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

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

Carol-Anne MacDonald
Policy, Risk and Research Division
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London
E14 5HS

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Dear Ms MacDonald

DP13/1: Transparency

This is the Financial Services Consumer Panel's response to the Financial Services Authority (now Financial Conduct Authority) Discussion Paper on Transparency (DP13/1).

The Consumer Panel welcomes the FCA's discussion paper on this important subject. We firmly believe that transparency is a legitimate regulatory tool and, used effectively, can be a significant factor in improving accountability, firms' behaviour and consumer welfare and protection. We have long encouraged the FSA to increase the levels of transparency within the financial services industry and indeed itself. Therefore, we support in principle the ideas in the FCA's Transparency Paper.

We believe the suggestions we offer below will bolster the proposals. Specifically, we ask the FCA to:

- Consider the introduction of monetary rewards for whistleblowers, subject to effective screening to weed out fallacious allegations. The scale of reward could be linked in relevant cases to the proceeds of revealed financial crime or fines obtained from enforcement action. A whistleblower money reward scheme could usefully be combined with the offer of immunity from prosecution and a robustly enforced requirement that all firms have a fair and effective whistleblowing strategy in place.

- Consider the publication of Regulatory History Reports for firms to provide an accessible chronological summary of a firm's disciplinary record, covering the scale of enforcement fines and penalties, the names and number of directors sanctioned or prosecuted, the scale of compensation payouts, the number of complaints and the proportion referred to the Financial Ombudsman Service and upheld, the number of variations of permission, and so on.

- Produce periodically a comprehensive, high visibility, report that seeks to quantify the benefits as well as the costs of financial conduct regulation seen in the round;

- Randomly select each year a sample of FCA published cost-benefit analyses and subject them to rigorous peer review, as a spur to higher quality analysis;

- Publish a list of internal audit reports and consider, on a case-by-case basis, whether full publication of the audit would serve the public interest,

- Publish a periodic log of meetings held by senior FCA staff with external stakeholders, and;

- Embed changes to promote transparency in a clear and rigorous plan of action; as the Panel noted in its response to the FSA's 2008 DP, a code of good practice alone would be unlikely to prove effective.[1]

We also ask the FCA to require firms to:

- Present their complaints data in improved context e.g. firms should list complaints by brands;

- Ensure that annuitants have access to timely and appropriate information that makes clear the benefits of shopping around and of taking advice, and the distinction between full advice and execution only guidance;

- Ensure that any requirement to publish claims data for insurance products mandates the quality of the information, including its presentation;

We hope you find these points useful and expand on them in the main body of our response, which is attached to this letter.

Yours sincerely

Adam Phillips
Chair

[1] In its response to DP 08/3 (26th August 2008) the Panel argued that a Code would only be of use "if it is rigorous and carefully enforced. There have been examples of codes of practice in the past that were set up with the best of intentions but which meant little in practice." DP13/1 acknowledges the failure of the DP08/3 Code.

Introduction

The FCA has emphasised the need to strike the right balance between fostering the public's legitimate interest in transparency and refraining from disclosure where there would be unfairness in doing so, where the public interest might be harmed, or where other legal consideration might prevent it. The Panel agrees that there may be occasions where public interest considerations outweigh the FCA's responsibility to be transparent. We are, however, concerned that the paper appears to place undue emphasis on restrictions without balancing these against the FCA's legal responsibility to adhere to the principle of transparency.

The paper notes that it is constrained by section 348 of the Financial Services and Markets Act 2000. It also implies that the following significantly restrict the provision of information:

- the due process requirement around public censure,
- restrictions under the Freedom of Information Act,
- the Data Protection Act; and
- Article 8 of the European Convention of Human Rights.

Listing these alleged prohibitive legislations without providing more context or in-depth exploration sends out the wrong messages to stakeholders. For example, although section 348 of FSMA prohibits the sharing of specific types of information, section 349 allows regulations to be made by Treasury to modify the effect of section 348 for the purposes of facilitating a public function. By making such modifications, Treasury provides the FCA with a number of 'gateways' to disclose information to certain third parties e.g. other UK or European Economic Area regulators. Also, the FCA has the ability to use its rule making powers more proactively. We note, for instance, that although the FSA was prohibited from publishing information about the complaints firms received, it introduced a rule change which required firms to individually publish data, thereby allowing the FSA to also publish this information in a central location[2].

