

## **Response to HM Treasury consultation on: A new approach to financial regulation: the blueprint for reform**

### **Introduction**

The Consumer Credit Counselling Service (CCCS) is the UK's largest dedicated provider of independent debt advice. Last year the charity helped 418,000 people with free advice and delivery of support services, including Debt Management Plans (DMPs), bankruptcy and welfare benefit checks – we are geared up to help many more. We welcome this opportunity to comment on HM Treasury's White Paper on financial regulation and draft Bill.

CCCS is run independently of taxpayer money on the basis of a unique set of relationships with all the major banks, credit card companies and other creditors – our funding model means we can provide impartial advice and specialist insolvency support as people need.

CCCS is committed to improving the situation of households in financial distress. By the end of 2010, our over 800 full time staff were managing almost £3.6 billion of unsecured debt.

CCCS experienced a 35 percent increase in demand for its services as a result of the recession, helping almost half a million people in 2009 alone. This would doubtless have been of interest to the FPC had it been around.

Given the nature of the problems our clients face, the key concerns of CCCS centre on the issue of consumer detriment. In general, this can come about in two ways:

- from conduct problems – for example, when products are badly designed or missold
- from macro-economic/prudential factors, such as interest rate variations or general economic tightening, which can impair consumers' access to needed credit or ability to service existing debts.

### **Therefore, our main points are:**

- The FCA should be established as the equal of the PRA and not its junior partner so that consumers have the confidence that they will be treated fairly. Consumer protection should be a strategic objective for the FCA or at least its highest operational priority (as we suggest in our response to Q6)
- There should be consumer representation on the FPC (Q1)
- People with a background in consumer advocacy should be members of the FCA's governing body (Q12)

- The Government should either retain a consumer panel for the PRA or ensure it sets out a wider strategy for engagement with consumer representatives (Q5)
- The PRA should at the very least be required to publicly explain why it has resorted to using its veto power, as its use implies regulatory failure (Q13).

Specifically, CCCS will be directly affected by any decision to transfer responsibility for the regulation of consumer credit from the Office of Fair Trading (OFT) to the FCA. Though this proposal is currently under review, the FCA needs to be geared to hit the ground running in this area, not least because of the risks of serious and long-term consumer detriment. Therefore we strongly urge the government to establish the FCA as a shadow regulator from the outset in anticipation of any such transfer.

Our response to the following consultation questions is based on the interests of our clients – both current and potential – and their relevance to our work. A recent report for the charity by the Financial Inclusion Centre (using CCCS data and other sources) found that 3.2 million households are in persistent arrears (or subject to insolvency action), with a further 3 million at risk of falling behind with repayments<sup>1</sup>, underlining the importance of an improved regulatory regime.

### **1. Do you have any specific views on the proposals for the FPC as described in paragraphs 2.6 to 2.24 and in Chapters 3 and 4?**

We believe the FPC should have regard to the interests of consumers in its decision-making. Decisions taken by the FPC, in particular, could have far-reaching consequences for the financial sector and the economy more widely. They may also have far-reaching consequences for consumers of financial services. It will therefore be important for the FPC to take the impact on consumers into consideration when pursuing its primary objective.

However, we fear there may be pressures to put prudential concerns ahead of consumer concerns. Further, we share the view of the Treasury Select Committee that membership of the FPC may be too narrow, in particular in its heavy weighting toward the Bank and financial service industry representatives. As the Committee have pointed out:

“[There should be a] diverse range of experience and views [to] contribute to the development of macro-prudential policy.”<sup>2</sup>

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<sup>1</sup> CCCS-commissioned report, *Debt and Household Incomes*, 12 July 2011  
[http://www.cccs.co.uk/Portals/0/Documents/media/reports/additionalreports/Report\\_Debt\\_and\\_household\\_incomes.pdf](http://www.cccs.co.uk/Portals/0/Documents/media/reports/additionalreports/Report_Debt_and_household_incomes.pdf)

<sup>2</sup> Treasury Select Committee, *Appointments of Michael Cohrs and Alastair Clark to the interim Financial Policy Committee, Fourteenth Report of Session 2010-12*, 8 June 2011.  
<http://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/news/interim-fpc-appointments/>

For both these reasons, we believe there needs to be consumer representation among the non-Bank members of the Committee to boost confidence that the new regime is not tilted in one direction over another.

In addition, we support proposals for the FPC to report on the effectiveness of its actions, but would like to see this extended to include assessment of their impact on consumers.

As part of its focus on unsustainable levels of debt, we hope the FPC will take into account data already available through existing channels, such as that provided by CCCS. A recent report by the Financial Inclusion Centre, commissioned by CCCS, urges the government and regulatory authorities to develop better intelligence on household borrowing, including more detailed information about financially vulnerable consumers. This would allow policymakers to better understand the implications of macro-level decisions, allow finite resources to be targeted more efficiently and help better secure consumer protection<sup>3</sup>. While the report's recommendations are its own, we believe better intelligence will be an essential component of an improved regime.

