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Date: 9 February 2022

Consultation Response

Which? Response to HM Treasury's consultation on Financial Services Future Regulatory Framework Review: Proposals for Reform

Which? welcomes the opportunity to respond to HM Treasury's consultation on Financial Services Future Regulatory Framework Review: Proposals for Reform.

It is right to periodically review the UK's regulatory framework to consider whether it remains appropriate in its current form and delivers a coherent, agile, and internationally-respected approach to financial services regulation that is right for the UK and consumers.. The main points from our response are:

- **We urge HM Treasury to reconsider its proposal to add new growth and international competitiveness secondary objectives for the PRA and FCA.** Our primary concern is that giving the regulators additional, potentially conflicting, objectives will have a negative impact on the protection and advancement of consumer interests. In particular, we consider this proposal is likely to complicate the FCA's decision-making process, dilute existing consumer protections and lead to a reduced willingness to advance new consumer protection measures. In addition, we do not think the positive case for this change has been made, or even that it is a role that regulators should perform. Past experience provides a stark warning about the negative consequences which can arise when regulators are tasked with promoting competitiveness, while others (e.g. HM Treasury itself and the City of London Lord Mayor, as well as the multitude of trade associations) are already tasked with this responsibility. In addition, we note that HMT can already make recommendations to the FCA about areas it should have regard to. Given these reasons, we consider that proceeding with this proposal has the potential to significantly undermine the FCA's ability to protect consumers and so we recommend that HM Treasury does not take it forward.
- **HM Treasury and regulators should not rely solely on formal consultations to gain input from consumer voices on regulatory proposals.** It is vital that there are opportunities for consumers and their representatives to engage with and scrutinise the development of regulatory proposals to help balance the input and lobbying from the well-resourced financial services industry. There is a strong case for Government and regulators to think more creatively about how best to gain views from this constituency, and not to rely solely on the views expressed in response to formal consultations.
- **We are particularly concerned that the consultation does not pay specific attention to the issue of direct redress for consumers.** We do not believe that relying solely on FCA and other regulators to enforce rules gives sufficient protection for consumers, especially given the growing prevalence of fraud and scams. We note that it is a recommended step in National Audit Office guidance on good practice in regulation

for policymakers to consider appropriate mechanisms for the public to seek redress in relation both to the actions of regulators and regulated entities¹. For example, the Government should consider strengthening the redress scheme provisions in section 404 Financial Services and Markets Act (FSMA) 2000, enacting an opt-out representative action procedure for consumers with financial services claims analogous to that in competition law, or further extend private rights of action and civil liability for breaches of FCA or other regulator rules.

- **We are mindful that there are many aspects of EU retained law on financial services matters of key importance to consumers, and where the benefits of having core rights and responsibilities set out in primary or secondary legislation clearly outweigh any perceived flexibilities of a ‘regulator rules based’ approach.** The areas of law covered include payment protections, mortgage loans, consumer credit, pensions and investment. In many cases, the existence of civil liability derived from rights in these areas will allow individuals to bring legal claims or take a complaint to the Financial Ombudsman Service if necessary. Moreover, there has already been a shift towards allowing further discretion of the FCA in some areas, such as the recent changes to the Packaged Retail and Insurance based Investment Products (PRIIPs) regulations concerning product information to be provided to consumers. This is a worrying trend without clear legislative safeguards and criteria being preserved.

ANSWERS TO QUESTIONS

1. Do you agree with the government’s approach to add new growth and international competitiveness secondary objectives for the PRA and the FCA?

