

September 2010

EXECUTIVE SUMMARY

Transparency: The Consumer Panel's View

Background

One of the objectives the Panel has set itself is to encourage the FSA to increase levels of transparency within the financial services industry. It is important that consumers have enough information, and the right sort of information, to enable them to make informed choices. The Panel has a particular responsibility to advise the FSA on its approach to transparency and to encourage it to be bold in this regard.

Since the implementation of the FSA we can look back and see how expectations of what it means to be transparent have changed. We are now living in a climate where parliamentary, regulatory and corporate bodies across the world are being urged to say more about things on which they have traditionally been silent. And the Freedom of Information Act 2000 (FoIA) is both a response to this new climate and a contributor to it.

The Panel firmly believes that transparency is a legitimate regulatory tool and, used effectively, can be a significant factor in improving compliance, without necessarily requiring the alternative of 'expensive' enforcement action. In addition it can only help consumers better understand the work of the FSA and financial services firms better understand what is expected of them. Accordingly, the Panel thinks now is an appropriate time for the FSA to determine its policy on greater transparency. The FSA has been given statutory powers that allow it to publish specific information which will help it better achieve its objectives so the Panel believes it is legitimate for it to do so and to a greater degree than it does at present.

This position paper is a statement of where we believe the FSA is and where it should be. It is backed by a piece of research the Panel recently commissioned to benchmark the FSA's approach to regulatory transparency against equivalent State regulators overseas. Our aim is to stimulate an informed and energetic debate, one that takes account of the real concerns and statutory barriers to some sorts of disclosures, and at the same time recognises the powerful advantages that transparency can bring about. As a result of opening this debate we wish to press the FSA to move further

towards becoming the world leading regulator in this regard we would like it to be.

Consumer Panel research

In light of the Panel's commitment to pushing the FSA to be more transparent it recently commissioned a piece of research which benchmarked the FSA's approach to transparency against several other overseas regulators on a number of criteria:

- Disclosure of complaints data
- Disclosure of firms entering enforcement
- Response rates to Freedom of Information requests
- Disclosure of firms' compliance with financial promotion rules
- Disclosure of governance procedures

On the whole the FSA fared favourably against its overseas counterparts:

- On complaints, where the FSA has committed in the past 12 months to publishing regulated firms' data, the FSA was actually ahead of the game, no other State financial services regulator having made such a commitment.
- With regards to the publication of enforcement proceedings the research indicated that the FSA was not out of line with the practices adopted elsewhere so seemingly in the middle of the pack.
- It was a similar picture with regards to its response rates to Freedom of Information requests – better than some, worse than others.
- The FSA's approach to disclosing firms' compliance with financial promotions rules came out as being somewhat more transparent than many regulators but lagged behind some of the US examples.
- On governance the FSA's position was again ahead of many but less transparent than in the US.

What does this mean?

The FSA has evidently given some thought to transparency as a regulatory tool. It issued a discussion paper on the subject in 2008 and followed that with a commitment to publish firms' complaints data, an initiative which met with a lot of pushback from the industry but has now been implemented. In addition the Panel's research indicates that the FSA, on the whole, compares quite well with other State regulators in its approach to transparency, perhaps behind the US but a long way ahead of some others. What else then need the FSA do?

It is the Panel's view that for the FSA to really set itself apart as a world-leading regulator it needs to go further than it has at present and become even more transparent. The following are ways in which we believe the FSA should do this:

Publication of complaints data – in addition to FOS's initiatives in this area, the FSA has made available a considerable amount of information for consumers and commentators alike. Accordingly, the Panel's research indicated that the FSA was already ahead of the game internationally in this regard.

The differences in performance between firms with regards to complaints handling – as the FSA's own recent thematic work has shown – can be significant and publishing complaints data enables the FSA to better achieve its statutory objectives by encouraging firms to improve their performance on this front. Nevertheless, we recognise the importance of contextualisation, and the need to provide context in a way which does not make the final result unwieldy or difficult to comprehend. One area where we feel that the current level of context could be improved is reporting by brand. Under the current arrangements when publishing complaints data firms will list the brands covered but will not be required to list complaints by brand. We believe it would be advantageous for consumers to have details of complaints by brand since, despite having the same parent company, brands often have separate management and are regarded separately by customers. For consumers to make effective use of the information that the FSA publishes, it needs to reflect their perceptions of financial products rather than firms' organisational reporting structures.

There are other areas where we believe the FSA could improve the way it presents complaints data. For example, at present complaints data is only published for firms that receive 500 or more complaints in the relevant reporting period. We understand the case for publicising data on high profile household name firms, but believe that in setting the threshold so high the FSA has overlooked the importance of complaints to smaller, local or niche providers, which may be lower in volume but could affect more vulnerable consumers. Since all authorised firms are required to maintain a record of complaints we do not see that the costs involved in making details public would be unreasonable.

Publication of enforcement proceedings – our research identified that the FSA was not out of step with other overseas regulators in its approach to naming firms going through the enforcement process.

