

StepChange Debt Charity response to HM Treasury consultation:

Financial Services Future Regulatory Framework Review: proposals for reform

February 2022

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Introduction

StepChange Debt Charity is the largest specialist debt advice charity working across the UK to support people struggling with problem debt. In 2021 we were contacted by almost 500,000 people seeking information and advice about debt.

We welcome the opportunity to respond to this HM Treasury consultation outlining proposals for reform of the financial services regulatory framework. As a debt advice charity, the experience of our clients highlights how financial services can create or contribute to poor outcomes for consumers, such as increased vulnerability to problem debt and the harm and hardship that problem debt causes.

The long history of widespread consumer problems with financial services highlights how poor conduct by firms, poor product design and the combination of these is linked to bad outcomes for consumers. This history tells us that effective regulation of financial service providers and markets is vital to improving consumer outcomes.

Given our role supporting households struggling with financial difficulty, we are particularly interested in regulation of consumer credit and mortgage credit markets, with aspects of insurance, pensions, savings and some aspects investments also relevant to the problems our clients may face.

Our starting point in response to this consultation is to emphasise the positive progress we have seen in some areas of financial services regulation in recent years, with the FCA tackling some longstanding causes of consumer harm in consumer credit markets.

However, as our recent report *Falling behind to keep up* highlights, there are still a number of areas where products and practices in credit markets are causing harm for financially vulnerable consumers.¹ The current discussion on the proposed Consumer Duty (in part as result of Section 29 of the Financial Services Act 2021) also highlights how the current FCA consumer protection objective and the FCA's high level principles have not delivered a culture where providers of financial services consistently put delivering good consumer outcomes at the heart of what they do.

Our response to the previous *Phase II* made the case of a new duty of care, and while we strongly support the proposed *Consumer Duty*, it remains to be seen whether this will deliver the culture change we associate with a duty of care. More generally, we urged the Government to use this review to consider how the FSMA might be amended to clarify and strengthen the authority of the FCA's consumer protection objective, but this is not clearly picked up in this consultation.

That said, we welcome the proposals in this consultation for activity specific have regards and obligations. Our previous response highlighted the need for legislation to give the FCA a clear and specific focus on financial inclusion. Our recent research shows how consumer credit markets

¹ StepChange Debt Charity (2022) *Falling behind to keep up: the credit safety net and problem debt*

continue to cause detriment for financially vulnerable consumers, with high cost credit still more strongly associated with harm. The current policy response is not sufficient. So we urge the Government to use the opportunity of any forthcoming Financial Services legislation to introduce a strong and targeted statutory financial inclusion focus for the FCA.

So while we welcome the commitment from Government in this consultation paper to maintaining high standards of consumer protection, the proposed Consumer Duty highlights the importance of the Financial Services and Markets Act 2000 (FSMA) regime setting clear expectations about firms' approaches to consumer protection. As a result, our responses to the consultation questions focus on making sure the proposed reforms do not reduce expectations or lower the bar of standards of consumer protection.

1. Do you agree with the government's approach to add new growth and international competitiveness secondary objectives for the PRA and the FCA?

As an advice charity supporting financially vulnerable consumers, we do have some concerns that the proposed secondary objective on growth and international competitiveness may come to blunt the FCA's focus on consumer protection.

We are somewhat reassured that the consultation paper points to the current FCA competition objective to highlight the Government's intention that the new secondary objective will not require or authorise the FCA to take any action inconsistent with its strategic and operational objectives.

However, the FCA's current competition objective has been specifically framed to promote the interests of consumers in the markets for regulated financial services. This framing is designed to naturally complement the consumer protection objective.

In contrast, the proposed growth and competitiveness secondary objective is directed at the UK economy as a whole, including the financial services sector as a whole. This may naturally compliment some parts of the FCA's responsibilities (such as those highlighted in the recommendations of the UK Listing Review) that are less likely to impact directly on the consumer protection objective. Our concern is that the proposed secondary objective becomes rivalrous to the consumer protection objective when applied to markets like mortgage or consumer credit.