Also troubling are the DP's references to withholding information because disclosure may 'harm' the public interest. Here the DP's reticence draws on the presumption that consumers may misunderstand the information. We agree that consumers may be swamped by too much information, but the onus should be on the FCA and firms to communicate in a simple, concise and effective manner. The FCA can itself learn how best to communicate using its new insights from behavioural economics. Even if the manner of disclosure falls short of ideal, it should be recognised that consumers have a wide range of capabilities and the disengagement of the less knowledgeable should not normally be taken as an excuse to deprive knowledgeable consumers of useful information. More importantly, there are many experienced public commentators as well as professional advisers who can and do use information released by the regulator and by firms to help consumers make more informed decisions.[3]

[2] Section 348 allowed the FSA (and now the FCA) to publish information about individuals if this information is already publicly available.

[3] The Oxera literature review accompanying the DP notes how information intermediaries can enhance the effectiveness of disclosure by reducing consumers' information-processing costs. Oxera cites some second-best arguments that question the value of disclosure – for example, it may facilitate tacit collusion amongst firms – but the answer is to deploy a range of policies to emulate first best – in the example, to use competition powers in tandem with disclosure to invigorate the market.

The Consumer Panel's response to the FCA's ideas

Whistleblowing

The purpose of a Whistleblowing Policy is to encourage employees to disclose any malpractice or misconduct of which they become aware, and importantly to provide protection for employees who report allegations of such malpractice or misconduct. An effective whistleblowing regime therefore has the potential to bolster compliance and provide intelligence, particularly in industries where detriment could have a significant impact on the lives of citizens e.g. financial services.

Under the Public Interest Disclosure Act 1998 employees in the financial services sector can bypass the general obligation on them to report to their employers (in the first instance), and go directly to the FCA. We believe that this places an extra duty on the FCA to ensure that it inspires confidence pre and post disclosure. Therefore, the Panel supports the FCA's proposals to improve its policy in this area, and specifically to give more details to the Whistleblower about the action that has been taken, or were under consideration, after they have contacted the FCA. Relevant and timely feedback is an essential part of the process, as well as a concerted effort to raise employees' awareness about their legal protections under PIDA.

We agree that the FCA should publish data about the number of whistleblowing incidents, including any action or indeed inaction taken as a result of information received. It is equally important that the FCA is rock-solid in protecting the identity of whistleblowers, and provides adequate information at the very beginning of the process on the policies it has in place to protect whistleblowers' identities, should they wish to be anonymous.

The DP provides no analysis of the incentives that drive – or inhibit - whistleblowing. The regulator receives 3,000 to 4,000 whistleblowing tip offs a year but finds it possible to act on only a small proportion - about 12%. Without further analysis, it is not clear whether the high proportion of in-actionable intelligence is a mark of weakness in the regulatory system. It may be. The FCA's approach to whistleblowing relies on "moral incentive"[4] but an honest individual's willingness to report malpractice may be compromised by a number of considerations: erroneous belief that a practice is ethical if commonplace; perceived disloyalty to friends; fear that a reported malpractice will not be effectively corrected; fear of career-destroying reprisal.[5]

The Panel has two recommendations:

- The FCA should ensure all regulated firms have an effective whistleblowing policy in place, one not diluted by a culture of bullying or intimidation or limited (in the case of former employees) by the wording of compromise agreements. Supervisory and enforcement action should be taken against non-compliant firms.

- The FCA should carefully examine the case for the introduction of monetary rewards for whistleblowers, subject to effective screening to weed out fallacious allegations. Where relevant, the reward could be linked to the proceeds of revealed financial crime or fines obtained as a result of prosecution, thus emulating American practice.

[4] Evidence by Mr Wheatley taken by the Parliamentary Commission on Banking Standards, 27th February 2013.

