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

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Financial Inclusion Commission
c/o Policy in Practice
Shropshire House
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Dear Sir/Madam,

Written submission from the Financial Services Consumer Panel to the Financial Inclusion Commission

The Financial Services Consumer Panel was grateful for the opportunity to give evidence to the Financial Inclusion Commission on 25 November. This submission expands on our oral evidence. We have set out general principles rather than answer all the questions in detail.

Introduction

We welcome the initiative set out by the Financial Inclusion Commission, which builds on the work of the Financial Inclusion Taskforce. Access to financial services has long been a Panel concern since our mystery shopping of basic bank accounts in 2002. We were pleased to lobby successfully during 2011 for a 'may have regard' to access in the new regulatory legislation. Our paper on 'Access to financial services' published in 2013 outlines our position on access[1]. And today 'accessibility' continues to be one of the three key principles that guides our work, alongside 'trust' and 'competition'.

Meaningful access is not indicated simply by a consumer having a financial product or being able to get one, but requires the product to deliver real benefits. These benefits can be objective, i.e. financial, or subjective, i.e. peace of mind, self-esteem, personal satisfaction. The benefits derived also have to be sustainable over time.

Lack of access to financial products can stem from:

- Market failure
  - There are no products available in the market that meet consumers' needs
  - Consumers cannot access financial products due to firms' withdrawal from particular geographical areas/market segments/distribution channels.
- Refusal
  - Firms refuse to offer products to consumers
- Price/payment exclusion
  - Firms are only willing to offer products to consumers at prices that are unaffordable or represent poor value for money

[1] http://www.fs-cp.org.uk/publications/pdf/Access%20position%20paper20131218.pdf

    - Firms are only willing to offer products on payment terms e.g. direct debit, annual premium, which make them inaccessible or unaffordable.
- Condition exclusion
    - Firms are only willing to offer products with terms and conditions that significantly reduce their utility or value for money.
- Affordability exclusion
    - Consumers have insufficient disposable income to pay for financial products even when they are reasonably priced
- Self-exclusion
    - Consumers choose not to access financial products due to
        - A lack of awareness of what is available
        - A lack of financial capability or confidence
        - The complexity of products
        - Lack of trust in providers
        - An inability to access products via the preferred channel
        - Lack of perceived need for/value in having financial products
        - Psychological barriers.

From a regulatory perspective, appropriate access to financial products does not require that *all* consumers have access to *all* products. Indeed, in some circumstances it will be more appropriate that consumers do *not* have access to a particular product. Appropriate access means that all consumers are able to make informed decisions about whether to use financial products and are able to access products that are necessary for everyday money management, medium-term saving, smoothing and protection and longer-term asset building.

The significant knowledge imbalances between consumer and provider[2], the conflicts of interest between brokers and consumers and the imperfect market conditions often mean that the majority, rather than the minority, are excluded from making informed financial decisions. Financial exclusion is a continuum along which people's position is subject to frequent change, and often depends on product type. Increasingly, the 'utility' definition of products stretches easily beyond access to basic transactional facilities to insurance, credit – and if credit, savings. Financial inclusion is thus difficult to define but can be intuitively understood. Our paper on 'Defining consumer vulnerability and disadvantage'[3] published in 2012 provides useful insight into where different consumers fit into the 'continuum'.

Transactional banking services

Transactional banking facilities are crucial for everyday money management. There has been a wide variety of initiatives that have outlined the problems with access in this area and noted potential measures that could be taken, not only by the banks, but by others like utility providers, to help people on low incomes. Products are now emerging which not only prevent a customer going overdrawn, but also do not charge unpaid item fees. These accounts typically cost a few pounds a month but do not have 'nasty surprises'.

