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Enforcement Review

10 July 2014

Review of enforcement decision-making at the financial services regulators: call for evidence

This is the Financial Services Consumer Panel's response to the Government's call for evidence on the enforcement processes of the Financial Conduct Authority and the Prudential Regulation Authority. We are grateful to the Treasury for allowing us to respond beyond the deadline of 4 July.

We have only addressed Q1 in detail, but we also touch on Q12.

Q1: Do the current enforcement processes and supporting institutional arrangements provide credible deterrence across the spectrum of firms and individuals potentially subject to the exercise of enforcement powers by the regulators? If not, what is the impediment to credible deterrence and where does it arise?

First, of course, firms must be aware of enforcement action against other firms, which may not always be the case, especially with the smaller players in the market

To be an effective deterrent, enforcement must change the behaviour of firms. That means they need to see that bad things happen to firms which break the rules. This goes beyond fines, which many regard as the cost of doing business, to individual or corporate loss of reputation, and loss of customers and shareholder value. The impetus for change may come from senior management – who do not want to risk putting their own firm at risk – or indirectly through shareholder or consumer pressure.

We believe that deterrence could be increased if the regulator were to harness the power of consumers in helping to 'co-regulate' the market through competition and switching. There is currently very little evidence about how consumers use knowledge about enforcement action in the financial services market to make informed decisions about choosing or switching providers.

To fill this gap, the Panel recently conducted a survey of consumers. We will shortly follow this up with consumer focus groups.

In our survey, 41 percent of respondents said that fines for financial misconduct would influence their decision 'a great deal' when choosing a financial services provider, the second highest reason for choosing a provider¹. A quarter of respondents also said that if

¹ Ipsos MORI on behalf of the Financial Services Consumer Panel conducted a Face to Face Omnibus Survey in June 2014 (unpublished as yet). 2nd highest response in a multiple response question, the main influence was 'previous experience with the financial services provider' at 43%.

their current financial provider had been convicted of a crime, e.g. manipulation of interest rates, they would decide to switch providers².

That consumers do not, in practice, switch away from firms which have been subject to enforcement action in large numbers suggests strongly that they are either not aware of the action, or that there are barriers to switching.

We believe there are a number of measures which would help increase consumer awareness, both retail and for small firms.

As a first step, there should be an onus on firms and individuals who have had an enforcement action taken against them to alert their customers to this fact, ideally in the form of a letter which outlines the sanctions and the scale of consumer detriment. More importantly, the same communication should give consumers the choice to leave the service provider without any penalty charges that would otherwise be applicable.

We have previously suggested the FCA to publish a Regulatory History Report at firm level, which would include information about findings by the Financial Ombudsman Service, particularly uphold rates, contextualised complaints data, prosecutions both successful and sanctions, closures etc. As far as possible, this record should have a monetary value attached to poor practices, for example the amount of compensation paid – to enable comparisons across firms and over time.

Although this information is generally publicly available, it is rarely easily accessible and is not conveniently located in one place. We believe the collation and presentation of a Regulatory History Report could greatly improve the way in which consumers engage with the enforcement information already in the public domain. A report of this kind could also inform shareholders and encourage boards to demand changes to protect or restore a firm's reputation

We believe there is scope to go further in making enforcement information accessible. The Food Standards Agency, for example, has some pragmatic, effective tools for raising standards in the food industry. These include mandatory hygiene ratings posted on the doors of restaurants and traffic light labelling for processed foods. We think the regulator and industry could learn from these, and similar, examples.

Question 12 says that early settlement can benefit consumers by getting compensation to them earlier than enforcement proceedings would have done. While this is true, early settlement means a loss of transparency. Firms' misdemeanours are not made public so cannot be used by consumers to make decisions, and the deterrent effect is lost.

The Panel has also called for consumers to be made aware, as early as possible, of 'warning notices' which mark the beginning of the disciplinary process against a firm, particularly as few cases fail beyond this point.

² In a multiple response question this was the 3rd most important influence on switching (26%) after 'if another provider provided better rates, fees or conditions for a similar product or account' (43%) and 'if you were personally dissatisfied with the customer service provided by your current financial provider (42%)