

Financial Services Consumer
Panel response to: HMT
Treasury's 'Regulated
activities – second
consultation document'

Regulated activities, Financial Services and Markets Act 2000 Financial Services Consumer Panel response to: HM Treasury's 'Regulated activities – second consultation document'

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Executive Summary

- a) The Treasury should ensure that its legislation awards the same rights to spouses and cohabitants.
- b) Where definitions of eligibility to third party rights exist, the Treasury should ensure consistency or explain why definitions differ.
- c) The Treasury should include long term care insurance as a regulated activity in the Regulated Activities Order and should not be hindered in doing so by the delay in discussions on long term care.
- d) The Treasury should not abolish the minimum denomination for allowing longer term debt securities providers to avoid authorisation.

- e) Arrangements capable of bringing about a deal, even if they do not, should be included as a regulated activity under article 23: arranging deals in investments.
- f) Editorial comment on specific type of investments could mislead so the exemption should only apply if there is no negligent mis-statement. Furthermore, in line with the comments we make in our response to Treasury's consultation on the Financial Promotion Order, we suggest that exemption should be conditional on disclosure of any financial interest.
- g) The Treasury should ensure that the Regulated Activities Order gives the FSA power to prevent abuses arising from websites which appear to give services of one kind (eg advice), but then direct users to execution-only services with lesser protection.
- h) The Treasury should look at its original objectives for wanting the FSA to regulate pre-paid funeral plans and re-assess article 55 against those objectives.
- i) We are pleased that the Non-Exempt Activities Order has been tightly drawn and that advising on a recommendation to buy a particular investment has been included as a specified non-exempt activity. This will contribute substantially to consumer protection.

Introduction

1. This paper is the response of the Financial Services Consumer Panel ('the Panel') to the Treasury's consultation document 'Regulated Activities'.
The Financial Services Authority (FSA) established the Panel to advise the FSA Board on the interests and concerns of consumers, to report on the FSA's effectiveness in meeting its consumer protection and public awareness statutory objectives and to keep under review and influence developments in financial services in so far as they impact on consumers. Further information about the Panel is available at the end of this document.
2. The Panel have also responded to the Treasury's simultaneous consultation documents 'Financial Promotion' and 'Regulating mortgages'. All of the Panel's responses to public consultations are published on the Panel's website at <http://www.fs-cp.org.uk>.

Regulated Activities Order

General comments

3. The text of the Order has significantly improved accessibility from previous drafts. It is therefore disappointing that the commentary is not more helpful, particularly to public interest organisations with limited resources to consider the document in the very short consultation period.
4. We draw Treasury's attention to the need to give advice agency workers clear guidance about the boundary between regulated and non-regulated activities. Such agencies could play a useful role in the dissemination of generic advice on financial services, particularly stakeholder pensions. Yet because of the complexity of the legislation, and worries about their own liability, these agencies tend to avoid giving any generic advice on financial services. The Panel would further draw Treasury's attention to the valuable work such organisations do in helping people manage their

debts. They may well be hampered in this work by being unable, for example, to discuss a client's mortgage endowment options with them.

5. An important element of consumer protection is provided through the protection of third party rights. That is, individuals other than the person who owns the financial product, may also be protected where they have an interest. Similarly, in defining certain activities as not requiring authorisation, the Treasury has set out those individuals who have third party rights. However, there are a number of anomalies in the definitions of individuals to whom third party rights should apply. For example in article 3, which describes how to interpret words in the Order, a close relative is described as a spouse, children, step-children, parents, step-parents, brothers, sisters, step-brothers, step-sisters and spouses of any of the above. In article 66 (2), by contrast, those able to benefit from employee share schemes are defined as 'wives, husbands, widows, widowers, or children or step children'¹. The definitions do not reflect the actual pattern of family life in the UK today and excluding unmarried partners and ex-spouses is unacceptable and unjustified.

The Treasury should ensure that its legislation awards the same rights to spouses and cohabitants.

Where definitions of eligibility to third party rights exist, the Treasury should ensure consistency or explain why definitions differ.