It is our belief that on paper very little stands in the way of people getting access to a bank account. Rather it is a decision on the part of the provider to actually provide it. There is currently little pressure on firms from the regulator to address the issues so often cited as barriers (e.g. the interpretation of Joint Money Lending Steering Group Guidelines) because access is often seen as a 'social policy' rather than a 'regulatory' issue. The Commission would be well advised to consider this issue in the light of its recommendations to the parties involved. We were pleased, however, to note the FCA's

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[2] See our Position Paper on Consumer Responsibility for a more detailed expose http://www.fs-cp.org.uk/publications/pdf/position-paper-consumer-responsibility.pdf

[3] http://www.fs-cp.org.uk/publications/pdf/Defining_disadvantage_&_vulnerability.%2020%20December%202012.pdf

recent work on 'vulnerability' and commend this to you. We are following their new programme on 'access' with interest.

The EU Payment Accounts Directive, requiring that consumers have the right to open and use a payment account with basic features, brings fresh momentum. The Directive must be transposed into UK law by September 2016. The Panel believes it is important that the minimum features in the directive are met in a way that meets consumers' needs; that there are no administrative barriers to exercising the right to an account; and that costs are reasonable.

Basic banking facilities cannot be viewed in isolation of the rest of the personal current account (PCA) market which relies heavily on horizontal and vertical cross-subsidisation. The Panel's report[4] on Cross-Subsidisation in the PCA market examines the nature of cross-subsidisation and highlights the possible winners and losers emerging from changes to the current 'free-if-in-credit' model. The Commission may wish to note the example set in the Netherlands where the industry agreed with the Salvation Army to provide current account services free of charge to those who cannot afford them. Financial inclusion in the Netherlands is at 99%.

Even where people are able to access accounts, inclusion must deliver benefits. The Financial Ombudsman Service saw a big increase in complaints last year from people on low incomes who had been treated unfairly by their banks. This may be another area for the Commission to consider.

Credit

Access issues relating to credit are complex because while some consumers are unable to access the credit products they need, there is clear evidence that others have been granted credit when they should not have been, due to a lack of compliance with regulation. We are pleased that the regulation for credit has come to the FCA so that the rules, most of which have been in place for a very long time, can be enforced properly.

The Panel was concerned by the bad practice the FCA found in the debt management sector and looks forward to a time when this is stamped out. However, it raises questions about access to ethical and affordable debt advice.

The Panel has welcomed the FCA's scrutiny of the short-term high cost credit market and is supportive of the regulator's intervention in this market to cap the total cost of credit and eradicate widespread poor practice in the market. The Panel has also, however, argued strongly that unauthorised overdrafts also fit the FCA's definition of short-term high cost credit and should, therefore, be subject to the same regulatory scrutiny. In relation to the FCA's upcoming review of the credit card market the Panel has stressed the need for the review to understand the different ways that credit cards are used by different groups of consumers and the way that these different patterns of use interact with particular product features and marketing practices.

Mortgages

The mortgage market presents different types of access problems. The new affordability assessments brought in with the Mortgage Market Review (MMR), have led to a number of mortgage 'prisoners' - borrowers who are trapped with their current lender. Typically, this is someone who comes to the end of a fixed term period and cannot remortgage or go elsewhere because they no longer meet the affordability criteria. Many require no extra borrowing and their personal circumstances have not changed since taking out the original mortgage. However, they are having to pay more because they cannot negotiate a cheaper rate, thus making them vulnerable to repossession. While the number of people in this position is relatively small, the Panel believes there is a need for a specific

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[4] http://www.fs-cp.org.uk/publications/pdf/pca_literature_review_report_FINAL%2020140911.pdf

rule to ensure that consumers are not unfairly treated or discriminated against by reason of their inability to access alternative, more competitive mortgage products.

The Financial Policy Committee has recently consulted on plans to introduce limits on measures such as Loan to Value and Loan to Income. The Panel believes that the FCA's affordability rules should be sufficient to combat irresponsible lending and that arbitrary limits will prevent access to lending for people who could afford to repay a loan.

Insurance

Nearly everyone needs at least one General Insurance (GI) product, whether it is compulsory insurance such as motor insurance, or other insurances such as home or travel cover. In recent times the market has adapted to changing customer demands and technological advances, however not all of these changes have been in the interests of consumers, creating detriment, dissatisfaction and potential exclusion for some consumers.

