



The Money Charity Response - HMT Financial Services Future Regulatory Framework Review (Phase 2) (February 2021)

The Money Charity is a financial capability charity whose vision is to empower people across the UK to build the skills, knowledge, attitudes and behaviours to make the most of their money throughout their lives, helping them achieve their goals and live a happier, more positive life as a result.¹

We welcome the opportunity to respond to HMT's Financial Services Future Regulatory Framework Review (Phase 2).

In this response, we set out our Key Points, make some overall comments on the issue then answer the questions posed in the Consultation Paper.

¹ See box on back page.

Key Points

1. Overall we support the proposed framework, with its emphasis on parliamentary setting and review of the policy objectives for financial services regulation, with detailed regulation delegated to expert regulators such as the FCA.
2. We recommend that Financial Inclusion, Financial Resilience and Wellbeing and Financial Capability be explicitly part of the policy framework for financial regulation, alongside enhanced provisions for consumer protection.
3. We wish to see a formal Duty of Care towards consumers introduced as part of the general regulatory principles for financial services.
4. We would like to see a provision enabling regulators to act when behaviour particularly damaging to financial service consumers occurs outside the normal regulatory perimeter.
5. We are not convinced by the argument for adding a “competitiveness” objective.
6. We support stakeholder consultation along the lines of the FCA Consumer Network, but think the statutory panels need review in terms of the visibility of their work (including how their work is received by the regulator) and clarifying the link between panel members and the constituency they represent.
7. Legislation should make clear that any early involvement of HMT ministers in the detail of FS regulation should (i) be evidence-based and (ii) be for the specific purpose of ensuring consistency with established broader policy goals of government.

Overall Comments: financial capability, financial wellbeing and the need for supportive financial services regulation

As a financial capability and wellbeing charity (see box on back page), an important part of our remit is to promote policies and regulations that contribute to enhanced financial capability, resilience and consumer wellbeing. There are many aspects to this, but two that stand out are:

(a) Clarity of information and understanding.

Consumers need to be able to understand clearly the nature of the products they are buying and the terms associated with these products. Surveys² show that the UK's

² For example, see Money and Pensions Service surveys of financial capability in the UK.

average level of financial capability is quite low, financial education in schools is patchy and often non-existent and many UK consumers do not understand things such as compound interest and the effects of inflation on borrowing and spending. Present bias and shortage of money leads too many people into financial commitments they later cannot service. Some firms take advantage of human weaknesses by lending when people are vulnerable, using over-complex or inconsistent language to describe their products and/or advertising in misleading and alluring ways. The FCA has cracked down on some of this behaviour but it is a work in progress rather than a solved problem.

(b) Supportive regulation.

In our view, **financial products and services should be designed to help consumers behave in financially capable ways**, rather than the opposite. We know from many fields of human activity that design matters: people tend to go where the crowd goes and the crowd goes where it is channeled to go. On the one hand, mortgages are a near-universal financial product which is highly regulated: care is taken to make sure that mortgage payments are affordable, interest rates not too high, lending behaviour responsible and mortgage companies solvent and robust to economic adversity. The UK knows from experience that an unregulated housing market can be disastrous for the economy, so has taken steps to moderate its extremes.

On the other hand, products or services such as mini-bonds, Bitcoin/Dogecoin or social media-driven investment platforms operate in what could be called the Wild West of financial services, luring unsophisticated investors into extreme positions and causing large-scale consumer harm alongside profits for the lucky or unscrupulous few. In the area of high-cost debt, the FCA has needed to intervene continuously and still new products emerge that escape existing regulation, such as the latest generation of buy-now-pay-later loans.³

As a financial capability charity, our core business involves delivering financial education to school pupils, students, employees, self-employed and community groups such as refugees, social housing tenants and ex-offenders. We teach the basics of budgeting and spending, managing different types of credit and how people relate to money emotionally and psychologically (which is where problems often arise). We try to teach what HMT would recognise as sensible approaches to money, credit and spending. However, educational workshops cannot offset the pressures arising from adverse product design and weak regulation. Along with others working in this space, we need help from Parliament, HMT and the regulators to make sure that financial

³ At the time of writing, the FCA has announced, in response to the Woolard Review, that it will be regulating the latest iteration of BNPL.

services lean in the same direction we do, towards responsible and sensible financial management, and not towards excessive debt, loose budgets and personal insolvency.