**2. Do you have any specific views on the proposals for the Bank of England's regulation of RCHs, settlement and payment systems as described in paragraphs 2.32 to 2.40 and in Chapters 3 and 4?**

**3. Do you have any comments on:**

- **the proposed crisis management arrangements; and**
- **the proposals for minor and technical changes to the Special Resolution Regime as described in paragraphs 2.41 to 2.44 and in Chapters 3 and 4?**

**4. Do you have any comments on the objectives and scope of the PRA, as described in paragraphs 2.46 to 2.61 and in Chapters 3 and 4?**

While we agree that the PRA's strategic objective to contribute to the stability of the financial system is an important goal, we are concerned that practices that cause harm to consumers will not be properly addressed when they are so widespread or entrenched that the costs of correcting behaviour are deemed too risky for overall stability.

Enabling the PRA to overrule the body charged with consumer protection risks sending a message to firms that they will not be forced to bear the full consequences of mistreating consumers.

At the very least (cf Q13), we believe the PRA should be required to publicly explain why it has resorted to using its veto power, as its use implies regulatory failure on the part of the FCA, the PRA or both regulators to achieve their objectives.

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<sup>3</sup> *Debt and Household Incomes*, p46-7

**5. Do you have any comments on the detailed arrangements for the PRA described in paragraphs 2.62 to 2.78 and in Chapters 3 and 4?**

We are concerned that plans to scrap the consumer panel for the PRA will put further distance between consumers and the decision-making process. While the PRA is required to consult the FCA in its decision-making, the FCA itself – unlike the Panel – is not set up to represent consumer concerns.

In any event, the weaker duty for the PRA to consult the conduct regulator – rather than having regard to its objectives – risks it being sidelined. Without a proper balance between prudential and consumer concerns, ordinary consumers of retail products may continue to lack the degree of regulatory focus or protection they expect or require. In coming to decisions and analysing their impact, the PRA should not neglect consumer outcomes.

To ensure that consumer issues are at the heart of the new regime, the Government should either retain a consumer panel for the PRA or ensure it sets out a wider strategy for engagement with consumer representatives. The latter might see the PRA set up regular working groups that assess the impact of its decisions with consumer bodies and charities that have an interest in financial matters.

**6. Do you have any views on the FCA's objectives – including its competition remit – as set out in paragraphs 2.80 to 2.90 and in Chapters 3 and 4?**

We welcome the intention to make consumer outcomes a central focus of the FCA.

We assume that the FCA's strategic goal – to protect and enhance confidence in the financial system – ultimately implies that the "confidence" which matters is the confidence of *consumers* that they will be well served by the financial system. This could be more clearly spelt out.

CCCS is concerned that simply restating one of the FSA's current statutory objectives will not be enough when it comes to consumer protection. While we welcome the FCA's new powers (see Q7), the massive detriment suffered by consumers under the previous regime – not least through the misselling of PPI – means that the new conduct regulator will have to operate with a clearer vision of what securing its consumer protection objective looks like.

Further, it is unclear whether consumer protection will be given priority when it conflicts with other operational objectives. We therefore urge the Government to make consumer protection part of the FCA's strategic objective or at the very least its highest operational priority.

**7. Do you have any views on the proactive regulatory approach of the FCA, detailed in paragraphs 2.91 to 2.110 and in Chapters 3 and 4?**

CCCS is hopeful that the new powers being given to the FCA will help protect consumers from the dangers of over-complex products and sophisticated sales techniques. It is encouraging to see that the FCA will not be mandated to promote competition when this is incompatible with its strategic or operational objectives.

CCCS will be directly affected by the potential transfer of all consumer credit regulation to the FCA – the charity takes action on behalf of its clients to help them manage their consumer credit commitments and holds its own consumer credit licence. We strongly support proposals that would bring together the regulation of mortgage and non-mortgage credit products under one authority.

In our experience, there is risk of more significant detriment in consumer credit than in any other area of retail financial services. As the OFT point out:

“The choices that consumers make to tackle their debt problems can have serious consequences both in terms of immediate financial cost, and long-term knock-on consequences on availability and cost of future credit.”<sup>4</sup>

The OFT’s recent probe into debt management companies underlines the need for effective regulation in this area. We believe, therefore, that the FCA should be set up as a consumer credit regulator in shadow form from the outset. A report by the Financial Inclusion Centre, commissioned by CCCS, outlines a plan of action that could be taken in this regard<sup>5</sup>. While we have reservations about some of the report’s recommendations, it demonstrates the scope of action that the regulator will need to embark on.

