Consultation response

FCA Discussion Paper: **Duty of care and potential alternative approaches (DP18/5)**

Response from the Money Advice Service

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1. About us

1.1. The Money Advice Service (MAS) is a UK-wide, independent service set up by Government to improve people's ability to manage their financial affairs. Our free and impartial money guidance is available online, and by phone or webchat.

1.2. We change lives by helping people make the most of their money. We use evidence to understand who, across the UK, most needs help and what works, and we use these insights to improve the ability of people to manage their money, either through partners, or directly.

1.3. We are responding to this consultation in respect of our statutory roles to enhance people's understanding and knowledge of financial matters; improve individuals' ability to manage their own financial affairs; and to work with partners to improve the availability, quality and consistency of debt advice across the UK.

1.4. MAS has led work with financial services firms, the third sector, government and regulators to develop the Financial Capability Strategy for the UK. This 10-year strategy aims to improve financial capability, giving people the ability, motivation and opportunity to make the most of their money.

1.5. The Financial Guidance and Claims Act 2018 makes provision for establishing a new Single Financial Guidance Body. It received royal assent on 10 May 2018. The new Single Financial Guidance Body (SFGB), which will bring together the Money Advice Service, Pension Wise and the Pensions Advisory Service will have statutory functions to:

- Provide free and impartial information and guidance to enhance people's understanding and knowledge of financial matters and their ability to manage their own financial affairs to the public
- Provide free and impartial debt advice in England
- Develop and co-ordinate a national strategy to improve:
    - the financial capability of members of the public
    - the ability of members of the public to manage debt, and
    - the provision of financial education to children and young people[1]

2. Executive summary

2.1. MAS supports the introduction of a New Duty that would give financial services firms a positive obligation to promote customers' best interests; and a fiduciary duty not to cause harm to a customer's financial interests. This New Duty could bring fairness to all financial markets and could help the FCA to deliver their commitments outlined in *Approach to Consumers.*[2]

[1] Financial Guidance and Claims Act, 2018

[2] https://www.fca.org.uk/publication/corporate/approach-to-consumers.pdf

2.2. MAS believe that there are currently potential gaps in the FCA's approach that may be addressed by introducing a New Duty, where firms are not breaching FCA rules, but the framework could be enhanced to give consumers greater protection.

2.3. A New Duty could give a better balance between firm and consumer responsibilities and help deliver extra protection and better treatment to vulnerable consumers.

2.4. The FCA's analysis of its Financial Lives survey identifies 50% of consumers display one or more characteristics of potential vulnerability. The FCA has shown in its Approach to Consumers that low financial capability is a key driver of consumer vulnerability. MAS believe a lack of financial capability could be considered a form of vulnerability, as something that contributes to other forms of vulnerability, or both.

2.5. There is a complementary relationship between financial capability and regulatory intervention. Some features of the financial market mean that whether consumers make good choices or not they face bad outcomes. These problems are exacerbated by the limited cognitive bandwidth created by financial difficulty, vulnerable circumstances or life events. The FCA can help by making sure existing products work fairly and ensuring appropriate access to the advice, guidance and products and services consumers need.

2.6. In line with the stated aim of the FCA's Mission to focus on prevention rather than cure, a New Duty - with a positive obligation to promote customers' best interests - could encourage firms to identify potential customer harm and avoid it.

2.7. To adequately monitor detriment the regulator should draw on a range of intelligence, including social policy data from consumer groups. Where detriment is identified the FCA must use its regulatory powers appropriately.

3. Response

Q1. Do you believe there is a gap in the FCA's existing regulatory framework that could be addressed by introducing a New Duty, whether though a duty of care or other change(s)?