No, we do not agree with the government’s proposal to add new growth and international competitiveness secondary objectives for the FCA, which is the principal financial services regulator we engage with. There are a number of reasons for this which, taken together, provide compelling grounds for resisting the addition of these secondary objectives:

- **Conflicting objectives will complicate the FCA’s decision-making process** - the FCA is already tasked with the strategic objective of making sure relevant markets function well, and also has three operational objectives (to protect consumers, protect financial markets and promote competition). We also believe that there are strong arguments for strengthening the current rules along the lines proposed by the FCA to put in place a new consumer duty. The current HMT consultation states that adding growth and competitiveness objectives would not prompt the FCA to take any action inconsistent with its existing objectives which, if this were to be the case, would call into question the whole rationale for introducing the additional objectives. In practice, we think that adding another objective, even if it is framed as a secondary objective, will

¹ ‘Principles of effective regulation’, National Audit Office, May 2021, at p. 20.

inevitably foster changes in how the FCA approaches issues since it will have to be incorporated into the way the regulator considers issues and reaches decisions. It would also seem to leave the regulator's decisions open to challenge on the basis that it may have failed to take account of competitiveness considerations. We are concerned that this will further complicate the regulator's decision-making process and potentially have a chilling effect on its ability and willingness to undertake activity to advance its other objectives, including to protect consumers.

- **A competitiveness objective threatens to dilute existing consumer protections** - we are concerned that the introduction of new growth and international competitiveness objectives may weaken consumer protection, with UK regulators competing with their international counterparts to dilute standards to attract inward investment. We take some comfort from the Treasury consultation which asserts that robust regulatory standards are the cornerstone of the attractiveness of the UK's markets. The Minister is also on record making clear that it is resilient and efficient markets, underpinned by effective regulation and competition, that are essential prerequisites for fostering an internationally competitive and respected financial services sector². However, if this is the case, and international competitiveness should be achieved through sound regulatory standards which provide a stable and secure environment, then we would suggest that additional growth and competitiveness objectives are not needed and there are preferable ways to enhance UK competitiveness. This would appear to be a view shared by the current FCA Chief Executive who was asked about the a competitiveness objective at his appointment hearing with the Treasury Committee where he made clear that he was personally not a fan and did not think that such a change is necessary in order to have a strong, successful and dynamic sector³. We also note that a recent survey confirms the competitiveness of the UK financial services sector under the existing regulatory framework, with almost 90% of global financial services investors planning to establish or expand operations in the UK in 2022.⁴
- **There is likely to be a reduced willingness to advance consumer protection measures** - While consumer groups seek to engage with the FCA and to respond to its consultations in order to ensure the consumer voice is heard and consumer interests are represented, their limited resources and funding inevitably mean that their capacity to do so can often be limited. However, in this context it is important to note that the FCA itself - in keeping with its consumer protection objective - has itself often driven significant positive change, for example in its work on vulnerability and in its current proposals for a new Consumer Duty. We are very uneasy about the introduction of new growth and international competitiveness objectives because we consider they will reduce the FCA's willingness and ability to address new, emerging harms and advance important

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<https://www.gov.uk/government/speeches/speech-by-john-glen-mp-economic-secretary-to-the-treasury-to-the-uk-finance-annual-dinner>

³ <https://committees.parliament.uk/oralevidence/746/html/>

⁴ https://www.ey.com/en_uk/news/2022-press-releases/01/investor-confidence-in-uk-financial-services-hits-new-high-amid-covid-19

measures to protect consumers since they will need to balance potential positive consumer outcomes with concerns that such measures may reduce the international competitiveness of the UK. Charles Randell, the FCA Chair recently highlighted this potential issue, pointing out to the Treasury Committee that *“the risk [is] that whenever we propose to do something, we receive a large amount of lobbying input saying this rule doesn’t exist in this country or that country or the other country, and therefore you shouldn’t do it.”*⁵

In our response to Q6 below we provide further views on what we consider to be the shortcomings of HMT’s proposed reliance on consultation as the primary mechanism to engage with stakeholders and allow scrutiny of the development of regulatory proposals.