It is our view that the FSA should name and shame firms that may be in breach of regulatory obligations. At present, though amended slightly in the 2010 Financial Services Act, section 391 of FSMA prevents disclosure of warning notices issued to firms. The issuing of a warning notice essentially marks the beginning of the disciplinary process against a firm, as few cases fail beyond this point. We firmly believe that a blanket prohibition on disclosure of such warning notices, which is the effect of s391 of FSMA, is

inappropriate, particularly when the period between the issuing of the warning notice and the final notice can be lengthy. This is particularly true of the bigger cases involving household names who can employ lawyers to ensure that the process is long and drawn out. In the meantime consumers remain vulnerable to poor treatment.

It is the Panel's view that consumers have the right to know about the alleged shortcomings of the firms with whom they deal at the earliest opportunity, so that they can protect themselves and be vigilant against unfair behaviour on the part of firms. Making this information public at an earlier point could also encourage firms to work with the FSA to achieve a speedy resolution to enforcement proceedings, in order to minimise reputational risk. Therefore the relevant legislation should be implemented to allow the FSA to name firms well ahead of the outcome of any enforcement action. This disclosure would be in the public interest and would support the FSA's consumer protection objective by giving consumers the information they need to protect themselves.

In practice this would amount to the FSA being given the power in certain circumstances to name firms at the commencement of the disciplinary process or when it issues a warning notice. It will be at a stage when the FSA considers that the firm does have a case to answer and is therefore broadly equivalent to the stage at which charges are brought in criminal and civil cases. It would have the added effect of speeding up the whole process.

The Panel tabled an amendment to the Financial Services Bill to this effect earlier this year. This would have enabled the FSA to be more transparent, and place it as a world leader on the international stage on this front. The amendment to the Act which was eventually passed actually saw the FSA being given power to publish details at the stage of issuing a decision notice. This is most certainly a step in the right direction and speeds up the process for all concerned. However, as it marks the end of the FSA's process, and is the point at which the firm can appeal to the Tribunal, the Panel is concerned that many consumers will remain vulnerable to unfair treatment by firms for the duration of the enforcement process.

Responding to Freedom of Information requests – the introduction of the Freedom of Information Act (FOIA) has changed the basic assumptions about disclosure and the FSA's approach to freedom of information requests appears broadly in line with its overseas counterparts. However, we feel that the FSA should be particularly mindful to the Information Commissioner's guidance on when and what to publish (http://www.ico.gov.uk/upload/documents/library/freedom_of_information/detailed_specialist_guides/awareness_guidance_3_public_interest_test.pdf):

"It may sometimes be argued that information is too complicated for the applicant to understand or that disclosure might misinform the public because it is incomplete (for instance because the information consists of a policy recommendation that was not followed). Neither of these are good grounds for refusal of a request. If an authority fears that information

disclosed may be misleading, the solution is to give some explanation or to put the information into a proper context rather than to withhold it.”

Publication of firms’ compliance with the FSA’s financial promotion rules – the Panel has long been an advocate of a Register for financial promotions, which would give a clear indication of those adverts which fail to meet the FSA standards. Such a Register would help firms and their advertising agencies better understand the standards expected of financial promotions and so improve their quality and compliance levels, while facilitating competitive innovation in the advertising and promotion of retail financial services.

Advertising has to compete for consumers’ attention. In a situation where specific ads that fail to meet the necessary standard are not publicly held up as examples of poor practice there is a danger that companies will copy them thinking that they are acceptable. Given that the FSA applies a risk-based approach to the regulation of financial promotions clear examples become very important to defining the boundaries of acceptable practice and maintaining effective regulation. Without identifying specific advertisements there will be no concrete examples for advertising agencies to rely on when deciding what is acceptable, unlike the situation in other market sectors which are regulated by the Advertising Standards Authority (ASA). The ASA already regulates most other industries aside from financial services so the motivation to treat financial services firms differently is, in the Panel’s view, not justifiable.

Publication of governance procedures – as the Panel’s research indicated there is a good deal of scope for the FSA to be more transparent with regards to publishing governance information. The US is way ahead in terms of its regulators’ approach to this issue, with prior release of board agendas and non-confidential board papers and the holding of open board/ commission meetings being commonplace. A good starting point for the FSA in this regard would be a prior release of Board agendas and a release of more extensive minutes of those meetings.

In summary the Panel’s research acknowledges how comparatively willing the FSA appears to be to use transparency as a regulatory tool. Nevertheless outlined above are areas where the Panel feels the FSA could provide more information to the benefit of consumers and firms alike. After all the proper basis for withholding information should be that disclosure would unjustifiably harm the business interests of firms or unjustifiably impede the regulatory functions of the authority. It should not take account of the fact that businesses might be uncomfortable with the prospect of disclosure, if no identifiable harm to them will occur.

To see the full version of the report:

http://www.fs-cp.org.uk/publications/pdf/fscp_transparency.pdf