

Financial Services Consumer  
Panel response to: HM  
Treasury consultation  
*standards for retail financial  
products*

May 2001

## Standards for retail financial products

Financial Services Consumer Panel response to:

HM Treasury's consultation 'standards for retail financial products'

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## Executive Summary

- a. For the CAT mark concept to be successful, the Treasury must be clear about what message it wants consumers to read into the CAT mark and ensure that CAT marked products live up to these expectations.
- b. It is important that any standard-setting encourages individual companies to cut out the inherently poor aspects of their own products without leading customers to assume that a bench-marked product is necessarily suitable for them.
- c. In order to increase transparency, any CAT marks need to be as specific as possible and avoid falling into vague generalities.
- d. Suitability issues may exist as much for CAT marked products as other products. Regulation of the sales process will continue to be necessary to prevent mis-selling of CAT marked products and of products which can be marketed as alternatives.
- e. We agree that the FSA's disclosure regime will be important in preventing mis-conceptions about CAT standards, about suitability and the degree to which they carry risk. But if a CAT marked product requires more than one or two qualifications about its safety in particular situations, then that is likely to reduce both the effectiveness of the disclosure regime and the value of the CAT mark concept. The same applies for consumer education.
- f. Inadequate CAT standards may be more damaging than no CAT standards since they create a dangerous 'halo effect' and perverse incentives for industry.
- g. We suggest caution for introducing CAT-standards into heavily segmented markets because a standardised product is less likely to be widely suitable.

- h. Government must have a strategy for making advice more widely available, properly supported and funded. If accrediting generic advice helped achieve this then the Panel would be supportive.
- i. The credit card market is too segmented to risk a 'one size fits all' CAT mark. The benefits of the proposed credit card CAT mark could be delivered through a code of practice and addressed by Unfair Contract Terms legislation.

## Introduction

1. This paper is the response of the Financial Services Consumer Panel ('the Panel') to HM Treasury's consultation 'standards for retail financial products'. The Financial Services Authority (FSA) established the Panel in December 1998 to represent the interests of consumers and to report on the FSA's effectiveness in meeting its consumer protection and consumer awareness objectives.
2. We welcome the consultation document 'standards for retail financial products' which raises key issues for all consumers, including those currently without many financial products. We welcome the open tone of the consultation and range of ideas put forward in it.
3. It appears that the Treasury hope consumers will become familiar with the CAT 'brand' rather than what the initials stand for, since they are different in each case. For this branding to be meaningful to consumers, they must have a correct understanding of what the brand CAT stands for and yet the Treasury have stepped back from setting this out. We can see two types of reasons for having defined standards. First, to create safe havens, ruling out inherently poor products and so to provide reassurance. Secondly, to give the marketplace an incentive to move towards products which are more consumer-friendly, without stifling innovation. If the Treasury intend consumers to consider CAT marked products a 'safe haven' they must say so and have a clear and consistent strategy for putting this message across, otherwise the branding won't work.

**For the CAT mark concept to be successful, the Treasury must be clear about what message it wants consumers to read into the CAT mark and ensure that CAT marked products live up to these expectations.**

4. However, we also warn that it would be hard to identify a CAT product that would be suitable for all. They cannot be the solution for every problem. CAT marked products may also require regulation to address the suitability issue and they must not distract Government from other regulatory tools

where necessary. In our response to the Treasury's consultation document on long term care insurance, we warned of the danger of inadequate CAT marks. Unfair Contract Terms legislation may be a more effective way of dealing with many inherently poor products and therefore the Office of Fair Trading (OFT) and other qualifying bodies must be encouraged to be proactive to tackle problems where they arise.

**Do readers agree there is a case for identifying retail financial services or products suitable for inexperienced users? If so, is it right to conclude that products for inexperienced users should be simple, clear and fair to help people understand what they are buying?**

5. Anything that increases transparency and comparability helps all consumers and not just the inexperienced. As such, if CAT standards are appropriate, they will not just benefit inexperienced users but all consumers. In addition, there is a case for identifying products that do not contain nasty surprises so that individuals can assume that they won't 'bite'.
6. However, it would be dangerous to have products with CAT marks that are so weak that they fall into generalities and do not guarantee against 'nasty surprises'. Weak CAT marks might even give false reassurance, as we suggest is the case in relation to the proposed CAT marks on long term care insurance<sup>1</sup>.