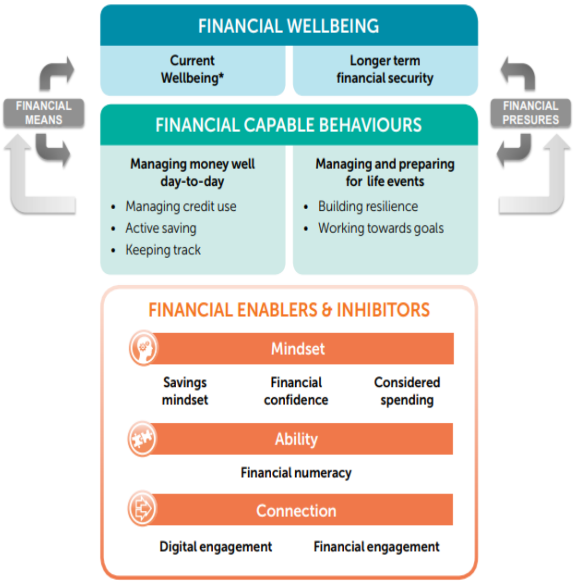
3.1. MAS believe that there are currently potential gaps in the FCA's approach that may be addressed by introducing a New Duty. These gaps can be identified through the FCA's Principle 6 (commonly known as Treating Customers Fairly [TCF]) and Principle 7 in areas where firms are not breaching FCA rules, but the framework could nevertheless be enhanced to give consumers greater protection.[3] We believe that a New Duty could enhance consumer protection, especially for those consumers with low financial capability.

3.2. Financial capability is a person's ability to manage money well, both day to day and through significant life events, and to handle periods of financial difficulty. It is driven by personal skills, knowledge, attitudes and motivations, and made possible by an inclusive financial system and

[3] https://www.fca.org.uk/publication/research/financial-lives-consumers-across-uk.pdf

supportive social environment. Financial capability helps people achieve the best possible financial well-being.[4] The Money Advice Service's financial capability framework (see Figure 1 below) captures the main elements of financial capability – the behaviours underpinning financial capability and the factors impacting it – in a single model.

Figure 1: The Financial Capability Framework



3.3. MAS have identified the following specific areas where we think a New Duty could enhance consumer protection:

The Savings Market

3.4. In the savings market, providers can reduce interest rates on existing customers' accounts by declaring an account "obsolete". The new rules on disclosure of interest rates are not currently applied to "obsolete" accounts. It is worth noting that these accounts are not necessarily obsolete from the customer's perspective, many of whom will not understand this term or what it means for their money.

3.5. Overall, 46% of UK adults have checked their savings account in the last 12 months to see if they are getting the best deal. However, people with lower levels of skills and knowledge and those with lower levels of confidence in making decisions about financial products and services are less likely to have changed their account provider or done anything to check if they are getting the best deal in the last 12 months.[5] People who felt there was nothing they could do that would influence their own financial situation were significantly less likely to have done anything to check if they were getting the best deal.

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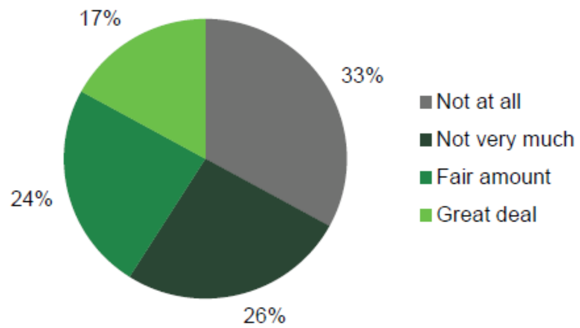
[4] MAS (2015) Financial Capability Strategy for the UK

[5] MAS (2015) UK Financial Capability Survey

Figure 2. Shopping around for better deals on bank/ savings accounts – preliminary analysis of data from the 2018 Financial Capability Survey



3.6. Many UK adults (42%) do not describe themselves as being confident managing their money and around half do not see that they can make a difference to their situation. Our research has found that financial confidence (comprising both confidence managing money day to day and the confidence to make financial decisions) is by far the most important individual dimension of the enablers and inhibitors of current financial wellbeing, and is also the most important dimension of longer-term financial security.[6] Low financial confidence presents a significant barrier to consumers actively engaging with their money, comparing and switching savings account.

3.7. MAS believes that a New Duty, giving firms have a positive obligation to promote consumers' best interests could set a consumer-focussed default across financial markets. Such a duty would mean, in this specific case that "obsolete" account holders should be migrated to accounts offering good value, without the requirement and consumer burden of having to open a new account. More generally, a positive obligation to promote consumers' best interests would mean that consumers are offered good quality products and services that meet their needs and that are sold in a way that is clear, fair and not misleading.

Credit

3.8. If a customer tries to withdraw funds beyond their overdraft limit, providers can allow the withdrawal without telling the customer at the point of making the decision what charges will result. Under TCF, as long as the customer has been told the charging structure, this is considered fair.