- **Past experience provides a stark warning about the negative consequences which can arise when regulators are tasked with promoting competitiveness** - we note that before the financial crisis in 2007-8, the UK regulator - the Financial Services Authority - was required to consider the UK’s competitiveness. And, in fact, a previous HM Treasury publication makes plain the negative impact that this appeared to have, noting that *“there is an argument that one of the reasons for regulatory failure leading up to the financial crisis was an excessive concern for competitiveness leading to the acceptance of a ‘light-touch’ approach to regulation and supervision”*⁶. Andrew Bailey, former Chief Executive of the FCA and currently Governor of the Bank of England, summed up its impact more pithily, observing that the regulator *“was required to consider the UK’s competitiveness, and it didn’t end well, for anyone.”*⁷ Given the scale of the consequences which arose from the financial crisis, and the role that competitiveness may have played in bringing about the crisis, we have significant reservations about proposals to re-introduce a competitiveness objective. In the words of one commentator, *“the reawakening of “competitiveness” risks sleepwalking into the mistakes of the past”*⁸.
- **Others are already tasked with this responsibility so it is not clear what additional role regulators can play** - There are already a number of other organisations which have responsibility to promote the UK’s financial services, including HM Treasury and the City of London’s Lord Mayor, while industry associations as well as firms themselves also have a clear interest in advancing this objective. In this context, it is not clear what additional role that regulators can play. However, there is a very real risk that this approach may have a considerable downside, since it will encourage regulators to do more to actively seek out and reflect industry views, thereby undermining regulatory independence. At a time when there is already a substantial systemic imbalance

⁵ <https://committees.parliament.uk/oralevidence/3177/pdf/>

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https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/927316/141020_Final_Phase_II_Condoc_For_Publication_for_print.pdf

⁷ <https://www.fca.org.uk/news/speeches/future-financial-conduct-regulation>

⁸ <https://www.ft.com/content/96517774-a6cc-4e30-a1a4-b82f612c1df3>

between the ability of industry and consumer stakeholders to advance their interests with the regulators⁹ this move would potentially serve to compound these differences.

- **HMT can already make recommendations to the FCA about areas it should have regard to** - The Financial Services and Markets Act 2000 requires the Treasury, at least once in each Parliament, to make recommendations to the FCA about aspects of the economic policy of the government to which the FCA should have regard. In March 2021 the Chancellor wrote to the Chief Executive of the FCA stating that the FCA should take a number of considerations into account in its assessment of the costs, burdens and benefits of potential rules or policies. These considerations included both growth and competitiveness¹⁰. Regular engagement between HMT and FCA, as well as more formal hearings such as those conducted by the Treasury Select Committee, offer the opportunity for Government and Parliament to hold the FCA to account, and for the FCA to explain how it has taken these considerations into account.

Taken together, we consider that not only has the case for adding new growth and international competitiveness secondary objectives not been made, but that proceeding with this proposal has the potential to significantly undermine the FCA's ability to protect consumers. In this context, we also note the statement of the Chancellor in his Mansion House speech in July 2021 that sharpening our competitive advantage should be 'while acting in the interests of our citizens and communities'¹¹. We urge HM Treasury to reconsider this element of its proposals.

2. Do you agree that the regulatory principle for sustainable growth should be updated to reference climate change and a net zero economy?

We agree that it would be sensible to amend the regulatory principle for sustainable growth in section 3B FSMA to make this clear, given the urgency of the challenges faced by the UK in this area. We are fully committed as an organisation to championing sustainability for consumers. However, we would additionally urge the Government to consider reviewing and amending the regulatory principle also found in this section of FSMA that 'consumers should take responsibility for their decisions'. As has been pointed out by other stakeholders, given the enormous changes in consumer markets in the last decade or so brought about in large part by new technology, it is more difficult than ever for consumers to take fully informed decisions and to protect themselves from exploitation. The current wording is therefore not sufficient, and could be supplemented for example to read, '...consumers should take responsibility for their decisions, to the extent that it is reasonable and practical for them to do so'. This legislative change would reflect the proposed changed approach and emphasis set out by the FCA in its current consultation on a new Consumer Duty where it states "consumers can only reasonably