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<sup>1</sup> See the Panel's response to HM Treasury's consultation document on long term care insurance, March 2001 available on the Panel's website at <http://www.fs-cp.org.uk>

**It is important that any standard-setting encourages individual companies to cut out the inherently poor aspects of their own products without leading customers to assume that a bench-marked product is necessarily suitable for them.**

**In order to increase transparency, any CAT marks need to be as specific as possible and avoid falling into vague generalities.**

### **Should the existing regulatory techniques be adapted to provide this service?**

7. It is not clear from the consultation document how the Treasury envisages regulatory techniques adapting in the light of CAT marked products. However, we warn the Treasury that a benchmarked product should not of itself lead to 'lighter-touch' regulation of selling. Any regulatory dividend' to firms to reflect inherent safeguards in products should be carefully considered alongside the risk of consumer detriment resulting from the purchase of these products in situations where they are not suitable. The Treasury's own consultation document points out, in paragraph 98, that the products are intended to be a starting point from which consumers may find it helpful to assess competing products against their own needs and aspirations but as we know, consumers rarely do this in a vacuum. The sales process may shape a person's evaluation of their own needs and aspirations and can turn a 'safe' product into a 'dangerous' one (and vice versa). In any event, there are few truly harmless product types. What makes a product risky is often its unsuitability to an individual purchaser. For example what made low-cost endowment mortgages so dangerous was their widespread sale to low to middle-income consumers who had no inkling of the risk of under-performance.
8. Furthermore, the overlap between CAT marked products and similar products in the sales process may create a need for the sale of CAT marked products to be backed up by regulation. For example, the Personal Investment Authority (PIA) issued regulatory guidance about the sale of personal pensions in advance of the availability of stakeholder pensions to prevent mis-selling of personal pensions.

**Suitability issues may exist as much for CAT marked products as other products. Regulation of the sales process will continue to be necessary to prevent mis-selling of CAT marked products and of products which can be marketed as alternatives.**

9. In para. 98, the Treasury suggests that the FSA's disclosure regime will be important in preventing mis-conceptions about CAT standards, about suitability and the degree to which they carry risk. We assume that the Treasury think this disclosure should specifically refer to the CAT standard, e.g. – 'whilst this product meets the charges, access and terms agreed by the CAT mark, it does not mean that it is suitable for you or free from risk'. We agree that there is a significant likelihood of CAT marked products having a halo effect, indeed this is part and parcel of the 'CAT mark' branding. However, if a CAT marked product requires more than one or two qualifications about its safety in particular situations, then it is likely to reduce the effectiveness of the FSA's disclosure regime.
10. The Treasury may also be considering the use of consumer education to enhance the effectiveness of CAT standards on consumer behaviour and competition. We support FSA's work on consumer education but have continually warned against over-reliance on it. It is new and untested as a regulatory tool and is unlikely to bear fruit for some years (and any success is very hard to measure). Consumer education is likely to work best in conjunction with other regulatory tools.

**We agree that the FSA's disclosure regime will be important in preventing mis-conceptions about CAT standards, about suitability and the degree to which they carry risk. But if a CAT marked product requires more than one or two qualifications about its safety in particular situations, then that is likely to reduce both the effectiveness of the disclosure regime and the value of the CAT mark concept. The same applies for consumer education.**

11. The Panel strongly welcomed the comparative information tables initiative currently in development by the FSA. These tables could be used both to strengthen and inform CAT marks. If one aim of CAT marks is to encourage the market to move towards more consumer-friendly products,

comparative tables may have a similar role, and FSA and Treasury should work together to ensure that they are complementary. In particular comparative information tables may help a standard cope with change, by helping to identify if a CAT mark starts to fall behind what is happening in practice. Depending on the products for which CAT marks are proposed, comparative tables would have to be made available for a much wider range of products than currently proposed, and possibly produced by other regulators. For example, PayCom might be encouraged to develop comparative tables for products within banking/loans sector.

### **Is there value in defining standards for basic financial products? Should the Government do this? If not, who should?**

12. What is important is that the standards have to be robust. A standard that is set too low may be dangerous if it encourages customers into a product without also encouraging the market to improve the overall quality of products. For example, the CAT marked standards for long term care insurance proposed in a previous Treasury consultation<sup>2</sup> are very low – for example, a 13 week period for claims processing is very generous, and we regret the failure to set any standard definitions for ‘activities of daily living’ or even to refer to the existing ABI standards.

### **Inadequate CAT standards may be more damaging than no CAT standards since they create a dangerous ‘halo effect’ and perverse incentives for industry.**

13. It may be confusing for consumers to have CAT standards for different aspects of different products, from cover to cost to comparability. The initial success of stakeholder pensions in encouraging personal pension plans (PPPs) to improve their competitive position over the past year or so shows that it is standards that are important, not that they are called a CAT. The Panel hope that stakeholder pensions will continue to have a positive impact on the pensions market generally.