6. The Treasury has particularly asked for comments on:
 - a) The modification of the business test for deposit – taking and investment business in the Business Order and the retention of the “by way of business” test for insurance business (referred to in paragraph 1.22);
 - b) The regulation of mortgages and whether it is likely to disturb the securitisation market (referred to in paragraph 3.5);
 - c) The definition of the funeral plan contract and whether it will create difficulties for the industry by catching ad hoc arrangements where pre-payments are made (referred to in paragraphs 3.8 and 5.32);

¹ Pg 85, HMT's regulated activities consultation document.

- d) The extension of the “principal purpose” tests to all media, the reformulation of the “principal purpose” test and whether it works equally well for all types of media (referred in paragraphs 3.9, 5.29 and 5.30);
 - e) The extension of the certification process to all media (referred to in paragraph 3.10);
 - f) The new hedging exclusion and whether the concept of a “primary transaction” is workable (referred to in paragraph 3.20 and 5.22);
 - g) Including an exclusion from deposit-taking for deposits received by a solicitor in the course of his profession (referred to in paragraph 5.13);
 - h) Abolishing the minimum denomination requirement for debt of more than one year and whether this will impact on consumer protection (referred to in paragraph 5.18);
 - i) The possibility of relaxing the overseas persons exclusion (referred to in paragraph 5.40); and
 - j) Whether the regime relating to the delegation of investment management by the trustees of an occupational pension scheme should be liberalised and whether the current regime discriminates against investment in private equity funds (referred to in paragraph 7.4).
7. We have comments on these issues and a number of others. We have ordered our comments as they arise in the Regulated Activities Order.

Article 3 – Interpretation of “qualifying contract of insurance”

8. The definition of a qualifying contract of insurance should include long term care. We note the absence of a statement from the Treasury on whether long term care insurance will be a regulated activity and the growing interest of older people in these products. We are concerned that continuing discussion on long term care insurance, as it stands, will miss the laying of the Regulated Activities Order, but this is no reason to exclude long term care insurance as a regulated activity.

The Treasury should include long term care insurance as a regulated activity in the Regulated Activities Order and should not be hindered in doing so by the delay in discussions on long term care.

Article 7: Accepting deposits – sums received by solicitors

Comment invited on: *Including an exclusion from deposit-taking for deposits received by a solicitor in the course of his profession (referred to in paragraph 5.13)*

9. Article 7 excludes from the definition of the regulated activity of accepting deposits 'sums received by solicitors'. We question whether this exclusion is necessary. The definition of 'accepting deposits' to be regulated includes the requirement that the money received must be lent to others or the deposit taker's activities are financed at least materially out of the deposit. Solicitors receiving sums from clients should not be using this money to finance their activities nor lend it to others. Certainly, if they do, it should be treated as a regulated activity.

Article 8: Accepting deposits – debt securities

Comment invited on: *Abolishing the minimum denomination requirement for debt of more than one year and whether this will impact on consumer protection (referred to in paragraph 5.18)*

10. Article 8² excludes from the definition of the regulated activity of accepting deposits 'sums received on terms involving the issue of debt securities'. In the commentary to the draft Regulated Activities Order, the Treasury explains that it has broadened the scope of this exclusion. For longer term debt securities the Treasury says 'it will allow debt raising from retail without authorisation so long as the debt has a maturity over one year'. No case is made in the commentary for any need to extend the scope. This exclusion is too sweeping, and the abolishment of a minimum requirement for longer term securities could allow retail investors to be drawn into a potentially risky investment by suggestions of high returns

where the risk is played down. This is particularly important at a time when some retail investors faced with lower nominal interest rates are very open to products which promise higher returns. Prescribed information is not an adequate substitute, as much recent research has shown a lack of financial literacy among retail investors.

The Treasury should not abolish the minimum denomination for allowing longer term debt securities providers to avoid authorisation.

Article 23: Arranging deals in investments – arrangements not causing a deal

11. We are concerned that the definition of arrangements excluded from requiring authorisation in article 23³ could have the unintended effect of excluding arrangements that are capable of bringing about a deal, even if they do not. We assume the Treasury only intends this article to exclude arrangements which are incapable of bringing about a deal.

Arrangements capable of bringing about a deal, even if they do not, should be included as a regulated activity under article 23: arranging deals in investments.