⁹ See, for example, the Financial Services Consumer Panel's response to *HM Treasury's future regulatory framework phase II consultation* for further information about this imbalance, available at https://www.fs-cp.org.uk/sites/default/files/final_fscp_response_hmt_fr_review_phase_ii_20210219_v2.pdf

¹⁰ <https://www.gov.uk/government/publications/recommendations-for-the-financial-conduct-authority-march-2021/recommendations-for-the-financial-conduct-authority-march-2021>

¹¹ <https://www.gov.uk/government/speeches/mansion-house-speech-2021-rishi-sunak>

be expected to take responsibility for their choices and decisions if firms act openly and with honesty, avoid causing customers foreseeable harm and take proactive steps to empower consumers to make good choices by establishing an environment in which consumers can make decisions in their own interest and realise their financial objectives¹².

3. Do you agree that the proposed power for HM Treasury to require the regulators to review their rules offers an appropriate mechanism to review rules when necessary?

We agree that this would be a useful and proportionate tool for HMT, without impinging unnecessarily on the regulators' independence. We recognise the delicate balancing act to be struck here, so would also suggest that the power be subject to the right of regulators to refuse to do so if they can provide a public and reasoned justification for why it would not be necessary or desirable to conduct such a review. Which? would be keen to see that such a power would be exercised in order to protect the interests of consumers, for example in situations where the rules in force are no longer having the effect intended, to the detriment of consumers.

4. Do you agree with the proposed approach to resolve the interaction between the regulators' responsibilities under FSMA and the government's overseas arrangements and agreements?

We have been carrying out a series of in-depth public dialogues around the UK, as well as wider consumer research, to gain insight into consumer awareness and priorities for trade deals. It is essential that the government ensures that the negotiating objectives for trade deals are aligned with our national policy priorities and that these reflect consumers' expectations. We have concerns if regulators are instead making their policy based on an assessment of the provisions within trade deals. Compliance with international law should be a matter in the first instance for central government. This is one of the reasons why we have called for the government to set out an overarching trade strategy which shows how our negotiating objectives are aligned with policy priorities - and were pleased to see that the National Audit Office's recent report¹³ assessing progress with trade negotiations also made this recommendation.

5. Do you agree that these measures require the regulators to provide the necessary information to Parliament on an appropriate statutory basis to conduct its scrutiny?

We agree with the proposal for a new statutory requirement for the PRA and the FCA to notify the relevant Parliamentary committee when they publish a consultation on any matter, in the interests of ensuring that committees are aware of all matters which require their scrutiny (particularly in view of the anticipated increase in the flow of rule changes and consultations). We note that any statutory provision containing this requirement will need to be drafted in a sufficiently flexible way to capture all relevant committees (including any new committees which may be formed in due course).

¹² A new Consumer Duty - Feedback to CP21/13 and further consultation. FCA, Para 6.15

¹³ 'Progress with trade negotiations', National Audit Office, December 2021

We also agree with the proposal for a new statutory requirement for the regulators to respond in writing to formal responses to statutory consultations from Parliamentary committees. In our view this requirement formalises what tends to happen in practice currently and so would not detract from the regulators' independence, and it should ensure a greater level of regulator engagement with (and consideration of) Parliamentary scrutiny and suggestions.

6. Do you agree with the proposals to strengthen the role of the panels in providing important and diverse stakeholder input into the development of policy and regulation?

We support the proposals to strengthen the role of the statutory panels, specifically *Measure 9: Statutory requirement for the regulators to publish information on their engagement with the panels* and *Measure 10: Statutory requirement for the regulators to maintain a statement on appointment processes for the panels*.

We also support the suggestion that the regulators should continue to consider the diversity of panel membership. We agree with HM Treasury that it is particularly important that a representative balance of stakeholder types and views are included, but we think that this should be reflected not just in the membership of the existing panels but through consideration of whether the number and type of existing panels provides a suitable balance between industry and consumer and wider civil society interests.