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<sup>2</sup> HM Treasury’s consultation document: *long term care insurance* was published in December 2000

14. Some CAT standards seem to be targeted at a segmented market, e.g. – basic bank accounts that target the socially excluded. There will be many people for whom a range of CAT marked products aren't right so they need to be developed in such a way as to make this clear. Paragraph 98 of the Treasury's consultation document highlights the difficulties for consumers of taking the correct message about CAT marked products – there is no implied guarantee that a CAT standard product will suit everyone, nor that they are risk free. Consumer education will have an important but particularly difficult role in helping people understand what CAT standards are and are not: in highly segmented markets, this will be even harder.

15. Product segmentation may also affect the willingness of product-providers to support a CAT mark, if a particular standard is too far removed from what providers perceive as a product designed for a particular segment of the market-place. This may explain why mortgage CAT-standards have not yet become widespread. In heavily-segmented markets, alternative means of encouraging consumer-friendly products may be preferable to CAT marks, such as a clearly-targetted benchmark or (depending on the level of consumer detriment) action under the Unfair Contract Terms legislation.

**We suggest caution for introducing CAT-standards into heavily segmented markets because a standardised product is less likely to be widely suitable.**

16. The Government should ensure that it has looked across current initiatives and identified links which might be made with CAT marks. An example is the ABI's 'Raising Standards' initiative, although we recognise that this is a voluntary scheme and will not cover all providers. A consistent message is vital otherwise any consumer education initiatives might get lost in a welter of competing messages.

17. Another factor in considering introducing CAT marks is being able to cope with change. We are not clear what happens to a CAT mark if market

shifts radically, whether companies be able to carry on using a CAT mark ad infinitum or whether the Government can upgrade them. These appear to us to be important considerations (and see our comments above on ensuring consistency with FSA's comparative tables).

### **Is it right to conclude, as in the Cruickshank report, that for some transparent products it is better to define product standards without a price limit?**

18. We agree that standards need to be tailored to the product but are concerned about significant consumer confusion if some CAT marks relate to price and other do not. It might be better only to use the term 'CAT mark' where the price is capped and to look for other terminology for other standards, although this may reduce the incentive for the industry to participate.
19. Ignoring price limits does not seem appropriate for basic bank accounts, where the equivalent of a price is a charge. Capping these or ruling them out is surely one of the major reasons for introducing basic bank accounts.
20. The Treasury needs to weigh up the purpose of any standard before ruling out price standards. For example, credit card market prices are very low for introductory rates and highly competitive at the margins but the mainstream providers are still very expensive and slow to respond to interest rate changes. It is certainly worth looking at more subtle ways of pushing prices down than simply imposing a cap, e.g. responsiveness to rate changes, the consistency of offering a generally low rate rather than just a low introductory rate. We already have a standardised APR that is supposed to supply comparability.

### **Are the suggested criteria for using products (box G) right? Could they be improved?**

21. Box G concentrates on comparability but this is likely to be hard in a highly segmented market. CAT marks might even restrain shopping around on

price if they suggest that a product is 'OK'. How is a consumer to know that the CAT mark applies only to cover rather than price?

22. If the reason for having a CAT standard is to create a safe haven and provide reassurance, the Government must be sure that a halo effect doesn't develop around a product which may have other aspects that consumers don't like, such as the risk to capital on a CAT marked equity ISA. If there are products which have some undesirable features and government wants to encourage change, a code of practice dealing with the problem feature may be more effective than a more all-encompassing CAT mark. For example, one of the welcome aspects of the mortgage CAT mark, has been to shift the market towards daily calculation of interest, and it might have been preferable to concentrate on this rather than a more general CAT mark which has not been widely taken up overall.

23. Recent CAT mark proposals have included requirements for 'clear' information. As they are not policed, CAT marks ought to concentrate on easily quantifiable standards, such as (for clarity of information) standard documentation or perhaps plain English accreditation.

**Which retail products, if any, should the Government consider for quality standards? Should any of these possible new standards define a price limit?**

24. Whilst we welcome the Government's consideration of CAT standards for credit cards and suggest that they should also look at credit agreements where consumers face similar lack of clarity, the Treasury should not make decisions on this sector until the task force on indebtedness reports.

25. We note that the 'price' of credit is particularly difficult to assess because, for example, it can include interest on interest. Any quality standard needs to address this point.

26. Those aspects of credit card practice which lead to most consumer detriment should, in our view, be dealt with by a code of practice or addressed by Unfair Contract Terms legislation. Any aspects of price, terms and conditions that are left relate to a highly segmented market and so may affect suitability for some people but not others. People use credit cards for very different things, for convenience or debt management. It is not clear, therefore, what credit card CAT marks would do for consumers.

