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Discussion paper: Business Leadership in Consumer Protection  
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**SENT VIA E-MAIL**

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Dear Kate

**Response to Discussion paper: Business Leadership in Consumer Protection**

The BBA is the leading association for the UK banking and financial services sector, speaking for 223 banking members from 60 countries on the full range of UK or international banking issues and engaging with 37 associated professional firms. Collectively providing the full range of services, our member banks make up the world's largest international banking centre, operating some 150 million accounts and contributing £50 billion annually to the UK economy.

We welcome the opportunity to respond to this discussion document. Our response to the discussion paper will consider some general points, rather than specifically addressing the detailed questions set out in Chapter 5 of the document. However, before we do so, we think it would be useful to set this in the context of the current regulatory environment for financial services in the UK and set out what we think are the characteristics of a good regulatory model.

**Introduction**

The UK retail banking industry is large, innovative and efficient. In 2007 there were in excess of 131 million accounts for individuals held by the UK banks, 103 million of which were interest bearing. These accounts are generally very actively used; there were 93 million requests to make bill payments and inter-account transfers over the telephone alone last year, with a further 314 million similar transactions initiated online – clear evidence that banking has embraced the internet revolution and kept pace with the massive technological changes of the past 15–20 years.

At the same time, the banking industry has maintained a significant branch presence of nearly 10,000 branches nationwide, enabling customers a greater choice of how to do their banking.

These huge numbers give some indication of the extent of retail activity with which the banking industry is involved. Whilst mistakes can be made and every one is important to the individual concerned, overwhelmingly retail activities are undertaken correctly, are executed rapidly, the records are complete and the process completed to the required timetable.

Customers value their banking relationship. The OFT's recent Market Study into personal current accounts showed levels of satisfaction at over 70 per cent, and independent surveys – such as the 2008 BBC Watchdog survey - consistently paint a similar picture.

Given the extent to which retail banking has become an intrinsic part of our daily lives, policy makers have (unsurprisingly) scrutinised the sector from most angles. The past decade has thus seen regulatory change on an unprecedented scale – with a raft of sweeping changes in the retail financial services market, including:

- a. the introduction of mortgage legislation for the first time in the UK<sup>1</sup>;
- b. changes to credit legislation – now under further review following recent European legislation – that will have taken nearly a decade to conclude when the final regulations come into effect in 2010;
- c. new rules on general insurance sales, revised in 2008;
- d. the introduction of a raft of 'fair play' mechanisms in a move away from the traditional *caveat emptor* relationship between banks and their customers. These include powers for consumer bodies to launch 'super complaints' where they perceive market failure, an 'unfair relationships' test for consumer credit and the Financial Services Authority's (FSA's) 'Treating Customers Fairly' (TCF) initiative, as well as the requirements of the Consumer Protection from Unfair Trading Regulations (CPRs);
- e. a series of reviews and additions to the Banking Code, Business Banking Code and Guidance; and
- f. European legislation to protect consumers when making 'distance sales' and 'e-commerce' transactions in an increasingly electronic age where transactions can be completed hundreds if not thousands of miles apart.

This list is not exhaustive but serves to show how much regulatory change the industry has had to face in a comparatively short space of time.

Notwithstanding the regulatory changes that have already been made and those under consideration, banks and consumers in the UK continue to face a confusing local regulatory situation. The jigsaw of regulators, with a focus in the retail space, have differing roles and responsibilities. There is, therefore, a complex matrix of authorities, each responsible for the monitoring and enforcement of different aspects of retail financial services, that is difficult to navigate and exposes an unintended consequence of regulatory inconsistency and volatility.

It is necessary, therefore, to address this lack of coherence. In a wider sense, it would assist the industry's ability to meet the public policy requirements of providing simple low cost mass market financial services products, encouraging greater engagement with and understanding of the implications of using financial services.