We saw how a focus on growth in mortgage and credit markets in the decade leading up to the great recession contributed to widespread consumer harm, which could and should have been better addressed by financial services regulation.

Therefore we ask HM Treasury to consider and articulate further how the proposed secondary objective would work with the consumer protection and existing competition objectives in practice. The FCA's intention for the Consumer Duty to set higher expectations of firms (than the existing Principles and Treating Customers Fairly guidance) points to the subtle influences that specific

changes to high level regulation can have on the everyday practices and problems experienced by consumers. As a result it seems possible that a secondary objective on growth and competitiveness applied across all areas of the FCA's regulatory responsibilities could weaken the focus of the consumer protection and existing competition objectives.

Here we note the discussion on Measure 16 in this consultation that proposes an ability to establish activity specific 'have regards' and obligations. This approach would seem to allow a more targeted approach to aligning the Government's growth and competitiveness objectives to specific areas of FCA responsibility in a way that reduces the risk of any conflict with the existing consumer protection and competition objectives.

2. Do you agree that the regulatory principle for sustainable growth should be updated to reference climate change and a net zero economy?

Given the Government's commitments to tackling climate change and the transition to a net zero economy, it seems sensible to update the regulatory principle for sustainable growth to reference climate change and the net zero economy.

However, we note the commentary in paragraph 3.15 of this consultation that 'regulators are not required to act to advance their regulatory principles'. In respect of the regulators' focus on growth and competitiveness, the Government concludes that a regulatory principle 'would not provide the regulators with the appropriate statutory basis...' to advance this aim. This might also be the case for the Government's aim of strengthening the regulators' remit in respect of climate change and transition to net zero policy objectives.

3. Do you agree that the proposed power for HM Treasury to require the regulators to review their rules offers an appropriate mechanism to review rules when necessary?

StepChange Debt Charity agrees that there should be appropriate mechanisms for the regulators to review their rules when necessary. There may be several ways to successfully achieve this.

Firstly, we believe that there are existing formal mechanisms that could require the FCA to conduct a review of their existing rules. For instance, the section 234C 'super-complaint' process may result in the FCA reviewing its rules where these are material to the complaint. HM Treasury might consider whether this process might be strengthened by requiring the FCA to take action to remedy or prevent any consumer detriment identified as a result of the super-complaint process.

The consultation paper points out that judicial review is available to challenge the regulators' rules.

Secondly, the regulators could be placed under a stronger duty to review the effectiveness of their rules under their own initiative where they find evidence of features of a market at odds with their objectives (in particular the FCA's consumer protection and competition objectives), or at set periods after a significant change or introduction of rules designed to achieve a specific regulatory purpose.

Thirdly, as proposed in this consultation, HM Treasury could establish a power to require the regulators to review their rules when necessary. We agree that this could create an appropriate and proportionate route for Government scrutiny of the regulators' rules. However, we agree that

preserving the regulators' independence is also vital so we would urge the Government to clearly set out the scope and grounds for this power to be used, such as what might constitute exceptional circumstances in the public interest.

4. Do you agree with the proposed approach to resolve the interaction between the regulators' responsibilities under FSMA and the government's overseas arrangements and agreements?

While we understand the importance of the issues raised by this question, we are concerned should the FCA become constrained from executing its consumer protection objective in consequence of an overseas arrangement and agreement. Here we note the statement in paragraph 4.31 that actions by regulators, including by amending their rules, could be challenged under the dispute settlement mechanisms of a free trade agreement.

Earlier in this consultation response we set out a view that incremental changes to high level regulation, such as the proposed *Consumer Duty*, can have important consumer protection benefits, which might in consequence create some new requirements on firms. The discussion in Measure 5 does not set out a clear view as to how trade agreements or deference arrangements would be arranged in such a way to ensure that similar necessary (but likely hard to define and anticipate in overarching agreements) rule changes would remain possible.