### **Is there a role for generic advice standards? – and for pension advice in particular?**

27. In its report 'Consumers in the financial market: annual survey of consumers, 1999', the Panel drew attention to evidence that few consumers go to advisers for a financial health check and that there still seems to be a sales based approach to advice. The Panel welcome the opportunity to promote debate on how to best provide access to advice.

28. The important issue is for Government/other to have a strategy for making advice more widely available, properly supported and funded. In its 1995 report *Financial services and low income consumers* the National Consumer Council called for an investigation into the feasibility of a free, independent financial planning service, financed by the government with a contribution for industry. Its 1997 report *Savings and investments for low-income consumers* suggested that voluntary advice bodies and the financial services industry might collaborate in building up a register of practicing independent financial advisers prepared to give a 'first stage' interview outlining an individual's options but with no selling involved. These suggestions should be pursued, and if accrediting generic advice helped increase provision the Panel would be supportive. There is a growing gap between heavily regulated 'advice' & completely unregulated info-providers. A possibility for bridging the gap could be built into accreditation standards, e.g.:

- training and competence standards;

- a 'free' introductory interview along the lines of the green form scheme for legal advice. To avoid this merely becoming a sales pitch for further services, an accreditation scheme might require some particular items to be covered;
- working with the Community Legal Service;
- provision of free access to FSA comparative information tables; and
- cross-referral to an independent advice service only, not tied.

29. Accreditation might give information providers, e.g. telephone help line staff or advice workers an incentive to acquire some form of basic qualification. This might then increase the provision of generic advice.

30. Any accreditation scheme should undergo rigorous piloting to avoid any dangers that disreputable advisers might use it as a way of generating leads. It would also be important to look at the experience of the Lord Chancellor's Department in setting standards for the community legal service.

**Government must have a strategy for making advice more widely available, properly supported and funded. If accrediting generic advice helped achieve this then the Panel would be supportive.**

### **Is the proposed credit card CAT standard (Annex E) sensible? Could it be improved? How?**

31. We have stated above, paragraphs 25-26, that it is difficult to have standards for credit cards because of the problems of comparing rates, in particular the difference between standard rates and introductory deals. It is important to recognise that CAT standards for credit cards may not be useful for everyone – some might like to have a annual membership fee and lower rates, and others prefer higher rates which they don't have to pay if they pay on time.

32. However, we see much to welcome in the proposed CAT marks. Rather than run the risk of 'one-size fits all' CAT marks, we think that the most

important aspects of the standards could be addressed in an effective code of practice or (if providers fail to comply) Unfair Contract Terms legislation. These include:

standards for penalties on late payment/non-payment. This is something a benchmark ought to be particularly useful for as consumers are not in a position to judge for themselves; and

choice of statement date

a commitment to responsible marketing

clarity about consumers' rights and responsibilities relating to credit cards used as part of a flexible mortgage.

**The credit card market is too segmented to risk a 'one size fits all' CAT mark. The benefits of the proposed credit card CAT mark could be delivered through a code of practice and addressed by Unfair Contract Terms legislation.**

## 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?

#### Colin Brown (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.

#### Ann Foster (Vice-Chairman)

Ann is a former Director of the Scottish Consumer Council and has over twenty years' experience in the consumer movement. She is also a member of the Consumer Council for Postal Services. She was formerly Director of Government Affairs with Monsanto.

#### Jean Gaffin

Jean chaired OFTEL's Advisory Committee on Telecommunications for Disabled and Elderly People until 31 December 1999 and is currently a Non-Executive Director of Harrow & Hillingdon Healthcare NHS Trust. She has extensive experience of working on behalf of vulnerable consumers. Previous posts 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, set up in 1989 by Scottish Consumer Council. She has over thirteen 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 has also lectured and co-authored a Guide to Money Advice in Scotland. Yvonne is presently a member of the FSA Consumer Education Forum and Credit Union Consultation Panel. Yvonne is a member of the Scottish Consumer Council.

## **John Howard**

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

## **Vinod Kumar**

Vinod is a 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.

## **Nick Pearson**

Nick is the National Money Advice Co-ordinator for the Federation of Information and 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 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 on 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. Other research has included 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.

## **Harriet Hall**

Harriet is a solicitor with considerable experience of consumer policy and retail financial services. She is a former legal officer with the National Consumer Council, where she worked on the needs of low income consumers, banking, credit, mortgages, regulation of equity release and long-term care insurance, the Financial Services and Markets Bill and the proposed EU directive on distance selling of financial services.

## **Dianne Hayter**

Dianne is the Chief Executive of a new cancer charity, the Pelican Centre. She is the former Director of Corporate Affairs for the Wellcome Trust and was previously the Chief Executive of the European Parliamentary Labour Party and, prior to that, Director of Alcohol Concern. She has substantial voluntary sector and trade union experience.

## **How to contact the Panel**

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