3.9. Consumers who experience persistent use of unarranged overdrafts can face a high level of detriment. Many financial products – and overdrafts in particular – are quite complex, and there is a known problem with their comprehension by consumers. In our UK Financial Capability Surveys, we have found that even the simple measures of reading a bank statement, comprehending inflation and buying power, and calculating a balance after interest were challenging for a significant minority of those surveyed. The low levels of understanding of overdrafts in particular – including consumers

[6] MAS (2016) Measuring financial capability – identifying the building blocks

not considering overdrafts to be debt, as well as being confused about how they work and the charges involved – and low consumer engagement are well-established issues.[7]

3.10. MAS therefore supported the FCA's proposals on the provision of information and tools to improve customer understanding and better use of overdrafts.[8] We agree persistent overdraft use is problematic and that it is essential that vulnerable consumers are identified and supported.

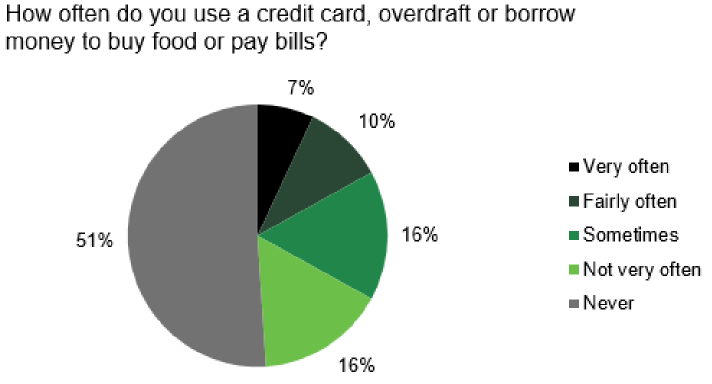
3.11. Access to affordable credit and people's ability to make informed financial decisions is key to day-to-day money management and an important aspect of financial capability.

3.12. 'Managing credit use' is identified in our financial capability model as a key financially capable behaviour – indeed, our UK financial capability survey found that managing credit use is the behaviour with the greatest impact on current financial wellbeing. Managing credit is also second only to building resilience in terms of the money behaviours that are most highly correlated with longer-term financial security. Helping consumers to manage their credit use effectively is therefore an important area of focus for improving financial capability.[9]

3.13. MAS has therefore implemented a long-term impact measure to reduce the proportion of 'financially struggling' and 'financially squeezed' adults who regularly use credit for everyday spending (to buy food or pay bills because they are short of money). We are supporting the UK Financial Capability Strategy's corresponding 'rallying cry' across the sector to reduce levels of reliance on unsecured credit for everyday spending. We are also undertaking work to develop financial rules of thumb to guide young consumers' credit use – which includes overdrafts as well as credit cards and loans, etc.

3.14. Advance preliminary analysis of MAS's forthcoming UK Financial Capability Survey 2018 shows that 7% of UK consumers use credit, an overdraft or borrow money to buy food or pay bills, and a further 10% do so fairly often. Among the over-indebted population, 44% use credit to pay for food or bills at least fairly often, and 21% do so very often.

Figure 3: Credit use (Preliminary analysis of UK Fin Cap Survey 2018)



[7] Atticus (2018) Consumer research on overdrafts

[8] https://www.fca.org.uk/publication/consultation/cp18-12.pdf https://www.fca.org.uk/publication/consultation/cp18-13.pdf

[9] MAS (2016) Measuring financial capability – identifying the building blocks

3.15. We estimate that 8.3 million people are over-indebted, i.e. they find keeping up with bills and/or credit commitments a heavy burden or have fallen behind on, or missed, any payments for bills and/or credit commitments in any three or more months in the last six months.[10] Firms should not grow this number by allowing customers to withdraw funds beyond their overdraft limit, without telling the customer at the point of making the decision what charges will result. If they are already at their credit limit this indicates a pre-existing level of financial difficulty.