[5] Even if the provisions of the 1998 Act succeed in protecting the whistleblower from immediate reprisals by the accused firm, the individual's career may be undermined by resulting industry-wide reluctance to hire. Research suggests that fears of reprisal and of ineffectual remedial response are key reasons that inhibit potential whistleblowers (see, for example, Smith, R. (2010), "The Role of Whistle-Blowing in Governing Well: Evidence from the Australian Public Sector", The American Review of Public Administration, 40(6), 704-721).

The FCA could usefully learn from the practice of competition regulators. For instance, the Office of Fair Trading incentivises whistleblowing by offering rewards of up to £100,000 to companies and individuals reporting cartel activity that leads to fines or criminal prosecution. Moreover, the first company or individual to blow the whistle on a cartel may be eligible for immunity from prosecution. We believe these two incentives could be adopted and adapted for financial services. Monetary incentives can be linked to any fines eventually obtained as a result of an FSA action (e.g.10% to 20% of the fine obtained). We would like the FCA seriously to consider and consult on these two specific incentives, especially in light of its new responsibility to promote effective competition. Finally, the advent of the new FCA provides a good opportunity for the FCA to re-launch its whistleblowing reporting telephone number and its policy.

Enforcement

The Panel has long called for increased transparency in the area of enforcement. One example is our call for the earlier publication of 'warning notices' which marks the beginning of a disciplinary process against a bank, particularly as few cases fail beyond this point. It remains the Panel's view that consumers have the right to know about the alleged shortcomings of the firms with whom they deal at the earliest opportunity, so that they can protect themselves and be vigilant against unfair behaviour on the part of the firms. We advocated that making this information public at an earlier point could also encourage firms to work with the FCA to achieve a speedy resolution to enforcement proceedings, in order to minimise reputational risk. To date, the FSA has only been able to publish decision notices and final notices.

However, the new FCA now has powers to publish information about the matters to which warning notices relate, as it considers appropriate pursuant to section 391(1)(c) of FSMA. This measure aims to bring "greater and earlier transparency" to the regulator's enforcement process which we believe could help consumers make more informed decisions. The legislation imposes restrictions on the types of cases where publication can occur and the details that may be released. Also, the FCA will not publish information where it can be shown that publication would be unfair to the firm or individual to whom it relates. We urge the FCA to limit its interpretation of 'fairness' in this respect and be clear about what fairness may mean in this particular context.

We support the FCA's proposals to publish the cost of investigations and the average length of investigations. We believe that these initiatives have the potential to drive improvements in the FCA's own efficiency. This type of information could also form part of the firm's 'Regulatory History' report which we suggest publishing under the section "Going beyond the ideas in the Transparency Paper" below. We do, however, question the wisdom of publishing enforcement resources by sector given this may provide valuable insight to less scrupulous firms.

Redress and complaint data

The difference between firms with regards to complaints handling can be significant and publishing complaints data enables the FCA to better achieve its statutory objectives by encouraging firms to improve their performance. Also, the Panel believes that a robust complaints procedure enhances compliance, fosters trust, and when effective, can provide important market intelligence which can be used to improve services, ward off impending problems, and inform consumer choice. Therefore, the Panel welcomes the FCA's proposals for greater transparency in this area; specifically we support the proposals to publish information about the redress payments made to consumers, including the formula and the criteria the FCA applies. We also support proposals which will see the FCA publish more information about the settlement process. We note that the FCA envisages some difficulty in publishing payment data, stating that although it could use section 165 of FSMA to require firms to provide data on redress paid, the information it receives would be regarded as confidential under section 348, and so the

FCA would need firms' permission to publish. In our view a more effective way of achieving the required result would be for the FCA to use its rule making powers to require firms to publish this information which the FCA could then use, as it did when it required firms to publish complaint data, as noted above.

The Consumer Panel has long called for better contextualisation of complaints data, and so we welcome the proposal to force firms to provide more context around published complaints data to improve understanding of what the data shows. There is a real need to provide context in a way which does not make the final result difficult to comprehend. One area where we feel that the current level of context could be improved is reporting by brand. Under the current arrangements when publishing complaint data firms will list the brands covered but will not be required to list complaints by brand. We believe it would be advantageous for consumers to have details of complaints by brand since, despite having the same parent company, brands often have separate management and are regarded separately by customers. For consumers to make effective use of the information that the FCA publishes, it needs to reflect their perceptions of financial products, rather than the firm's organisational reporting structures.