In this sense, we welcome the current regulatory review, with its emphasis on parliament setting policy and regulatory targets for each financial services sector. We hope that Government and Parliament fully take this opportunity to put in place a framework that helps improve the financial capability, wellbeing and inclusion of all people in the UK.

We understand from HMT/FCA forum we attended on 1 February 2021 that HMT is interested in hearing specific and detailed suggestions on financial service policy solutions, so we take the opportunity to make specific recommendations.

Answers to consultation questions

Chapter 2 questions 1-5 on the proposed framework (page 25 of the consultation document)

1. How do you view the operation of the FSMA model over the last 20 years?

See Overall Comments above.

2. What is your view of the proposed post-EU framework blueprint for adapting the FSMA model?

Overall, we agree with the model proposed, particularly with its emphasis on a clearer statement by parliament of the policy objectives of regulation (purpose, scope, core elements and activity-specific regulatory principles). This will make it clear to the regulators what they are supposed to achieve in more specific ways than is currently the case with the high-level objectives of the Financial Services and Markets Act.

New policy wording can both draw on the experience of recent mistakes⁴ and be prospective: it can look forward to ways in which we as a country wish to improve consumer resilience and wellbeing in the future, as part of the “levelling up” agenda. We would like to see policy guiding regulators under the following headings:

Financial inclusion

We are one of the signatories of the recent letter (Friday 5 Feb 2021) to John Glen, Economic Secretary to the Treasury, from a group of charities and consumer groups led by Fair by Design, calling for a financial inclusion duty to be included in the FS regulatory framework. Our joint letter calls for a duty in the following terms:

⁴ For example, those described in the Gloster Report into the collapse of London Capital and Finance, which found multiple and puzzling supervisory failings at the FCA.

“As part of the Financial Services Future Regulatory Framework Review, we urge you to ensure the FCA has either a duty or cross-cutting ‘must have regard’ to financial inclusion.”

This letter refers specifically to the FCA, but the duty should apply to all financial services regulators. For example, inclusion is relevant to the Payment Systems Regulator and to prudential bodies such as the Bank of England that have far-reaching powers over the financial system.

Why is inclusion important? While most UK residents have reasonable access to financial services, there are some (still a large number in absolute terms) who are excluded due to complex social factors. For example:

- Around one million people remain unbanked.
- Around two million people operate exclusively in cash.
- Around one million do not have Internet access.
- The poverty premium has recently been estimated to average £478 per low-income household per year.
- Around 11 million people either choose not to use credit or do not have access to credit.
- 4.8 million people are living without access to at least one essential household appliance (fridge, freezer, cooker or washing machine).⁵

The final bullet point shows concretely what it means to be on a low income and not have access to credit: it affects people’s access to necessities, not just things it might be nice to have.

In our financial capability work we regularly come across people who are affected by one or more of the above aspects of financial exclusion. Clearly exclusion is a bad thing and what may start as financial exclusion flows across into other areas of life. For example, lack of access to the Internet and sufficient digital devices was a significant cause of homeschooling difficulties during the Covid-19 lockdowns.

Two important financial inclusion issues are access to cash and access to bank branches. HMT is fully aware of these. They illustrate how financial services policy must at the very least “have regard to” financial inclusion. Preferably, financial inclusion should be a positive duty for financial service regulation. This would harmonise financial services regulation with other aspects of Government policy and enable Government to operate in a more joined-up way.

⁵ The Money Charity, *The Money Statistics January 2021*, page 17.