3.16. The recent FCA thematic review into early arrears management in unsecured lending shows that firms are still missing early opportunities to identify consumers in financial difficulty and offer appropriate forbearance. Moreover, the findings showed that a firm's culture can influences the approach taken to giving due consideration and forbearance to consumers in arrears difficulties.[11]

3.17. FCA research on 'Creating and sustaining cultures of compliance' suggests that how you signal the duties of firms to staff is important and a New Duty could help with that as well as potentially signalling to consumers what standard of care they should expect.[12]

The Loyalty Penalty

3.18. The 2015 UK Financial Capability Survey shows that levels of financial capability across the UK remain stubbornly low. While many people are taking control of their finances and putting something aside for a rainy day when they can, there are still far too many failing to get the help they need and therefore at risk of detriment. The Financial Capability Survey found that:

- 42% of UK adults do not describe themselves as being confident managing their money (giving themselves a score of seven or less out of ten) and around half agree that their financial situation makes them anxious or don't see that they can make a difference to their situation.
- Only 48% of adults agree that there are things they can do that will influence their own financial situation.
- People who report low confidence making decisions about financial products and services are less likely to have switched current account or taken any other actions to check they were getting the best deal in the past 12 months.
- Around one in eight people agree that they are too busy to sort out their finances.
- One in three (30%) do not discuss money openly with anyone.
- Around one in eight (13%) people agree that they are too busy to sort out their finances

[10] https://www.moneyadviceservice.org.uk/en/corporate/debt-publicationsin_the_UK.pdf
[11] https://www.fca.org.uk/publications/thematic-reviews/early-arrears-management-unsecured-lending-tr16-10
[12] https://www.fca.org.uk/insight/creating-sustaining-cultures-compliance

3.19. These findings are relevant to consumers' capability to shop around for financial products and essential services. We know that consumers with lower levels of skills and knowledge and those who lack confidence making decisions about financial products and services are less likely to have changed a number of products or providers or done anything to check if they are getting the best deal in the last 12 months.

3.20. The lack of both triggers to compare products and prompts to switch products combined with low levels of financial capability in the UK has given rise to consumers paying a loyalty penalty. A loyalty penalty is the cost of being a long-standing customer, compared to a new customer receiving the same product or service. In markets such as energy and home insurance, this occurs when loyal customers default onto a more expensive 'standard' tariff once their original contract comes to an end.

3.21. Consumers who have been with their home insurance provider for five years or more pay 70% higher premiums than new consumers despite evidence suggesting that they pose no higher risk than new consumers.[13] Citizens Advice have identified that currently 47% of consumers of home insurance are paying a loyalty penalty in the UK.[14]

3.22. Since new regulations came into force, people are more likely to notice price increases. However, the Citizens Advice research identified that 32% of consumers still renewed their policy without checking for better deals first and that vulnerable consumers are particularly likely to be penalised by the loyalty penalty.[15]

3.23. There does appear to be a loyalty penalty in the pensions market too. Pension providers have offered their loyal customers annuity rates up to 15%-20% below the market best rates. Pension providers have previously also failed to promote or offer enhanced annuities to their customers which could result in people with health conditions missing out on higher rates. Offering a consumer a rate 20% below the best market rate is equivalent to taking the last 11 years of a person's pension contributions away. Although this treatment of consumers does not seem fair, these companies were not breaching the FCA's Principles.

3.24. From March 2018, the FCA put rules in place so that consumers now see the difference between the providers' quote and the market-leading quote when they request a quote for an annuity for a specific income.[16] Following the FCA's Retirement Outcomes Review, providers are now required to ask consumers basic questions about their health and lifestyle to determine whether a customer is eligible for an enhanced annuity.[17] MAS are currently undergoing work to build upon our Annuity Comparison Table tool to include the Enhanced Pension Annuity Quotation Form, to help consumers better understand that they

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[13] FCA, Price discrimination and cross-subsidy in financial services, September 2016.

[14] Citizens Advice, The insurance loyalty penalty: unfair pricing in the home insurance market, November 2017.

[15] Citizens Advice, The insurance loyalty penalty: unfair pricing in the home insurance market, November 2017.

[16] FCA PS17/12

[17] FCA MS16/13

may be able to get a better annuity rate depending on their health condition. Shopping around for the best annuity rate on the open market can increases a person's retirement income by 10% on average.

3.25. MAS believes that by introducing A New Duty - giving firms a positive obligation to promote customers' best interests and a fiduciary duty not to cause harm to a customer's financial interests – the FCA could start to address the loyalty penalty, which is currently causing harm to consumers' financial interests. Citizens Advice estimate that the cost of the loyalty penalty in the home insurance market alone is £708,500,000 per annum.

