FSA Annual Public Meeting – 3 July 2012 – Adam Phillips

Thank you chairman.

This year the Panel's work has continued to be dominated by the transition to the new twin peaks structure, the public debate about the role of regulation and the UK's relationship with the European Union. Unfortunately the behaviour of the banks, in particular, has tended to focus attention more on treating the symptoms rather than the causes. The problems revealed over the last couple of weeks have once again highlighted underlying weaknesses in the business models of banks and in the character and culture of their senior management.

In this environment, the Panel has continued to concentrate on its role of advising the FSA on policy, while trying to ensure that the new architecture will be able to deliver a better outcome for people living in the UK than the present one has to date. I have consciously referred to people rather than consumers, because I think a large section of the retail side of the financial sector has focused for far too long on selling products to consumers, rather than helping people to make financial transactions safely and efficiently, borrow money on reasonable terms, save for the future and protect themselves against unexpected events.

The FSA has been being slow to act to stop mis-selling, to expose and publicise bad behaviour and to discourage the industry from launching products which are poor value. The Panel has allocated significant resource this year to identifying and promoting changes to the new Financial Services Bill which will help the new regulators be more effective than the FSA. Two key elements for which we are lobbying are enabling the FCA to strengthen rules to ensure the industry has a duty of care towards its customers and allowing it to publish information about the behaviour of organisations and individuals it regulates in order to inform consumers, without the threat of criminal prosecution to reveal this information. We believe that both of these are essential if the industry is ever to regain the public's trust.

I set out the Consumer Panel's expectations for the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA)in a speech to the British Bankers' Association (BBA) in January.[1] We are looking forward to the FCA becoming an effective regulator, which is something the FSA has found difficult. To be fair, the FSA has made a serious attempt over the past two years to engage with outcome-focused regulation in the retail market, but the financial crisis has not made that easy. The conduct-focused role of the FCA gives it a better chance of meeting that aspiration, but to be effective it will have to be clearer than the FSA has been about what it expects and more determined to achieve what it sets out to do. This means:

Firstly, carrying out better economic and research analysis, looking at root causes rather than symptoms, and having sufficient resources to engage effectively with the PRA and Financial Policy Committee on behalf of the consumer;

Secondly, if necessary conducting a well thought out debate with the industry and consumers about what it is aiming to achieve and the consequences of regulatory intervention;

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[1] The Financial Conduct Authority – *A Keynote Briefing* – BBA 25 January 2012

Thirdly, less focus on process and the application of rules than the FSA and more focus on the intended outcomes and the extent to which they are not being achieved;

Fourthly, taking actions that encourage good behaviour by the industry and rebuild consumer confidence – in our view this requires early intervention and regulatory transparency including publicising regulatory action such as warnings and Own Initiative Variations of Permission (OIVoPs);

Firthly, effective working relations with Europe representing the interests of both the citizen and the industry, something which the FSA has done very well; and

Finally, more effective and well-publicised enforcement which includes holding managers in Significant Influence Functions (SIF's) to account.

If the FCA can do this there is a good chance that it will be able to deliver better treatment of people. However, a regulator cannot **force** people or organisations to behave better. What it should do is create an environment that rewards good behaviour, make clear statements about its intentions, allow reasonable time for organisations to adapt and punish those who fail to meet its requirements. The rest will be up to the industry. The events of the last two weeks are not encouraging, but I remain hopeful that they will act as a catalyst to stimulate real change.

If I look back over the last year, The Mortgage Market Review has been a major policy initiative by the FSA. It has provided a helpful proving ground for some of the opportunities and problems that the new regulatory structure will create. The Panel is pleased that the FSA responded positively to its concerns about the overly-prescriptive nature of the original 2010 proposals and the need for a robust cost-benefit and impact analysis. We welcome the majority of the proposals in the recent consultation and believe that they should improve consumer protection. We remain concerned about the predicament facing so called 'mortgage prisoners' – those with interest only mortgages and those trapped on the standard variable rate because they are unable to meet the affordability criteria – and have urged the FSA to act quickly to mitigate this situation. We also hope that the lessons learned in this process will be considered by the Financial Policy Committee when developing its strategy for dealing with asset bubbles.