Article 29: Arranging deals in investments – introducing

12. We understand that it is the Treasury's intention to reflect existing exclusions for regulated arranging deals in investments for introducers. Whilst we are not clear why the wording of this exclusion is different from the wording in the 1986 legislation we are content to see the exclusion mirror the 1986 exclusion.

13. The Order does not reflect the inclusion of mortgage lending within regulated activities with respect to introducers. Where the introducer is the agent of the lender, not the borrower, how far would the activities of the introducer in arranging the mortgage fall within the scope of the legislation? In such circumstances, the Treasury must make clear who is responsible for the actions of the introducer.

² Pg 41

Article 34: Managing investments – attorneys

14. We hope that this Article will also apply to attorneys and guardians appointed under the Adults with Incapacity (Scotland) Act 2000.

Article 50: Advising on investments – advice given in newspapers etc.

15. We are concerned that the exclusion from requiring authorisation for the activity of ‘advice given in newspapers etc.’ is too wide. For newspapers, it is possible that the principal purpose test could be worked and subsequently checked but a big newspaper could give a great deal of bad and partial advice to a lot of people and do a lot of harm and still not fall within the regulated activities. With newer media, it seems very hard to apply the test at all and subsequently to check it

Editorial comment on specific type of investments could mislead so the exemption should only apply if there is no negligent mis-statement. Furthermore, in line with the comments we make in our response to the Treasury’s consultation on the Financial Promotion Order, we suggest that exemption should be conditional on disclosure of any financial interest.

16. Since the ‘principle purpose test’ may prove to be an ineffective tool for the regulator, other consumer protection considerations in defining advising on investments and the related exclusions must err on the side of protecting consumers. Requiring a publication to become authorised in order to carry on its activities does not have to be viewed as the end of the world, indeed the magazine, ‘*Growth Company Investor*’, www.growthcompany.co.uk, is authorised.

Comments invited on: *The extension of the “principal purpose” tests to all media, the reformulation of the “principal purpose” test and whether it works equally well for all types of media (referred in paragraphs 3.9, 5.29 and .30)*

³ Pg 56

17. The nature of websites will make it very difficult to prove that one section/site had the principle purpose of advising on investments as the boundaries between other sections and sites may be fluid. A particular problem in applying the principal purpose test to websites could be where a website provides execution-only business and it, or a related site with links, is giving advice on investments. There is also the risk of a website giving generic advice which is biased in favour of one particular type of investment, and then giving a link to a related site which is selling those investments on an execution-only basis. We are not clear from the consultation document how electronic news services (such as a regularly updated electronic news service emailed to a mailing list) will be treated. We consider that this should be treated in the same way as a 'tip sheet'.

The Treasury should ensure that the Regulated Activities Order gives the FSA power to prevent abuses arising from websites which appear to give services of one kind (eg advice), but then direct users to execution-only services with lesser protection.

Comment invited on: *The extension of the certification process to all media (referred to in paragraph 3.10)*

18. We question what value certification has for consumers. How has certification worked under the previous regulatory system? Has certification ever been revoked? Have certificates ever been given in respect of the weekly 'money supplements' of particular newspapers? How do 'advertorials' affect certification? These issues should be addressed before certification is extended.

Article 55: Funeral plan contracts – plans covered by insurance or trust arrangements

Comment invited on: *The definition of the funeral plan contract and whether it will create difficulties for the industry by catching ad hoc arrangements where pre-payments are made (referred to in paragraphs 3.8 and 5.32)*

19. Our main concern with the definition of regulated funeral plans is that it looks to the unwary as if there is a vast range of protection for consumers when in fact, very few plans will be covered.
20. We reiterate here our belief that consumers and their families of all funeral plan contracts should have access to the Financial Ombudsman Service irrespective of whether or not they are within FSA regulation.

The Treasury should look at its original objectives for wanting the FSA to regulate pre-paid funeral plans and re-assess article 55 against those objectives.

Article 57: Regulated mortgage contracts

Comment invited on: *The regulation of mortgages and whether it is likely to disturb the securitisation market (referred to in paragraph 3.5)*

21. We have given comments on the regulation of mortgages in our response to Treasury's consultation paper 'Regulating mortgages' which we have published alongside this response.