Financial resilience and wellbeing

Resilience and wellbeing are rapidly growing subjects in research and policy. It is increasingly recognised that traditional measures of performance such as GDP and company profits, important though they are, do not capture the ultimate purpose of economic activity, which is to improve human wellbeing within a sustainable natural environment. The distribution of wellbeing is also important. The “levelling up agenda” recognises that if some parts of the country or social groups prosper while others fall behind, this ultimately is damaging to the national interest.

Many studies of wellbeing have been undertaken, including the recent FCA analysis of wellbeing in relation to debt.⁶ A few years ago the charity Age UK conducted a detailed statistical study of the wellbeing of older people in the UK and found that financial wellbeing was one of the five key wellbeing domains.⁷ In our work in financial capability education we focus particularly on financial wellbeing and we have found demand for our financial wellbeing workshops (now delivered online) surging in the aftermath of Covid-19.

The HMT review of financial services regulation presents an opportunity to formalise the promotion of financial wellbeing as a duty of the UK’s financial services regulatory framework. This is a high-level objective, applicable to regulation of the whole sector. We suggest a duty along the following lines:

“The ultimate reason for financial services and the purpose of financial services regulation is to improve human wellbeing within a sustainable natural environment. In carrying out their statutory duties, regulators should develop the tools to identify and measure the effects of the regulations they apply on wellbeing, and design regulations to maximise human wellbeing within a sustainable natural environment.”

Such a provision would be helpful to us and others working in the financial capability/wellbeing space. It would also link financial services regulation more clearly with other aspects of public policy such as health, education, the environment and economic development. If all aspects of public policy and private and charitable sector activity are leaning in the same direction, the chances of achieving positive outcomes will be enhanced.

⁶ Garforth-Bles et al 2020, *The Wellbeing Effects of Debt and Debt-related Factors*, FCA and Simetrica.

⁷ Available at: <https://www.ageuk.org.uk/our-impact/policy-research/wellbeing-research/index-of-wellbeing/>

Financial capability

As a specialist financial capability education charity, we would like to see an explicit link made between financial regulation and financial capability along the lines set out in our Overall Comments at the beginning of this response. Specifically, that for each consumer-facing sub-sector of financial services there should be a policy goal to promote financial capability by:

(a) Ensuring that information about financial services and products is presented to consumers in clear, understandable, fair and balanced ways, so that consumers understand what they are buying and the accompanying risks and costs.

(b) Ensuring that financial services, products and marketing assist consumers to behave in financially capable ways (rather than the opposite). The grain of financial service offers should lead towards good budgeting, saving and spending decisions, and away from unmanageable debt, high financial stress and personal insolvency.

It is important that an evidence-based approach is taken to both these aspects, i.e. that firms and regulators carry out consumer research to test whether (a) people actually understand the products being promoted to them, and (b) whether product design actually assists people behave in financially capable ways.

3. Do you have views on whether and how the existing general regulatory principles in FSMA should be updated?

While there is an existing requirement in the FSMA to promote consumer protection, the current wording in Section 1 of the FSMA is ambiguous, giving little indication of what “an appropriate level” of consumer protection might be. The current review, in our view, creates an opportunity for parliament to be much clearer about what type of consumer protection it wishes to see. There are two amendments we would like to see:

Duty of Care

For some years, consumer organisations and parliamentary bodies⁸ have been calling for financial service firms to be subject to a formal Duty of Care toward their consumers. Under pressure from Parliament the FCA initiated discussion of the issue, which has now been subsumed into a general discussion of the FCA Principles. We are currently awaiting the FCA’s latest discussion paper, which has been delayed because of the Covid-19 pandemic.

⁸ For example, the Financial Inclusion Commission and the Treasury Select Committee.

In our responses to the FCA and in our October 2019 response to the first phase of HMT's regulatory review we supported the call for a Duty of Care. In our October 2019 response to HMT⁹ we summarised recent examples of poor corporate behaviour and how the FCA had been forced to step in. Since then, further examples have continued to occur. For example, the Gloster Review has given a vivid description of how poorly some financial service firms (hopefully a minority) behave.