There are other areas where we believe the FSA could improve the way it presents complaints data. For example, at present complaints data is only published for firms that receive 500 or more complaints in the relevant reporting period. We understand the case for publicising data on high profile household name firms, but believe that in setting the threshold so high the FSA has overlooked the importance of complaints to smaller, local or niche providers, which may be lower in volume but could affect more vulnerable consumers. For instance, some IFA firms might have significant numbers of complaints relating to their overall client base but fall short of the 500 threshold. Since all authorised firms are required to maintain a record of complaints we do not see that the costs involved in publication would be unreasonable.

Again this information could form part of the 'Regulatory History' report we suggest under the section "Going beyond the ideas in the Transparency Paper" below.

Greater product disclosure and product performance

The Consumer Panel supports the FCA's proposal for greater transparency, firm disclosure, and product performance, particularly in the annuity market.

We agree with the FCA's assessment of the current constraints faced by consumers in the annuity market. Indeed we have drawn the regulator's attention to these precise issues in the past. We also agree that the new FCA, with a wider remit which includes a competition operational objective has a duty to ensure that the market operates more effectively so that consumer detriment is reduced and that the market is competitive.

It cannot be emphasised enough that purchasing an annuity is an important decision for consumers reaching retirement and one that cannot usually be put right if the wrong decision is made. One of our main concerns has been consumers' inability to engage effectively with the annuity purchasing process, and the consequences of this lack of engagement, which can result in the purchase of the wrong type of annuity at an uncompetitive rate. We would therefore like to see appropriate and effective regulatory requirements in place. In our view this must include an assessment of how the Open Market Option operates, the barriers to shopping around, and perhaps more importantly appropriately targeted intervention to ensure that this market operates more effectively.

The Panel is especially concerned that consumers who do try to shop around will be confronted with understanding the differences between full advice and non-advice. Particularly when non-advise sites and service may look like a full advised service to a consumer, yet, the purchase of an annuity on a non-advice basis could mean the consumer paying as much or more than if he or she sought full advice. The issue here goes beyond transparency where charges are concerned, non-advice, as execution only,

is not underpinned by the essential consumer protection mechanism i.e there is no recourse to the regulatory redress channels, which represent the hallmark of full advice. Therefore optimal transparency around the type of advice consumers purchase and the consequences of those choices is crucially important.

Publication of claims data for insurance products

The Panel supports the FCA's proposal that firms should publish claims data on insurance products. We agree that this could work well for "add-on and non-core products such as warranty, home emergency, identity theft, and mobile phone insurance". We also believe that publishing information such as claims per customer, successful claims percentage following initial contact, premiums vs. payout ratios and the rate of claims reduced or refused for non-disclosure may make the market work better for consumers.

Like the FCA we believe that greater information disclosure may lead to consumers focusing not just on price but product value and quality. Claims data that reveals poor performance may incentivise firms to improve behaviour to avoid negative publicity.

However, publishing claims data in a way that consumers will understand and pay attention to is the challenge in this area. We are therefore of the view that greater focus on the quality, rather than the amount, of information available would help consumers to ensure that the insurance product they are buying is suitable for their needs.

Given the proliferation of comparison websites we would also like the FCA to assess how it can apply improved transparency in this area, for instance around website owners, sponsors and incentives.

Going beyond the ideas in the Transparency Paper

The Panel believes that there are other areas where the FCA can encourage transparency and be a more transparent regulator. We list these below:

Publish a Regulatory History Report about firms: The Panel is of the view that the information consumers need to make an informed decision may often be available somewhere but is rarely easily accessible or conveniently located in one place. We believe the collation and presentation of a regulatory history report would greatly improve the way in which consumers engage and use information already in the public domain. In addition, an easily accessible history of regulatory behaviour could put extra direct pressure on boards to improve a firm's reputation.

To this end we recommend that the FCA should facilitate, on its website, a section[6] where consumers and other interested parties can find out about the regulatory history of a firm or individual. This should include findings by FOS, contextualised complaints data, prosecutions both successful and otherwise, sanctions, closures[7] etc. As far as possible, the record of poor practice should have a money value attached – for example, the money amount of compensation paid - to enable comparison across firms and over time. It would be important to have a clear chronology to enable readers to discount, if they were so minded, those penalties that occurred in the distant past.[8] We note that there is already precedent for the collation and presentation of this type of information by regulators such as the Solicitors Regulation Authority.