Article 67: Overseas persons

Comment invited on: *The possibility of relaxing the overseas persons exclusion (referred to in paragraph 5.40)*

22. Paragraph 5.40 of the Treasury's commentary on the Regulated Activities Order asks for views on relaxing article 67 which defines those overseas persons who will be exempt. We strongly urge the Treasury not to relax this article. At a time when consumers are more likely, via the internet, to purchase financial products from overseas persons, sometimes unwittingly, it would be dangerous for the Treasury to widen the exclusion. For example, one of the major concerns we have with respect to consumer dealing with overseas persons over the internet is that consumers are unlikely to realise that they may well not have access to statutory redress mechanisms. The commentary does not make the case for any consumer or commercial benefit arising from any extension and we oppose it.

Exemption Order

23. It is not clear from the Exemption Order, and there is no commentary on it, whether small Christmas savings clubs and similar groups will be exempt from FSA's regulatory scope. The Treasury needs to clarify this.

Non-Exempt Activities Order

24. The Treasury has particularly asked for comments on:

- The proposal to specify dealing in investment as principal but not other related activities such as dealing as agent and arranging (referred to in paragraphs 6.6-6.9);
- The proposed specification of discretionary investment management but not safeguarding or administration (referred to in paragraphs 6.10-6.14);
- Whether it is necessary to specify particular circumstances as not amounting to a recommendation (referred to in paragraphs 6.18-6.19); and
- Whether recommendations should be specified only in relation to buying and subscribing for investments and disposal of personal pensions rights or whether they should extend to other transactions such as underwriting and other disposals (referred to in paragraphs 6.15-6.22).

25. We were previously concerned that the boundary between mainstream and incidental business would leave many consumers without adequate protection. We are pleased that the Non-Exempt Activities Order has been tightly drawn. This will contribute substantially to consumer protection.

26. We particularly welcome the proposal that specifies that advising on a recommendation to buy a particular investment is a non-exempt activity. Such advice from an unauthorised adviser could both confuse individuals and expose them to unnecessary risks.

We are pleased that the Non-Exempt Activities Order has been tightly drawn and that advising on a recommendation to buy a particular investment has been included as a specified non-exempt activity. This will contribute substantially to consumer protection.

Comment invited on: *Whether it is necessary to specify particular circumstances as not amounting to a recommendation (referred to in paragraphs 6.18-6.19)*

27. We do not see the need to specify particular circumstances as not amounting to a recommendation. Such a list would quickly become out of date and could increase confusion. It may also open up gaps in protection if there are special circumstances applying. For example, a tax adviser might use the exemption for information on the maximum permitted pension to act as an introducer to a company representative, rather than an IFA. While members of professional associations are usually required to refer clients only to an IFA, anyone can call themselves a 'tax adviser' and may not necessarily be a member of a professional organisation.

Business Order

Comment invited on: *The modification of the business test for deposit-taking and investment business in the Business Order and the retention of the "by way of business" test for insurance business (referred to in paragraph 1.22)*

28. The Panel has no comments to make on the test for insurance businesses. However, we are concerned (in view of the comments in paragraph 1.22 of the Treasury's document) that the current drafting for deposit-taking omits the current condition catching anyone who 'accepts deposits on more than particular occasions'. We think the current drafting could fail to catch businesses which conduct deposit-taking on a less than 'day to day' basis and would like to see the current Banking Act definition retained in full.

About the Financial Services Consumer Panel

The Financial Services Consumer Panel was established by the Financial Services Authority (FSA) in December 1998 to ensure that consumers' interests are represented in the development of the regulation of financial services. The Panel is independent of the FSA so that it can: advise the FSA on policy as it evolves, monitor the FSA's effectiveness in meeting its statutory objectives towards consumers, review developments in financial services where they impact on consumers, and publicly report its findings and recommendations. It can raise its own concerns and has resources to carry out its own research.

Who is on the Panel?

Barbara Saunders (Chairman)

Barbara is a public interest member of the PIA Board. She is an independent consumer consultant and past Chairman of the Council of the Insurance Ombudsman Bureau. Among other public and professional appointments she is a Non-Executive Director of the West Hertfordshire Hospitals NHS Trust and a member of the Architects Registration Board.

Colin Brown (Vice Chairman)

Colin is an independent consultant specialising in consumer affairs. Previously Deputy Director of Research at Consumers' Association and Senior Fellow at the Policy Studies Institute, he has over 20 years' experience of social and consumer research.