In our view, a Duty of Care for financial services should follow established legal lines. There are two forms, arising historically from the Law of Tort and from fiduciary law. The first is well established in consumer protection and takes the form of:

“A duty of care to avoid reasonably foreseeable harm to the consumer.”

“Avoiding reasonably foreseeable harm” is the test devised by the Courts to give expression to how a firm should think about consumer protection. It derives from the celebrated case of *Donoghue v Stevenson* (1932), the “snail in the bottle” case. This is an appropriate analogy for financial services, because for many consumers the product being sold to them is contained in a “dark bottle”. There is information asymmetry which means the consumer must trust the provider to be selling them something that is safe and beneficial.

The second form of Duty of Care is the fiduciary one, which already exists in UK insurance law:

“A firm must act honestly, fairly and professionally in accordance with the best interests of its customer.”¹⁰

In our view, a combination of these two forms of the Duty of Care would provide the basis for an appropriate level of protection for consumers. The advantage of working with existing law is that the Courts have already established the meaning of the terms and we do not have to try to “invent a new wheel”.

We understand there is opposition from within the industry to such a Duty of Care on the grounds that it might lay firms open to legal action. From our point of view, this is exactly the advantage. The possibility of regulatory action under a Duty of Care and/or a class action by consumers would force the legal and risk advisers of FS companies to flag up to senior management the business risk of product design or firm behaviour that might give rise to legal action. By internalising this assessment in the decision process there is a chance we can reduce the amount of poor behaviour in the marketplace and improve consumer outcomes.

⁹ Available at: <https://themoneycharity.org.uk/media/The-Money-Charity-Response-HMT-Review-of-Financial-Regulation-Oct-19.pdf>

¹⁰ Insurance Conduct of Business Sourcebook (ICOBS) 2.5.

The industry would benefit from this as it would improve the industry's reputation over time.

A catch-all perimeter principle for consumer financial services

We understand in a practical sense why there is a perimeter for financial services regulation (e.g. the "FCA perimeter") but it seems to us that perimeter issues have arisen frequently and in ways that are controversial and damaging to consumers.

We therefore feel that better solutions are needed for demarcating the perimeter and for dealing with serious problems with consumer financial services that straddle or fall outside the perimeter. The Gloster review has given vivid evidence of how weaknesses in the perimeter can give rise to consumer harm and the FCA itself flags up perimeter issues on a regular basis, including in its annual perimeter report. In our view, it is unhelpful to have regulated firms selling unregulated products or for hot consumer investment products such as Bitcoin/Dogecoin to lie outside the perimeter. At the time of writing, we have just experienced the GameStop frenzy, an unseemly zero-sum, mutually predatory fight over fundamentally low-value assets among hedge funds, banks and retail investors. Some people, presumably including retail investors, have lost large amounts of money, with (in the case of some of retail investors) little understanding of the game they were involved in.

We think there needs to be some sort of catch-all provision that would allow financial service regulators to step in when they see serious consumer detriment occurring in financial services lying outside the perimeter. We do not have the legal resources to provide a clear formulation of this provision, but we would like to see HMT and regulators apply their resources to designing an appropriate provision.

The provision would need to contain a definition of "retail financial service or product" and a definition of "serious consumer detriment" to guide when intervention would be justified. We think it is in the public interest that regulators have a broad duty to prevent, as far as they can, any action towards consumers that is deliberately predatory or damaging, or that obviously – by omission or negligence - could lead to consumer harm.

We are not saying that all risk in financial markets can be removed, but there is a difference between normal risk taken on in knowledge of what the risks are (for example, that share prices can fluctuate around true values) and risks that arise from behaviour that is predatory or negligently damaging and may be invisible to, or deliberately hidden from consumers.

4. Do you have views on whether the existing statutory objectives for the regulators should be changed or added to?

We are not convinced by the argument for adding a “competitiveness” objective to the FSMA. There are two ways of thinking about competitiveness. One is the positive approach, which is around innovation, improved design and better consumer service, which is generally good for both companies and consumers. But there is a second approach, which is the “race to the bottom” approach, which relies on reducing regulation and redistributing income to shareholders and executives at the expense of consumers and employees. We hope that those advocating the “competitiveness” objective mean the former, but there is a risk they might mean the latter.