The regulators' faced policy constraints when Britain was a member of the EU. However EU policy making (in areas such as the Consumer Credit Directive for instance) had a detailed and fairly transparent process with many opportunities for consumer advocates to participate in the policymaking process. The subsidiarity principle and legislative precision on minimum and maximum harmonisation provisions also gave some safeguards against consumer protection becoming ossified or falling to a lower common standard. It is not clear how these opportunities for consumer advocate participation or safeguards on consumer protection standards might be carried forward into future overseas arrangements and agreements.

5. Do you agree that these measures require the regulators to provide the necessary information to Parliament on an appropriate statutory basis to conduct its scrutiny?

We agree that Measure 6 and Measure 7 appear to be sensible and proportionate innovations that would help Parliament to conduct its scrutiny.

6. Do you agree with the proposals to strengthen the role of the panels in providing important and diverse stakeholder input into the development of policy and regulation?

StepChange agrees with the proposal to strengthen the role of the panels in providing input into the development of policy and regulation.

As an advice charity that advocates for policy change to make financial services markets work better for consumers (and financially and otherwise vulnerable consumers in particular) we recognise the important role of the statutory Consumer Panel.

However, consumers using financial services are an extremely broad group with a very wide range of differing needs, problems and concerns, which are not necessarily always aligned. Therefore we support the proposal to consider expanding the number of panel members to reflect this diversity of experience. We agree with the point raised in paragraph 6.15 that the panel system may currently underrepresent the needs of vulnerable consumers, so an expansion of the Consumer Panel might specifically focus on addressing this need.

Charities and not-for-profit organisations supporting and working with consumers are in a strong position to support the statutory consumer panel with data and insight on consumer on the issues consumers are facing with financial services providers and products. However giving consumers a voice takes up time and resources that can be in short supply for consumer groups.

So a strong and effective consumer panel also needs the ability to directly support consumer groups, where necessary, to deliver the insight that the panel needs. We urge the Governance to set out a strategy, as part of this review, that would allow the consumer panel to support (including through funding) collection of insight by consumer organisations.

7. Do you agree that the proposed requirement for regulators to publish and maintain frameworks for CBA provides improved transparency for stakeholders?

Our response to the previous future regulatory framework consultation raised a concern that the current regulatory principle set out in Section 3B 1(b) of FSMA 2000, and the form of CBA requirement that it drives, creates a high bar for the FCA to intervene to advance its consumer protection objective, particularly in respect of the needs of vulnerable consumers. In this respect we would urge the Government to consider whether the regulatory principle could be amended to reframe proportionality in terms of requiring interventions to be efficient and necessary to further the regulators' objectives; particularly where an intervention is aimed at supporting vulnerable consumers or reducing serious consumer detriment.

While we have concerns that the current CBA requirements may overly constrain the consumer protection objective, we agree that the proposal for regulators to publish and maintain frameworks for CBA will provide improved transparency for stakeholders.

8. Should the role of the new CBA Panel be to provide pre-publication comment on CBA, or to provide review of CBA post-publication?

We would suggest that any CBA panel is tasked with post-publication review rather than pre-publication comment. We agree with paragraph 6.28 that establishing a formal procedure for pre-publication comment on all CBA would very likely slow down policymaking. Even setting a threshold may not avoid this as decisions over how the threshold is applied may come under challenge by parties anticipating that an intervention may apply to them.

If the aim of this proposal is to improve transparency and confidence in the regulators' CBA approach, a post publication review focusing on methodology and approach seems preferable. However, we would urge the Government to consider how this independent panel would add value to

the current regulators' approach. For instance, the FCA can currently place a wealth of experience, capability and resource behind CBA, which is published in a reasonably transparent way.

In this respect we believe that a significant area where CBA methodology could be improved is in capturing and assessing the benefits of a proposed regulatory intervention to consumers. For instance, FCA CBA will often focus on direct consumer benefits (money saved) in a way that can undervalue broader consumer benefits (such as the value of greater wellbeing and lower social costs) that flow from addressing detriment.

