit