UK Shareholders' Association
UKSA, 1 Bromley Lane, Chislehurst, BR7 6LH
Phone: 01689 856691
Email: officeatuksa@gmail.com
Web: www.uksa.org.uk

ShareSoc
UK Individual Shareholders
Suite 34, 5 Liberty Square, Kings Hill,
West Malling, ME19 4AU
Phone: 0333-200-1595 Email:
info@sharesoc.org
Web: www.sharesoc.org

Consultation Response: FCA Approach to Consumers

A joint submission on behalf of Private Investors from ShareSoc and UKSA

UKSA and ShareSoc are pleased to make this joint response on behalf of individual investors, who collectively account for 12% of the UK stockmarket, or 30% if you include their beneficially owned investments via funds, pensions, ISAs, etc.

This is an important consultation. This is an important moment in UK as political pressure is growing to address the problems of the financial services industry. Much progress has been made since 2008 and we recognise this. However much more needs to be done.

In this response we review the FCA objectives, its role, evidence of market failure and comment on the structure of the consultation and then give specific responses to the consultation questions.

Parliament has given the FCA a single strategic objective – to ensure that relevant markets function well – and three operational objectives to advance: to secure appropriate protection for consumers; to protect and enhance the integrity of the UK financial system; and to promote effective competition in consumers' interests.

As the UK's financial services conduct regulator, it is the FCA's role to supervise the conduct of around 56,000 firms supplying financial products and services that help drive the UK economy. Individually and collectively, their actions have an impact on the approximately 65 million people[4] currently living in the UK. With over two million people employed in financial services in the UK, the financial sector is a leading UK industry.

However, the FCA quotes evidence that the markets are not working properly:

"For example, as of August 2017, 37 banks offered 189 different current accounts, with an average of 9 different accounts per provider.[26] Some consumers do not believe there is a difference between these providers. Of the 1.9 million consumers with a day-to-day (normally current) account held for more than 3 years who have never switched account provider, one in seven (15%) cite this lack of difference between providers as a reason not to switch.[27] We see a similar picture in the savings and general insurance markets, with this reason being one of the top three given for not switching for home insurance, cash ISAs and savings accounts."

In well-functioning, competitive markets, firms compete to win business on a range of factors, including quality and service. This in turn drives effective choice and lower prices. The FCA says "We will discuss the potential barriers to this, and how we propose to address them in our Approach to Competition, which is due to be published in due course. "

UKSA and ShareSoc interest is principally in investing, investments and investment and savings products.

This consultation fails to size the market or the relative importance of the different sectors, which one might segment as follows, for example:

1. Banking
2. Mortgages
3. Bank loans and other loans (other than property mortgages)
4. Insurance
5. Savings
6. Pensions
7. Investments
8. Products sold by the financial services industry
9. Platforms.

We find that the 6 questions raised are very generic. Answers would be different for different sectors and for the different types of customer (we explain our categorization of able customers, disadvantaged consumers and incapable consumers below. There are of course other categorisations that could be used.)

With respect to transparency, we welcomed and were pleased that the FCA appointed Chris Sier to chair its working group on disclosure of costs and charges for institutional investors and look forward to seeing his report which we understand will be published imminently. Transparent disclosure of costs and charges is essential information for consumers.

Our answers to your specific questions are below.

Q.1 FSMA requires us to take into account the eight principles of good regulation. One of these is the general principle that consumers should take responsibility for their decisions. While having regard to the general principle that consumers should take responsibility for their decisions, do you agree that there are circumstances where consumers cannot be expected to take responsibility? What do you think these circumstances are? How could – and should – the FCA intervene in these cases?

The ability of consumers to 'take responsibility for their decisions' depends on their level of knowledge and their capacity to use that knowledge. We cannot expect consumers to take responsibility if

1) they are incapable of the necessary learning. We call these 'incapable consumers', or
2) they do not have access to the tools for necessary learning. We call those who are capable but without access to necessary tools 'disadvantaged consumers'

We call those who fall into neither category 'able consumers'. Only 'able consumers' can be expected to take responsibility for their decisions. It is the responsibility of Government, having established the principle of consumer responsibility through the FSMA, to support processes that enable *all* consumers to take that responsibility.

We require people to have a driving licence before they are allowed to drive unsupervised. Learners are allowed to drive only when supervised. The FCA might consider a certificate/certificates of competence prior to any consumer being allowed to purchase a specific financial services product(s). This could be part of the national curriculum which might restrict consumers to only purchasing products if they had passed O level, A Level or degree level knowledge.

The aspiration of any drive to increase the effectiveness of consumer financial decision-making must be to reduce the number of incapable consumers, reduce the number of disadvantaged consumers and turn all into able consumers. The building blocks for doing so are:

1) Process
2) Regulation
3) Tools
4) Education

It is unfair to criticise a document for not doing a task it did not set itself, but we suggest that any proposal to deal with part of the problem has little meaning unless embedded in a holistic set of proposals. The FCA's thinking appears to have been limited by its formal objectives, and possibly by a concern not to cross departmental boundaries or upset political factions. We appreciate also that there are budgetary issues. But the final sentence in this question, 'How could – and should – the FCA intervene in these cases?' reflects an extraordinarily limited approach to solutions.

We suggest that the FCA's thinking is excessively constrained by its obsession with the advice industry. This causes it to limit its ideas on 'process' to one where consumers seek regulated advice before buying financial products. It also limits its ideas on 'tools' to the provision of regulated financial advice. There are much better and cheaper ways of going about both these things.

We mention some things under the above heading and therefore missing from the FCA's document:

1) Education. Actually astonishing there is no mention. Fundamental to any long-term solution
2) Money Advice Service. Lost its way. A big subject outside scope of this consultation but:
    a. Bring in independent outsiders, including real investors, educators, behavioural specialists, communicators,
    b. eliminate industry capture, (see Q4 below for relevance)
    c. Give MAS clear objectives (not just *enhance* financial understanding and capabilities, etc etc - see MAS/FCA/HMT framework doc 26/3/2013 - the non-action-oriented word 'framework' is a giveaway)
    d. Clarify its governance. Note the three fingers in the pie of its 'framework'. The Chairman and four of the six non-exec directors have City connections
3) Use of internet
    a. FCA-sponsored modules to establish individual consumer capability, must be accessible to all IFAs and applied to all potential clients
    b. FCA-sponsored training modules linked to the results of a) above
4) Break the advice monopoly
    a. Empower pension funds
    b. Empower companies
    c. Empower a few independent organisations
    d. Distinguish between robot-advice and face-to-face – the former much easier to review, the latter requiring individual skills and integrity

We applaud the new enthusiasm for behavioural factors and for using the specialist skills of other organisations (does this mean this has not happened in the past – disgraceful if true?). The new FCA has shown that it is willing (and probably able) to take a broader view. In coming to a conclusion on how it is to meet its objectives we hope it takes on the responsibility of advising government on what else needs to happen, outside its remit, so that government can fulfil its implied responsibility for consumer capability. Who else is going to do it?

Q2: It is not always easy to identify which consumers are vulnerable at any point in time. But these consumers may face a higher risk of harm, and may suffer more severe harm as a result. Do you agree that firms have a responsibility to take reasonable steps to identify the signs of vulnerability, and to have processes in place to take appropriate action where they have identified a consumer with a particular need and at a particular risk of harm?

Yes of course (we assume that 'firms' here means financial advisers). They are the first point of contact, who else is going to do it?

Q3: In a number of areas, for example financial exclusion, there are aspects that sit directly within the FCA's remit, but others that are part of a broader social policy debate and therefore in the domain of other parties, including Government. Which consumer issues do you think sit directly within the FCA's remit, and which are more a matter for Government? Are we right to commit our resources to working with other organisations, such as firms, other regulators, government, courts, consumer groups etc., where improved consumer outcomes may require action that is not within the FCA's regulatory toolkit?

Yes of course, you must do that. Our opening Q1 answer explains why to do otherwise is simply erecting an artificial barrier to fixing the problem.

Q4: In this approach document we set out our vision of 'well-functioning markets that benefit everyone.' Do you agree with the aspirational vision and outcomes that we explore? Are there any further barriers or risks to us achieving it?

We agree with your 'aspirational vision and outcomes', though they are not clearly expressed in a single vision statement.

Yes, there are barriers, serious ones that have until now bedevilled your efforts at consumer protection, and it's best to be honest about what they are. Starting with a disclaimer, we all know that the great majority of firms in the financial services industry (including the financial advice industry) are socially conscious, keen to benefit society as a whole and staffed by individuals with the same qualities. But, as with all groupings there are a few bad apples (if not there would be no need of regulation). So it is important to recognise the financial pressures on the industry, and to recognise also that these make it hard for the good players to maintain their ethical standards.

William Bernstein, the American neurologist, part-time fund manager and writer on investment matters ('The Intelligent Asset Allocator', 'The Four Pillars of Investing') has published a 20-page investment guide for millennials (‘If You Can: how millennials can get rich slowly’) that is built round five obstructions to good personal investment habits. The last is: ‘The financial services industry wants to make you poor and stupid’. The fact that there are so many good people and firms in the industry fighting to contradict this brutal statement does not invalidate its underlying truth in terms of economic pressures.

And the reasons are not difficult to find: ‘Stupid’, because clever well-informed people do not need advice nor will they buy most of the industry’s products. ‘Poor’, because the industry does not create original wealth but is a service industry that stands between the wealth creation of enterprise and the sharing of that wealth by stakeholders. To that extent it’s a zero-sum game and the more that goes to the industry, the less to stakeholders.

This is the ultimate barrier. It makes the phrase ‘well-functioning markets that benefit everyone’ an oxymoron. See also ‘Responsible Investing’ on UKSA’s website.

Q5: We have described our approach and detailed some of the data we have used (notably our Financial Lives Survey 2017) to identify how far our vision is from consumers experiences across a range of retail products or sectors. What further metrics would you use? Are there any specific data sources or tools that may be of benefit?

No need for more metrics. The enormously impressive and comprehensive survey probably didn’t tell you anything you didn’t know but gives you the intellectual backing to do what needs to be done.

Q6: In the final section we set out our framework explaining how we will work, including how we intend to prioritise consumer issues, select interventions and design remedies. Do you agree with this framework? Would you like us to consider any additional or alternative factors in how we regulate: a. for all consumers b. for the most vulnerable or excluded, and c. to meet the challenges of the future?

This final section contains a number of interesting and sensible operational plans, but In general the framework is too un-focussed and repetitive to meet its grander intentions (witness the occasional use of the words ‘vision’ and ‘strategy’) and does not face up to the inherent conflicts identified earlier.

A) The title of the section, ‘Our vision of a well-functioning market, and how we will work to achieve it’ implies that consumer protection is achieved by a ‘well-functioning market’, presumably the market for financial products and services. This is untrue: in fact the most favourable outcome for consumers is that all are able to make their own decisions, both on asset allocation and on direct investments in asset types of their choice, without the intervention of expensive intermediaries. If that Nirvana (impossible, of course) was achieved there would be no demand for products and services and therefore no market.

Nevertheless, in the real world, any statement or objective about consumer choice must acknowledge the primacy of direct investments. The section headed ‘Our vision for a well-functioning market that works for consumers’ should be anchored with the statement:

‘Consumers will have either the knowledge or the access to advice to enable them to chose between different direct investments and savings products’.

…. and the four statements on page 33 should be modified accordingly

B) We understand the emphasis given in the document to vulnerable consumers but caution against the implication in the framing of this question that there are two classes – vulnerable and non-vulnerable – to be supported by two different regimes. The key is that we are all different. The problem is one of designing a regime that adapts to these differences and it is not helpful to suggest that separating individuals into two boxes could be a practical solution.

C) The sub-section 'Designing remedies around real behaviour' includes an important statement that we would challenge. 'Our extensive testing has shown greater disclosure often leads to only marginal changes in behaviour'. This looks like an excuse to let the industry off the hook in the realm of transparency. We regard as suspicious the absence from the document of 'Transparency' as a theme (playing to the desire of the industry to maintain information asymmetry).

We suggest that full disclosure only has marginal effect when the recipients do not have the education to understand the disclosure. This is no reason to conceal information from those that do. Transparency as a principle is fundamental to market efficiency and we would like greater emphasis (or greater justification) in the final document. The comment is also rather contrary to the section that follows: 'Full disclosure: communicating effectively'.

We would be pleased to meet to discuss our comments with you.

John Hunter
Chairman
U K Shareholders' Association

Cliff Weight
Director
UK Individual Shareholders' Society

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