[6] Possibly the FCA register

[7] Again we note that the information we refer to are mostly in the public domain. We do not believe it would require a disproportionate cost to collate, even if in the interim this requires links to be provided to other sites.

[8] Mr Roger McCormick, director of the Sustainable Finance Project at the London School of Economics similarly suggests a "Sustainability Report": "What Makes a Bank a "Sustainable Bank"?", McCormick, R., (2012), *Law and Economics Yearly Review*, Vol. 1., Part1

Publication of Governance Documents: There is more scope for the FSA to be transparent with regards to publishing governance information. It is our view that the FCA should release board agendas prior to the meetings taking place. Moreover, more extensive minutes should be available after these meetings. The current style of minutes does little to improve understanding of the Board's priorities. Consideration should also be given to the publication of a list of Internal Audits, and full publication of the related report if thought in the public interest.

Periodic major report on Conduct Regulation Benefits and Costs
The Panel recommends that, subject to resources, the FCA should produce periodically a comprehensive, high visibility, report that seeks to quantify the benefits as well as the costs of financial conduct regulation seen in the round. Such a report could be seen as supplementing National Audit Office investigative reports and would provide the FCA with an analytical basis to challenge industry investigations that focus exclusively on excessive regulatory costs. Consumers have a clear interest in less costly regulation, but there exist a danger as memories of current scandals dim that too little weight will be placed on the associated regulatory benefits. The 2006 publication "The Cost of Regulation Study" commissioned jointly by the FSA and Financial Services Practitioner Panel provides an egregious example of the tunnel vision and regulatory capture that the Panel believes should be steadfastly avoided.[9]

Cost and Benefit Analysis: To help spur improvements in the quality of analysis, and as a further guard against regulatory capture, the FCA should annually subject a small random sample of its cost benefit analyses to rigorous peer review. The value of such an approach was demonstrated by the Panel's commissioning of peer reviews of the CBA[10] in the 2011 Mortgage Market Review Consultation Paper.

Log of Senior Management Meetings: We believe that the FCA's leadership team can do more to be transparent about its stakeholder meetings. This information can then be used by interested parties to gauge if senior managers are striking the right balance between engaging with its various stakeholders. We recommend a quarterly publication of meetings held with external parties by senior management of the FCA and do not imagine that this would prove too difficult to administer.

Campaign on transparent charges: We would like to see an energetic campaign by the FCA to improve transparency around costs and charges. The Panel has long argued that the cost of financial services is often opaque, multi-layered and excessive. We note that although one of the consequences of the Retail Distribution Review will be increased clarity around the cost of services, we believe that there is considerable scope for more regulatory activities around clarity of charges, so that consumers can do more to compare prices and make informed decision on the type of advice they need.

Conclusion

The Consumer Panel appreciates the FCA's efforts to commit to being a more transparent regulator, and to holding the financial service sector up to higher standards of transparency. Nevertheless, as highlighted above, we believe the FCA can and should do more to truly commit to the principle of transparency and achieve real and tangible benefit for consumers. Only by setting itself higher standards can the FCA expect the industry to follow suit and rebuild the public's trust. We urge the regulator not to lose sight of the real detriment caused to consumers when markets work in opaque and mysterious ways.

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[9] Deloitte (2006), "The Cost of Regulation Study". The Practitioner Panel qualified the findings by noting the addition of the FSA's "highly costly and time intensive" Treating Customers Fairly Initiative, which now lies at the heart of FCA philosophy.

[10] Peer Review of Part of Cost Benefit Analysis in Mortgage Market Review. A Report for the FSA Consumer Panel.

Finally, we hope that the FCA will place sufficient emphasis on the implementation of this change agenda, especially at a time when the regulator is stretched by the number and significance of other initiatives. If implementation takes the form of statements of principles alone then the desired outcomes will not be achieved. To this end we urge the FCA to focus on a robust change programme which will ensure that the letter and the spirit of these proposals are fully realised.