Pivotal, the certainty of a more stable, transparent and efficient regulatory regime creates the right environment in which the banks' ability to compete with each other will be enhanced rather than constrained.

### **Better Supervision and Enforcement**

The retail banking industry has long held concerns on the fragmentation of the regulatory framework.

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<sup>1</sup> Mortgage Conduct of Business Sourcebook introduced in October 2004 replaced *The Mortgage Code*, self-regulated industry guidance.

### The Consumer Confusion

For a customer who wants a personal current account with an overdraft:

- i) The deposit-taking activities are technically the responsibility of the FSA;
- ii) But are delegated to the Banking Code Standards Board (BCSB) through the Banking Code;
- iii) Who monitor and enforce transparency requirements determined by the OFT;
- iv) Whereas the Advertising Standards Authority (ASA) would monitor any advertising;
- v) And OFT and FSA share responsibility for ensuring contract terms are fair;
- vi) Which also sets out the requirements for the credit assessment and underwriting decision to provide the overdraft;
- vii) But where data is analysed in the underwriting process, data governance is the responsibility of the Information Commissioner's Office (ICO);
- viii) Although the OFT, through the Consumer Credit Act (CCA), is responsible for the actual provision of the overdraft if the customer chooses to draw it down;
- ix) However, if the consumer gets into financial difficulties, the debt solution agreed might be regulated by, for example, the OFT, HM Courts or the Insolvency Service.

Retail banking activities are regulated partly by the FSA as the prudential regulator of the bank and lead regulator for deposit taking, savings, investment, insurance and some credit (typically home loan activities); partly by the OFT in respect of credit; and the more detailed standards governing day-to-day activities such as deposit taking, savings accounts and how an individual switches from one bank to another are set out in the industry-generated Banking Code supervised by the BCSB. The Financial Ombudsman Service (FOS) is open to all retail customers, and, whilst not strictly a regulator, is an important part of the retail regulatory piece given that its decisions can have a significant influence on how a bank - or indeed another financial service provider - does its business.

Co-ordination and stability is clearly beneficial both for consumers and for the industry. Clearly policy changes are necessary, as is an attitude of practical co-operation rather than the boundary demarcation that has so often coloured this debate.

The industry believes that taking these suggestions on board will ensure the long term provision of high quality and innovative products for consumers within a strong and protective framework. Consumers will know where they stand, as will the industry.

### **A Safe and Sound System - Clear and unequivocal primary/secondary legislation**

*Rigorous application of HM Government's Better Regulation Principles to new legislation and good practice guidance to ensure that any unintended regulatory consequences are avoided*

This thinking has already been shared informally with the BERR Better Regulation team<sup>2</sup>.

The FSA sets out its own principles of good regulation as:

- Efficiency and economy – a responsibility placed on the FSA.
- Role of management – the responsibilities of the senior managements of firms.

<sup>2</sup> BBA response to the BERR Consumer Law Review: Call for Evidence.

- Proportionality – the restrictions that the FSA imposes on industry must be proportionate to the benefits that are expected.
- Innovation – the desirability for facilitating innovation in connection with FSA-regulated activities.
- International character – a desirability for maintaining the competitive position of the UK in an international context.
- Competition – the need to (a) minimise the adverse effect on competition that may arise from FSA activities and (b) to facilitate competition between the firms that the FSA regulates.

The Department for Business Enterprise and Regulatory Reform (BERR) has recently published its own guidelines targeted at regulators in general:

- Regulators should provide general information, advice and guidance to make it easier for regulated entities to understand and meet their regulatory obligations.
- Regulators should involve regulated entities in developing both the content and style of regulatory guidance.
- When offering compliance advice, regulators should distinguish between statutory requirements and advice or guidance aimed at improvements above minimum standards. Advice should be confirmed in writing, if requested.
- Regulators should provide the appropriate means to ensure that regulated entities can reasonably seek and access advice from the regulator without directly triggering an enforcement action.