HM Treasury's consultation document also considers the issue of wider stakeholder engagement in the regulatory process. It explains (at Paragraph 25 of the Executive Summary) that it is vital that there are opportunities for consumers, relevant stakeholders and firms to engage with and scrutinise the development of regulatory proposals. It goes on to suggest that the government considers that the existing primary method for this engagement, the regulators' requirement to consult publicly on their draft rules, remains the key mechanism for this engagement. We concur that open consultations are key to elicit views from a variety of stakeholders, and we appreciate the steps that regulators (e.g. the FCA) make to go beyond their statutory requirement to consult. However, HM Treasury should be aware that the capacity of consumer groups to respond to consultations can be limited. To give a sense of the scale of the task in responding to consultations about financial services, in 2021:

- the FCA issued approximately 50 Policy consultations, guidance consultations or Discussion Papers
- the Payment Systems Regulator issued 11 consultations
- HM Treasury consulted on major topics such as Buy Now Pay Later, the Future Regulatory Framework, Access to Cash, Financial Promotions, Cryptoassets and Stablecoins
- the Department for Work and Pensions (DWP) consulted on a range of topics, including Stronger Nudge to Pensions Guidance, Permitted Charges within Defined Contribution Pension Schemes, and Simpler annual benefit statements

- the Financial Ombudsman Service consulted on its Plans and Budget, and also on Temporary changes to reporting the outcomes of proactively settled complaints.

In addition, other organisations such as the Competition and Markets Authority (CMA), Bank of England, Lending Standards Board and various Select Committees (most notably the Treasury Committee and Work and Pensions Committee) all publish consultations which are of interest to consumer stakeholders.

We simply do not have the capacity to respond to all the issues consulted on, and already have to make difficult decisions about prioritisation. We understand that other consumer organisations face similar challenges. We suggest HM Treasury and regulators should take account of the potential shortcomings of relying just on consultations to enable proper scrutiny of regulatory proposals. There would seem to be a strong case to think more creatively about how best to gain views from this constituency, and not to rely solely on the views expressed in response to formal consultations. One option to achieve this could be to make greater efforts to seek views from consumer representatives through informal processes (e.g. informal roundtable discussions) which may be easier to engage with as they do not require pre-reading, extensive knowledge of the subject matter, or submission of a written response. Additionally, we would encourage regulators and policymakers to undertake proactive engagement with consumers themselves who may have direct experience of, or who would be impacted by, the regulatory changes being considered.

7. Do you agree that the proposed requirement for regulators to publish and maintain frameworks for CBA provides improved transparency for stakeholders?

In general terms, we agree with the proposal for a new statutory requirement for the regulators to publish and maintain a public version of their framework for conducting CBA. However, as the latest consultation document shows, respondents to the previous consultation had a range of specific concerns about the detail and content of the regulators' CBA, and as a result we feel that the requirement to publish a framework would not go far enough to address those issues (and, in any event, the FCA already publishes a framework on its approach to CBA). For example, as stated in the consultation, some consumer groups felt that CBA was overly concerned with the cost to firms, and disregarded quantifying benefits. In addition, the FCA only publishes a cost-benefit analysis on the policy option it selects to take forward, rather than the process followed by Government Departments which set out a range of potential interventions and the costs and benefits associated with each option.

In order to address these deficiencies in the regulators' current CBA outputs we would suggest that the statutory intervention should be more prescriptive. In particular, it should require regulators to conduct a CBA for a range of potential interventions and the costs and benefits associated with each option rather than conducting this solely for its preferred option. This should include quantification of the 'do nothing' option, and as well setting out the financial costs to consumers it should seek to estimate the wider impacts of action or inaction on consumer wellbeing. Recent research undertaken by Which? in conjunction with Simetrica-Jacobs sought

to make use of HM Treasury's Wellbeing Guidance¹⁴ to quantify the wellbeing impact of scams on victims, looking beyond just the financial losses suffered.¹⁵ In total, the research found that victims of scams in the UK suffer a hit to their well-being that can be calculated at £9.3bn a year, well beyond estimates of financial losses. Regulators should be required to adopt a similar, more expansive approach to quantify the total costs borne by consumers of different policy options.