In addition, we note the Government “retains an open mind” (2.86) as to how the FCA will secure its operational objectives in relation to its competition remit, especially with regards to consumer protection. The FSA has recognised that success in securing effective competition in some retail markets will only occur if the FCA tackles the underlying characteristics of the market to promote “informed choice”.<sup>6</sup>

However, rather than an informed choice, the consumer of debt management services is typically making a “distress purchase”. The Money Advice Trust has produced research showing that people who are over-indebted, vulnerable and desperate for help tend to make quick decisions about complex and often unfamiliar debt solutions and tend not to shop around<sup>7</sup>. Consequently, consumers are more likely to purchase the services of the first company they come across, regardless of its ability to provide appropriate advice. Any competitive pressures are thus substantially diluted.

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<sup>4</sup> OFT, *Debt Management Guidance Compliance Review*, September 2010

<sup>5</sup> *Debt and Household Incomes* pp43-7

<sup>6</sup> FSA, *The Financial Conduct Authority: Approach to Regulation*, June 2011

<sup>7</sup> MAT, *An independent review of the fee-charging debt management industry*, June 2009

Given these circumstances, a consumer of debt management services would be in a much better position to make an “informed choice” if:

- Debt management companies were compelled to state the availability of free services in their advertising;
- Firms were required to point to clear guidelines about exactly what options are available to debtors, ensuring consumers are not just informed about the most profitable debt solutions.

These are proposals that CCCS will also be submitting to the FCA as it consults on its regulatory approach.

**8. What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?**

We strongly support the proposal to give designated groups a statutory role in the evidence-gathering process so that the FCA is obliged to respond and investigate if it determines that there is an issue causing mass detriment.

Debt advice agencies like CCCS are well-placed to submit evidence with a view to early intervention when clients are suffering due to bad practices.

Many people counselled by CCCS have been poorly served by the financial services industry, whether in terms of the appropriateness of products they have been sold, their level of indebtedness, or the so called solutions they have been offered to mitigate or manage their debt problems.

Our main concern would be to ensure that bodies applying to become designated groups should meet rigorous criteria, similar to that for groups wishing to become super-complainants. This would guard against a “free-for-all” and reduce the likelihood of vexatious complaints, in turn increasing the legitimacy of the process and reducing the risk of costs being passed on to the consumer.

**9. What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?**

We support these proposals and believe they have the potential to improve the regulatory culture to bring swifter and more effective redress for consumers.

However, it should be pointed out that regulatory transparency will have more impact on the conduct of firms when there is a truly competitive market, which is not the case in many areas of financial services.

**10. Do you have any comments on the competition proposals for the FCA set out in paragraphs 2.111 to 2.119 and in Chapters 3 and 4?**

**11. Do you have any views on the proposals for markets regulation by the FCA, described in paragraphs 2.120 to 2.123 and in Chapters 3 and 4?**

**12. Do you have any comments on the governance, accountability and transparency arrangements proposed for the FCA, as described in paragraphs 2.124 to 2.132 and in Chapters 3 and 4?**

We welcome the fact that the FCA board will have a majority of non-executive members, but would prefer to see positions of governance at the FCA filled through a process of open competition rather than Treasury/BIS appointment.

As with the FSA, it is essential that people with a background in consumer advocacy are members of the FCA's governing body – this will boost confidence in the authority's consumer protection agenda.

The FCA should be as outward-facing as possible. The statutory Consumer Panel should be adequately resourced and mechanisms should be put in place to ensure its research, findings and advice are given due consideration by the FCA board and senior executive.

Further, the focus and composition of the Panel will need re-assessment if and when consumer credit responsibilities are transferred from the OFT to the FCA.

**13. Do you have any comments on the general coordination arrangements for the PRA and FCA described in paragraphs 2.138 to 2.149 and in Chapters 3 and 4?**

We are concerned that the PRA's veto power indicates that conduct and consumer protection issues will take second place to prudential regulation under the new regime.

Further, as has been pointed out:

“[T]o permit the PRA to overrule the FCA sends a dangerous message to the industry that only firms which are small enough to fail without causing damage to financial stability will be forced to bear the full consequences of mistreating consumers.”<sup>8</sup>

The Government has said that transparency will be an important factor in ensuring the PRA and FCA coordinate well. It is therefore unclear why the PRA should not at minimum publicly explain why it has resorted to a veto, as its use implies regulatory failure on the part of at least one of the new regulatory bodies.

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<sup>8</sup> Which?, *A new approach to financial regulation: building a stronger system – consultation response*, 14 April 2011

**14. Do you have any views on the detail of specific regulatory processes involving the PRA and FCA, as described in paragraphs 2.150 to 2.195 and in Chapters 3 and 4?**

**15. Do you have any comments on the proposals for the FSCS and FOS set out in paragraphs 2.196 to 2.204 and in Chapters 3 and 4?**

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