A particular aspect of the mortgage market is that conduct regulation has important prudential elements. In the present structure, where both conduct and prudential issues are regulated by the FSA, the Panel was able to contribute to the discussion of issues that relate to the potential interaction of conduct rules and prudential controls. This will be more difficult in the future where the Consumer Panel will have no statutory relationship with the PRA. We are continuing to argue that the lack of a statutory role for the Panel which enables it to question the actions of the PRA and require answers, in the way that is currently possible with the FSA, is a major weakness in the new Bill. We still hope the Government will recognise this.

The other major policy initiative by the FSA has been the Retail Distribution Review (RDR). This is finally close to becoming a reality. The Panel published a significant research project last year aimed at understanding how to ensure that the principles of the RDR could be incorporated in the platforms market. This is a market which has the potential to manage assets of more than £1 trillion. Its efficiency therefore significantly influences the cost of asset management for retail investors. The Panel was the only consumer group to respond to the consultation. We are very pleased that the debate stimulated by this research has led the FSA to introduce proposals which we hope will lead to a more transparent market delivering better value for investors.

The Panel has also focused attention on the ‘advice gap’ this year. The need for financial advice and education is growing as people are required to take more responsibility for their long-term financial health. Patterns of employment are changing and employers and the state are providing less financial security. The Panel has commissioned two significant research projects this year looking at ‘straightforward outcome’ products and the advice market, clarifying where the gap might really lie and identifying underlying causes and potential solutions. We are pleased that both the government and industry are now directing more attention at this area and we are involved in the various projects that are developing solutions.

We have been convinced for some time that it is essential that consumer credit is regulated by the same organisation that regulates deposit taking. It is a nonsense that that the FSA regulates the notification of an unauthorised overdraft and the grounds on which payments may be bounced but not the overdraft itself. That is regulated by the Office of Fair Trading. In the circumstances, it's not surprising that some banks have been able to profit from the resulting confusion. We are therefore pleased that the government is proposing to transfer the regulation of credit to the FCA. We have published a position paper and two reports on the issues that need to be taken into account to ensure that consumer protections are maintained and hopefully enhanced in the transfer.

Since the crisis, the European Union has become central to UK regulation. Most prudential rules are now set by Europe and subject to maximum harmonisation. Financial conduct regulation is rapidly moving in the same direction. Two years ago the Panel regarded a sub-group that met bi-monthly and a part-time policy officer as sufficient to maintain an effective grip on what was happening in Europe. We now, this year, have had a working group meeting monthly and a full-time policy officer dedicated to Europe. Several Panel members are members of stakeholder groups for EIOPA[2] and ESMA[3] and we are partners of BEUC[4], the European consumer group. We believe that it is essential that the interests of consumers are effectively represented to EU institutions, given the very limited resources of consumer groups in most Member States.

In the coming year the Panel intends to continue its work advising the FSA on consumer issues, but to focus half its resource on four main strategic areas;

1. Consumer credit regulation, where it is essential that consumer protections are not lost in the proposed transfer from the OFT to the FCA;

[2] European Insurance and Occupational Pensions Authority
[3] European Securities and Markets Authority
[4] Bureau Européen des Unions de Consommateurs

2. General insurance, where price competition assisted by comparison websites is leading to the hollowing out of the protection offered by these policies and potentially a major loss of confidence in insurance;
3. Decumulation, where the impact of the closure of defined benefit pension schemes, falling annuity rates, Solvency 2, the cost of long term care and the problems of getting advice are creating major risks for the mass market ; and finally
4. The future effectiveness of the FCA as a conduct regulator, ensuring that customers are treated fairly and the industry provides good value products and services which meet customers' needs. This is the single most important priority for the Panel.

I would like to conclude by thanking my colleagues for their support and hard work. In particular, I would like to acknowledge the valuable contributions of David Metz and Caroline Gardner who both retired from the Panel in December. I would like to welcome Martin Wheatley and thank him for taking on a very difficult but hugely important job. I would also like to echo the comments to pay tribute to Hector Sants and his role in leading the transformation of the FSA into the FCA. His experience will be missed in the new structure and the Panel would like to wish him well for the future.

Thank you.