8. Should the role of the new CBA Panel be to provide pre-publication comment on CBA, or to provide review of CBA post-publication?

In our view the new CBA panel should provide pre-publication comment on the regulators' CBA, as we believe that this approach will be more effective in improving the quality of the CBA (and would likely produce improvements sooner). In Which?'s view, scrutiny on this more specific, individual, in-depth basis would also be more likely to result in positive changes to the CBA process, compared to a more general 'post-publication' approach.

We recognise the potential for this approach to cause delays and we therefore appreciate that there will be a need for thresholds, exemptions and expedited processes, where appropriate. However, we would also predict that as the quality of CBA improves, the volume of comments and advice that the panel would be required to provide on each CBA would decrease, as best practices are identified and adopted.

9. Do you agree that the proposed requirement for regulators to publish and maintain frameworks for how the regulators review their rules provides improved transparency to stakeholders?

We agree with the proposal to require the PRA and FCA to publish and maintain a framework for how regulators review their rules. As the consultation notes, the regulators already review their policies and the FCA publishes its framework for ex post impact evaluation, but the proposed requirements would improve transparency and ensure a greater degree of consistency over when and how regulators review the impact of their rules.

We also agree that the content of the framework should be left to the regulators to develop. We have already observed the FCA taking positive steps to be more transparent about the outcomes it seeks, with its latest Business Plan seeking to ensure accountability by setting measurable goals and reporting publicly on progress made¹⁶ - a process that was adopted in its *Consumer Investments: Strategy and Feedback Statement* where specific, detailed target outcomes were published.¹⁷ We would expect the regulators to consult on their proposed

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https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1005388/Wellbeing_guidance_for_appraisal_-_supplementary_Green_Book_guidance.pdf

¹⁵ <https://www.which.co.uk/policy/digital/8403/scams-and-subjective-wellbeing>

¹⁶ <https://www.fca.org.uk/publication/business-plans/business-plan-2021-22.pdf>

¹⁷ <https://www.fca.org.uk/publications/corporate-documents/consumer-investments-strategy>

framework to ensure it helps to ensure the desired level of transparency, and this should include efforts to seek input from consumer stakeholders that are unable to respond formally.

10. Do you agree with the government’s proposal to establish a new Designated Activities Regime to regulate certain activities outside the RAO?

We do not agree with this proposal. From a consumer perspective, it is important that the regulatory perimeter is clear and that any activities (and entities that carry on such activities) that might lead to consumer harm are authorised and subject to compliance sanctions. It would be unnecessarily complex and lacking in transparency to create a new regime.

11. Do you agree with the government’s proposal for HM Treasury to have the ability to apply “have regards” and to place obligations on the regulators to make rules in relation to specific areas of regulation?

It is welcome that the Government recognises the importance of public policy considerations such as protecting consumers from harm. In addition, it is often not appropriate for regulators such as the FCA to have to make difficult judgments on matters of social policy when considering new rules. In this context, ‘have regards’ directions or a power to direct that rules should be made may be necessary. But, especially given concerns about the independence of regulators and the arguments we make in answer to Q1 about conflicting objectives complicating the FCA’s decision-making process, it would in our view be preferable to have key principles and rights on such issues set out in primary legislation in the first place (as is proposed on access to cash, for example).

About Which?

Which? is the UK’s consumer champion. As an organisation we’re not for profit - a powerful force for good, here to make life simpler, fairer and safer for everyone. We’re the independent consumer voice that provides impartial advice, investigates, holds businesses to account and works with policymakers to make change happen. We fund our work mainly through member subscriptions, we’re not influenced by third parties and we buy all the products that we test.

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February 2022