We are not clear what adding a “competitiveness” objective would gain. For financial services delivered in the UK, all firms (domestic and foreign) must follow the same rules, so there is no competitiveness advantage. For UK-based firms delivering financial services overseas, they must comply with the rules in the markets they are supplying. So, there is no gain either way.

Innovation we think is already well covered in the UK’s financial services legislation, so we do not see any advantage in adding an explicit “competitiveness” objective.

Chapter 3 Questions 6-9 Accountability, scrutiny and stakeholder participation.

Four points from us here:

Parliament to set FS regulatory policy

We like the overall approach of giving Parliament the power to set financial services regulatory policy and to scrutinise it via the select committee process. Sometimes there is political point-scoring at select committees, but where members develop expertise and forensically question regulators the scrutiny process can, and we believe has, raised the bar for performance. Select committee proceedings on matters of public concern receive considerable media coverage and this gives the public a means to be informed and to interact with the process.

Consumer networks established by regulators

Where regulators establish stakeholder networks, these can be effective. We would particularly like to praise the FCA’s Consumer Insight team, which organises regular Consumer Network meetings with charities and consumer groups working on financial service issues. We have been a member of this Network for some years. The Consumer Insight team keeps us up to date with FCA regulation, consultations and decisions and calls ad hoc meetings on issues such as the Woolard Review. These are two-way meetings in which the FCA team updates us, but also gives opportunity for us to describe our experiences and views. One advantage of the Consumer Network is that members attend as representatives of their organisations, so there is a formal link to a

set of wider constituencies. The Network is attended from time to time by the CEO and by the Chairman of the FCA, so there is some direct interaction with the highest level of decision-making. Having said that, we are not absolutely sure how consumer representations are seen by the policy and regulatory divisions within the FCA and how consumer representations are weighed in comparison with other representations received from other interest groups. This is an area for future attention.

Statutory Panels

Regarding the statutory panels, we are less clear that in their current form they are working as well as they could. The panel we are most familiar with is the Financial Services Consumer Panel. While we have found the contributions of individual members of this panel helpful and well-informed when we have heard them speak at FCA and other events, we are less clear how the panel as a whole operates, how it is recruited and how it acts representatively for its constituency. Neither are we clear whether or how the panel is listened to by the regulator.

We suggest the operation of the statutory panels be reviewed with the goal of raising the visibility of the panels' work, *including how their work is received by the regulator*, and clarifying the link between panel members and the consumer constituency they are supposed to represent.

Early involvement of HMT ministers

On the question of the early involvement of HMT ministers in designing financial regulation (paragraphs 3.23 to 3.33 of the consultation document), we understand the rationale for this in terms of ensuring coordination with other areas of policy. However, involving ministers in the detail of regulation before anything has been made public to some extent contradicts the goal of regulatory independence and creates opportunities for idiosyncratic intervention. We therefore suggest that the provision for pre-public ministerial involvement be worded to make it clear that (i) it should be evidence-based and (ii) it should be for the specific purpose of ensuring consistency with established broader policy goals of government, including the policy goals set for financial services regulation.

The Money Charity is the UK's financial capability charity providing education, information, advice and guidance to all.

We believe that everyone achieves financial wellbeing by managing money well. We empower people across the UK to build the skills, knowledge, attitudes and behaviours to make the most of their money throughout their lives, helping them achieve their goals and live a happier, more positive life as a result.

We do this by developing and delivering products and services which provide education, information and advice on money matters for those in the workplace, in our communities, and in education, as well as through influencing and supporting others to promote financial capability and financial wellbeing through consultancy, policy, research and media work.

We have a 'can-do' attitude, finding solutions to meet the needs of our clients, partners, funders and stakeholders.

Tel: 020 7062 8933

hello@themoneycharity.org.uk

<https://themoneycharity.org.uk/>