While the consultation paper notes the potential cost to financial services firms of more, or more frequent, data requests from regulators, the Government does not appear to have considered the costs and difficulties of capturing and evaluating data on consumer detriment and the broader costs of this to consumers and society more generally.

Consumer advocacy groups (like StepChange) are in a good position to help the regulators to build a deeper understanding on consumer impact that could materially improve CBA. However, there is no particular strategy to support consumer advocate groups to do this. Therefore we urge the Government to consider whether the proposed introduction of a CBA panel should be accompanied by a strategy to support (and perhaps resource) consumer advocates to better inform CBA with data and insight.

9. Do you agree that the proposed requirement for regulators to publish and maintain frameworks for how the regulators review their rules provides improved transparency to stakeholder?

Our answer to question 3 suggested that regulators should be under a stronger duty to review the effectiveness of their interventions. Therefore we agree that regulators should be under a requirement to publish and maintain frameworks for how they review their rules.

However, the precise nature of the requirements for such a framework would need to be considered carefully. For instance, paragraph 6.37 suggests as an outcome of this proposal stakeholder confidence 'that reviews are happening regularly'. If a regular review requirement was applied across the entire FCA rulebook (for example) there is surely a risk of 'resource blight' that could undermine other important aspects of the FCA's work.

A more proportional approach would be to require regulators to conduct post-implementation reviews of rules at specified points after implementation and against criteria based on the outcomes that the rules were intended to achieve. We do not believe that a more general review of existing rules should necessarily be frequent, but the framework could require regulators to establish a proportionate schedule (taking account of other priorities under statutory objectives) to review existing rules over time.

10. Do you agree with the government's proposal to establish a new Designated Activities Regime to regulate certain activities outside the RAO?

We agree with the Government's proposal to establish a new Designated Activities Regime to regulate certain activities outside the RAO. However, the Government proposes not to restrict the

DAR to retained EU law, retaining the ability to designate other activities in future as necessary. This seems sensible, but we would urge the Government to ensure the criteria for allocating activities into DAR or RAO are clear and do not result in any reduction in consumer protection or regulatory oversight.

11. Do you agree with the government’s proposal for HM Treasury to have the ability to apply “have regards” and to place obligations on the regulators to make rules in relation to specific areas of regulation?

We agree with the Government’s proposal for HMT Treasury to have the ability to apply ‘have regards’ and to place obligations on the regulators to make rules in relation to specific areas.

Our main interest here is with the consumer protection and competition objectives of the FCA. The scope of the FCA’s responsibility is very broad and crosses financial services sectors and markets with very different users, issues and public policy concerns. So we agree with the argument set out in paragraph 7.39 that there needs to be a balance between cross-cutting and activity-specific regulatory principles. In this respect, we believe the FSMA regime could be made more effective by better targeting of sector-specific issues.

Our response to question 7 argued that the regulatory principle set out in section 3B 1(b) of FSMA 2000 might be amended to take better account of the consumer protection needs of financially and otherwise vulnerable consumers in respect of sectors, products or practices where there is a higher risk of consumer detriment.

Our response to question 4 of the previous phase II consultation highlighted the need for a better regulatory focus on financial inclusion issues. We argued that currently there is no clear duty or cross-cutting ‘must have regard’ provision to require the FCA to pursue financial inclusion as a core objective.

In Chapter 3 of this consultation the Government ruled out introducing a cross cutting financial inclusion objective or principle. We would ask the Government to reconsider whether the ability for HM Treasury to apply ‘have regards’ or rulemaking obligations to specific areas of regulation should include provision for financial inclusion in areas of regulation where there are known financial exclusion issues (for instance consumer credit and some aspects of insurance). Here we do not share the Government’s view that the FCA is sufficiently equipped through its operational objectives and regulatory principles to support the Government’s leadership on this agenda. Here, we note the recommendation of the Woolard review for the FCA to work towards increasing the participation of mainstream lenders in providing alternatives to high cost credit. It is not clear how the FCA can be certain of delivering significant progress on this recommendation under its current objectives and principles.