Q2. What might a New Duty for firms in financial services do to enhance positive behaviour and conduct from firms in the financial services market, and incentivise good consumer outcomes?

3.26. Recent changes in public policy and the marketplace – such as the pension freedom and choice reforms - have put more responsibility on individual consumers and increased the need for a greater and more innovative regulatory response.

3.27. MAS believes that a New Duty could give a better balance between firm and consumer responsibilities – the importance and complexity of financial services products can give rise to an imbalance of knowledge, understanding and bargaining power between firms and their consumers.

3.28. The choices that consumers face are complex, and the way firms communicate and structure propositions can do more or less to enable and support consumer capability. Some features of the financial market mean whether consumers make good choices or not they can face bad outcomes – for example, when accessing insurance, or banking as a third-party, or using effective digital comparison tools, or engaging with credit referencing. As our response to the creditworthiness consultation highlighted, firms need to do more to ensure the products they offer are effectively assessed for affordability.[18]

3.29. These problems are exacerbated by the limited bandwidth created by financial difficulty. People in financial difficulty often filter out non-essential communications because of the excessive cognitive load being in debt places on them.[19] This is a common and persistent cognitive bias and the market should be expected to take account of it.

A New Duty with a positive obligation to promote customers' best interests could encourage firms to identify potential customer harm and avoid it, in line with the stated aim of the FCA's Mission to focus on prevention rather than cure.

[18] Money Advice Service response, *FCA CP17/27: Assessing creditworthiness in consumer credit*, (October 2017)
[19] Money Advice Service, *How to use behavioural science to increase the uptake of debt advice*, (September 2017)

Q3. How would a New Duty increase our effectiveness in preventing and tackling harm and achieving good outcomes for consumers? Do you believe that the way we regulate results in a gap that a New Duty would address?

3.30. A New Duty, with a positive obligation, could help deliver extra protection and better treatment to vulnerable consumers. The FCA's analysis of its Financial Lives survey identifies 50% of consumers display one or more characteristics of potential vulnerability.[20] MAS believes a lack of financial capability could be considered a form of vulnerability, as something that contributes to other forms of vulnerability, or both.

3.31. Those with low financial capability are vulnerable because it limits the ability of individuals and families to manage their money, plan and make financial decisions that are right for them. Low capability can contribute to other forms of vulnerability because it leaves families in a precarious position, unable to respond when life events such bereavement occur, and individuals experiencing health difficulties without the adequate financial buffer to address them.

3.32. MAS is working to build awareness and trust in the support and guidance available to vulnerable consumers in a way that is focused, timely and relevant. This is both through our commissioned work and with partners through the Financial Capability Strategy.

3.33. We have approached this with a focus on life events and our commissioning of debt advice services. Our debt advice commissioning strategy for 2018–2023 was designed with families with dependent children, low household incomes and those who experience mental ill health in mind.

3.34. Our Right Place, Right Time research explored which life events are most likely to see people need advice and guidance and why they might not seek help at those points.[21] The biggest opportunity to get more help to more people is through building awareness and trust in what's available.

3.35. We are also trying to help organisations understand consumers who may be in vulnerable situations. Two examples of this are our What Works Fund and our project with the Money Advice Trust and the University of Bristol on the debt advice approach to vulnerability. The What Works Fund provided grants to over 65 projects totalling over £11 million. Many of these concentrated on reaching those in a difficult place.

3.36. This is an area the SFGB is going to continue to take very seriously, as the objectives of the new body specify it must bear in mind the needs of people in vulnerable circumstances.

3.37. A New Duty of care could give vulnerable consumers the confidence to seek help from their bank or other firm, knowing they can get tailored support to meet their needs. A New

[20] FCA Financial Lives Survey 2017
[21] MAS, Right Place Right Time research 2017

Duty giving financial services firms a positive obligation to promote customers' best interests; and a fiduciary duty not to cause harm to a customer's financial interests could enable consumers to take legal action to obtain redress for a breach of a duty of care. Consumers are currently unable to take legal action solely as a result of a breach of an FCA principle such as treating consumers fairly.

Q4. Should the FCA reconsider whether breaches of the Principles should give rise to a private right for damages in court? Or should breaching a New Duty give this right?

Q5. Do you believe that a New Duty would be more effective in preventing harm and would therefore mean that redress would need to be relied on less? If so, please set out the ways in which a New Duty would improve the current regime.