There are a number of key issues affecting consumers of GI products:

- Insufficient information to enable choice – it can be difficult for consumers to make an informed choice when buying on-line. Policies tend to be promoted on headline price which exploits people's natural behavioural biases, with little other information about important features such as exclusions and excess fees. This leads to problems when consumers try to claim and realise that they are not covered for something, or have extremely high excesses.
- Lack of affordable cover for groups of people appropriately – and inappropriately - labelled 'high risk' - Basic policies with charged for extras may reduce the availability of affordable insurance for some consumers. There is a risk, therefore, that certain groups (e.g. particular age groups seeking travel or motor insurance) could become excluded from GI products as the scope of what firms deem to be mainstream becomes narrower and any non-standard requirements are not covered or carry prohibitively high charges.

The biggest problem, however, is in the increasing use of more individualised underwriting. As risk pools get smaller, cross subsidies decrease, and those perceived to be at the riskier end can get priced out altogether.

Advice

Financial products are often complex and financial decisions can have far reaching consequences. There is generally too much choice, rather than too little. The pensions freedoms available from April 2015 will generate a bewildering range of choices for consumers ill-equipped to make them. What consumers need therefore is access to a range of services that provide, within clearly defined parameters, information, guidance or specific recommendations.

The Retail Distribution Review, which reformed the regulated investment advice market, has led to a greater degree of professionalism and a removal of commission bias. On the downside, advice is now charged for explicitly and the market is excluding people with relatively small sums to invest. People on low incomes who have regularly sacrificed to save for their retirement are vulnerable to losing out if they cannot access appropriately priced advice and products. Automated online advice services have sprung up to fill this gap, but consumers are often not aware that if they buy a product this way they are, in effect, buying it execution only and have no recourse to redress for miss-selling.

The Mortgage Credit Directive, which introduces new mortgage regulations due to come into force in March 2016, raises concerns about the possibility of new 'hybrid' equity release products that could fall outside the current regulatory regime for Lifetime mortgages and into the MCD regulations. The issue here would be that currently, advisers working in the equity release market are required to hold a relevant and specific qualification. If products that are ostensibly equity release products fall into the MCD, unqualified advisers and those who do not have proficiency in the equity release market will be permitted to advise on and sell these products.

Unregulated advice, which can mean information and guidance as well as generic advice, is a valuable tool for consumers. The Panel believes the Money Advice Service should push regulatory boundaries to deliver a more effective service for consumers. It will be vital that everyone who needs it has access to the 'Guidance Guarantee' as they make decisions about managing their assets post-retirement.

Savings

Most people recognise that having some savings is a good idea, and of course building up a 'savings buffer' can help reduce reliance on short-term debt. It should be made easier to save 'little and often' with a choice of accounts available for those who do not have large sums to open their accounts with or put away each month.

Savings are countercyclical, so people will tend to save more (or at least pay off debts if they can) in a downturn. The trick is to get people to save rather than spend as confidence returns.

The commission may wish to consider matched funding initiatives like Saving Gateway, which have been demonstrated to work.

Financial capability, behavioural psychology and cognitive neuroscience

The occurrence of behavioural biases is taken into account by the FCA in its consideration of risk. Further understanding in psychology, cognitive neuroscience and economics would aid MAS and others in the delivery of both financial capability and advice initiatives. Some industry players are beginning to use tools like eye-tracking etc to hone their marketing. It is imperative that MAS, the social sector and advisers in the pay of consumers do their best to keep up to speed to challenge the use of these tools but also to make use of them appropriately to help people make more informed choices.

Innovation

The FCA has launched a new Innovation Hub, designed to help new and established businesses to introduce innovative financial products and services to the market. The Panel believes the Hub should focus on encouraging innovation which meets the particular needs of groups who are currently excluded or poorly served by financial services firms.

We hope the above will assist the Commission in its work. Please do not hesitate to contact us for more information.

Sincerely,

Sue Lewis
Chair
Financial Services Consumer Panel