These cannons of better regulation should be combined and applied in conjunction with a rigorous regulatory impact assessment and detailed cost benefit analysis to ensure that any changes to regulation have been thoroughly tested before application.

Amplification of these industry requirements results in:

**A safe and sound system that promotes stability** – in order to provide this, the following are required: clear responsibilities for regulators, agreed interpretation of the standards required, consistency and coherence in the application of regulatory requirements and high quality monitoring. Financial institutions require agreed, transparent and more robust industry-level standards, setting out the minimum requirements that they need to meet in their interaction with customers. They need coherence across regulators and formalised recognition of the relevant bodies and codes involved.

**Fairness to consumers** – consumers have a right to fair treatment and the provision of products that meet their needs in a way that is fair and comprehensible. Consumer fairness is brought about by a combination of regulatory requirements and through assessing the outcomes of the transactions consumers make against their initial expectations. Consumers have a right to know what they can expect when purchasing a financial product or a financial service from an institution. Consumers also need to know what is expected of them.

**A capacity for innovation** – innovation is currently at risk of being constrained as an unintended consequence of constant legal and regulatory change. New products are not being developed and brought to market as quickly as they could be. This is (a) because resources are constrained by mandatory change and (b) due to a lack of certainty in the framework. The standards of five years ago are not the standards of today - and the standards five years hence may well be different again.

However, if the complaints mechanism – of which the industry is fully supportive – judges complaints in respect of industry actions that took place five years ago against today's standards, then this brings in a retrospective element, the consequences of which have potential both to price out innovation particularly where it relates to the provision of straight forward products for the mass market.

**International competitiveness** – much effort has been placed on creating a single market for financial services by the European authorities and their attention continues to be focused on the retail agenda. Many retail services can already be transmitted across borders and, as EU initiatives progress, opportunities are anticipated to increase substantially. For the UK to be successful in this new business requires the implementation of EU requirements in a proportionate manner, similar to that of other EU countries and to provide the industry with a regulatory framework that promotes financial stability.

### *Fair Play Mechanisms*

Another area where the different approach to rule making has created a divergence in outcome has been through the growth of 'fair play' measures. The FSA has – through its statutory principles and its more principle-based approach – developed a requirement for firms to treat customers fairly, expanded through six desired outcomes. These apply at different stages and to different aspects of a bank/customer relationship. The FSA also periodically reviews the application of the Unfair Terms in Consumer Contracts Regulations (UTCCR), which are 'copied out' from EU legislation and are more prescriptive in nature. By making these reviews the FSA seeks to ensure that its rules – and business behaviour – are compliant with these requirements.

The OFT, whose role is one of enforcement only, takes a consistently more prescriptive line through UTCCR and the Consumer Protection from Unfair Trading Regulations (2008) (CPRs) . The 'copy out' of the European legislation however needs guidance to explain the text in the UK context and whilst the Banking Code covers some important guidance areas; it cannot cover all areas and is, in any event, not binding.

As an alternative dispute resolution mechanism, FOS is required to consider what would have been fair and reasonable in all the circumstances of a case and, as a result, defines fairness on an ad hoc basis. While it is not bound by precedent, it can in turn set precedents elsewhere, which override the understood interpretation of the FSA rules of that time. This might conflict with their own earlier decisions and other regulators (e.g. FOS can and does take today's rules and apply them to historic situations; it can make conflicting decisions; it can override industry/FSA agreements such as mortgage exit fees and with 'time bar red letters').

Importantly, the Fairness Commitment to consumers in the 2008 edition of the Banking Code is the first consistent approach to fairness agreed by all the regulators. This commitment highlights a number of actions consumers can expect in their day-to-day dealings with their bank.

### **Customer responsibilities**

In his speech to the Financial Services Forum on 9 February 2006, the former FSA Chairman, Sir Callum McCarthy set out what caveat emptor should now mean in the retail market for financial services. The FSA is shortly expected to issue a discussion document on consumer responsibilities. Whilst there are limits in the current *Treating Customers Fairly* space, consumer rights should also be matched with consumer responsibilities - this is in the interests of consumers and must be clearly defined and well communicated.

