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

Richard Lawes
Conduct Specialists Department
Financial Services Authority
25 The North Colonnade
Canary Wharf
London
E14 5HS

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Dear Richard

Retail product development and governance – structured products review Guidance Consultation Review

This is the Financial Services Consumer Panel's response to the FSA's Guidance Consultation on retail product development and governance for structured products.

The Panel is pleased that the FSA has undertaken an assessment of seven major providers of structured products in the light of concerns about the growth in sales of structured products and the increasing complexity of the products themselves. We are fully supportive of action by the FSA to help firms to meet their obligations to retail customers and to the regulator.

We have no specific comments on the technical content of the proposed Guidance, although much of it seems to be a statement of what should be obvious to firms, rather than an expansion of complex or opaque regulatory requirements. If that is what is needed however, we are glad that the FSA is providing it. We would have liked to have seen more examples of existing good industry practice included within the guidance, but it may be that no others were found.

Our major concern is the findings of the review itself, which we thought were deplorable. There is evidence of non-compliance across the board, from product design to consumer communications and post-sales administration, suggesting breaches of the principle of Treating Customers Fairly in a number of areas.

Collectively the findings were strong indicators of significant potential consumer detriment across a number of major firms and, given the nature and extent of non-compliance, we are concerned that this potential detriment may have crystallised already in some areas. While the Guidance cannot be retrospective, we would expect post-sales reviews initiated now to identify such existing consumer detriment, which should be addressed immediately by firms and by the FSA. We urge the FSA to consider enforcement action against those firms whose non-compliance has led to consumers being mis-sold, mis-informed or where their interests have been put at risk.

Our particular concerns included:

- Product approval processes that contained a number of weaknesses, with some failing as a result of commercial pressures.

- Widespread failure to identify target markets, suggesting product creation (and, it seems, subsequent distribution) based on income generation and not consumer need or demand.

- A lack of understanding of the complexity of individual products and the use of exotic indices for what firms considered to be relatively simple products.

- Variable levels of training and support offered to distributors, with reliance on financial promotions as a source of product information.

- Deficiencies in the standard of terms and conditions relating to early redemption charges and difficulty in explaining product features to consumers.

- Inadequate post-sales product monitoring and inappropriate systems and controls for outsourced post-sale administration.

The fact that there are firms operating in this highly sophisticated market that actually have to be reminded of the most basic principles of governance and treating customers fairly demonstrates the urgent need for the FCA's more proactive, interventionist approach.

We recommend that the FSA undertakes further work in the structured products sector shortly, including consumer research and mystery shopping. If there is still evidence of non-compliance within the sector we recommend that the FSA immediately puts prescriptive rules in place to protect consumers.

We note that the FSA has undertaken a Cost Benefit Analysis of the Guidance in the light of its commitment to undertake and consult on a CBA if proposed Guidance is likely to impose significant costs that were not considered when the FSA consulted on the rules to which the Guidance relates. It is explained in Annex 3 to the Consultation that such significant costs could be generated by aspects of the Guidance that relate to TCF outcomes and product stress-testing and modelling in particular. It seems to us however that firms already complying with FSA requirements are unlikely to incur any significant additional cost at all. If firms find the cost of basic compliance and treating their customers fairly too high, we suggest they consider exiting this sector of the market.

Our assessment of the possible costs themselves, as set out in Annex 3 (including Table 1.1), is that they would be far outweighed by the cost of complaints handling, restitution and financial penalties that would be incurred by firms failing to deliver TCF outcomes and/or demonstrate compliance with FSA requirements. In our view firms should already be operating on a basis that is consistent with the Guidance as a matter of good practice. As is identified within the CBA, the principal benefit of the guidance will be improved matching of products to consumer needs. This will be a considerable step forward for consumers and firms alike. We urge the FSA to be robust in dealing with any claims from firms that the costs of compliance with the Guidance are disproportionate or in any way prohibitive.

Yours sincerely

Adam Phillips
Chair
Financial Services Consumer Panel