Jean Gaffin

Jean was Chairman of the Advisory Committee on Telecommunications for Disabled and Elderly People (until 31.12.1999) that provides advice to the telecommunications regulator, OFTEL, and is a Non-Executive Director of Harrow & Hillingdon Healthcare NHS Trust. She has extensive experience of working on behalf of vulnerable consumers. Previous positions include: the Executive Director of the National Council for Hospice and Palliative Care Services and Chief Executive of Arthritis Care.

Yvonne Gallacher

Yvonne is Chief Executive of Money Advice Scotland, which was set up by the Scottish Consumer Council. She has over 10 years experience of consumer credit/money advice issues and of working with vulnerable consumers in a variety of roles, including debt counsellor, trainer and manager. She is Co-Director and Secretary of the Government funded Lead Body for Advice, Guidance, Counselling & Psychotherapy (CAMPAG). Yvonne is a member of the Scottish Consumer Council.

Joan Harbison

Joan is Chief Commissioner of the Equality Commission for Northern Ireland. She was Chair of the Commission for Racial Equality for Northern Ireland since its inception in 1997 and is a former Chairman and member of the Executive Committee of the Northern Ireland Association of Citizens' Advice Bureaux. She has held a number of public appointments including being Vice Chairman of the Eastern Health and Social Services Board and the Northern Ireland Standing Advisory Commission on Human Rights and was a founding member of the Human Fertilisation and Embryology Authority.

John Howard

Solicitor with extensive experience as a former presenter/editor of the daily consumer programme on Radio 4 'You and Yours'. John is currently a freelance broadcaster and his work includes presenting personal finance TV programmes. He is a member of Mortgage Code Compliance Board.

Vinod Kumar

Social scientist with market research skills and extensive voluntary and public sector experience of policy analysis and research. Now retired, Vinod has previously worked for the Commission for Racial Equality and was Head of Policy and Research at the Royal National Institute for Deaf People. He is currently Non-Executive Director of Barnet Health Authority, Board member of the South Barnet Primary Care Group and member of the Consumer Liaison Group of the Medical Research Council.

Gerald Lanchin

Gerry is a Vice President of the National Federation of Consumer Groups. He is a former Under Secretary of the Consumer Affairs Division of the Department of Trade and Industry and author of "Government and the Consumer". His involvement in consumer protection includes being a former Council Member of Consumers' Association and of Consumer Congress Committee. He was the first chairman of the Direct Mail Services Standards Board and a member of the Data Protection Tribunal for 10 years.

Nick Pearson

Nick is the National Money Advice Co-ordinator for the Federation of Independent Advice Centres. A career spent in advice organisations including the National Association of Citizens' Advice Bureaux where he was manager of the Money Advice Support Unit, he has particular experience of credit, debt and personal finance issues and of working with vulnerable consumers.

Paul Salvidge

Paul is a former Senior Civil Servant with extensive experience of regulatory work, employment law, competition, consumer protection, telecommunications, financial services and company law. He was previously Competition Policy and Consumer Affairs Director at the Department of Trade and Industry.

Richard Smethurst

Richard is Provost of Worcester College, Oxford University; he chairs the Training Standards Panel of IMRO, of which he is a non-executive Director. He has served as an economic adviser in Whitehall, and the Monopolies and Mergers Commission, where he was Deputy Chairman. Richard lectures widely on financial and economic topics to businessmen and adult education groups. He is President of the National Institute of Adult Continuing Education.

Jane Vass

Jane is an independent consumer researcher specialising in financial services. She was previously Head of the Financial and Economic Research Group at Consumers' Association and is still author and editor of a number of Consumers' Association publications in addition to other research, including work for the National Consumer Council. Her current committee memberships include: Council of the Ombudsman for Estate Agents, the Inland Revenue Tax Law Rewrite Project Consultative Committee and the FSA Training Advisory Panel.

Dave Watts

Dave is a partner in a media business which is involved in publishing, editing and journalism - personal finance plays a large part in this. He is a former editor of "Which?" and "Money Which?" and former Assistant Director of Consumers' Association. He was also a policyholder representative on the Insurance Brokers Registration Council for nine years.

How to contact the Panel

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