Whilst there is a well-recognised imbalance in favour of consumers between the responsibilities of firms and their customers, an environment in which consumers are no longer required to weigh up the reasonableness of their financial decisions is evidently detrimental.

To continue to relieve consumers of the consequences of their actions would lead to inappropriate consumer decisions and risk taking. Firms in search of legal certainty are already incurring excessive costs by being extra careful in trying to protect themselves against future claims and/or regulatory action; these costs eventually get passed down to consumers.

In order for the relationship between banks and customers to work most effectively, customers should take some actions such as:

- Taking the time to read documents before they sign them;
- Be honest and divulge all relevant information when applying for financial products or services;
- Read and reflect on communications received;
- Transact responsibly – i.e. only what they can comfortably afford;
- Inform their banks/financial providers of changing circumstances.

Additionally, consumers might be encouraged to:

- Proactively educate themselves to be generally more financially aware;
- Review their circumstances periodically to ensure that the financial product or service taken is still appropriate for their lifestyle;
- Be more security aware/conscious to minimise the risk of fraud.

### **Readily accessible dispute resolution role**

We support the aims of the use of an Alternative Dispute Resolution (ADR) mechanism. However, whilst strictly not a regulator, banks and other financial services firms frequently alter their practices in response to FOS decisions. FOS has an overarching responsibility for the dispute resolution mechanism and its sweeping mandate allows it to consider what is fair and reasonable in all circumstances extending beyond legislation. Its scope extends to personal customers and small businesses (which are defined as businesses with a turnover of less than £1m).

The industry's relationship with the FOS can present problems. Whilst FOS argues that the industry may not engage with them sufficiently early as an issue develops, there are equal concerns in the industry about the lack of consistency in FOS decisions and a perception that the FOS does not always act as a balanced alternative dispute resolution service.

Whilst FOS is set up to operate on a case by case basis, taking into account all relevant circumstances, there are a growing number of instances where the complaint addressed by the FOS had either a more generic application or where there were clearly different interpretations (by the industry and the FOS) of the standards that were required at the time that the product or service was sold.

The 'wider implications' framework was put in place with the intention that where a complaint or set of complaints being investigated by FOS has wider implications either for a number of consumers, a financial entity or for a section of the industry, then this would be referred to the FSA for investigation and consultation. In practice this has seldom happened - the process is not one that is transparent and open - FOS decisions have sometimes resulted in extensive changes to how firms apply the

FSA rules, rather than such changes being subject to the consultative requirements (including cost benefit assessments placed on the FSA by the Financial Services and Markets Act).

The Hunt Review of FOS published last year made a number of recommendations in this respect. These include:

- The need for a mechanism to establish common interpretations by FOS and the FSA, particularly in subjective areas such as determining what is fair in the TCF area.
- The requirement for greater coherence of FOS adjudications and decisions and a greater transparency of outcomes, therefore improving consistency.

Implementing the Hunt Review is of very considerable significance. Taken together, the recommendations that it contains, minimises outlier decisions being made by FOS and reduces retrospection by binding the FOS into agreeing in advance the way in which the standards placed upon the industry by the FSA are subsequently interpreted by them when disputes arise.

## **Conclusion**

The BBA believes that for banking matters, considering all aspects of a banking relationship, clearer legislation and regulatory stability will enable banks to develop new products within a stable framework. We believe that now is the opportunity to take forward a considered discussion about how best to tackle the future regulation of retail banking.

## **Self-regulation**

The discussion paper and the additional economics paper provide a useful analysis of the pros and cons of self-regulation, as well as considering the circumstances under which self-regulation may be suitable.

1. In principle, we are generally supportive of the idea of self-regulation. However, in practice, we are now acutely aware that self-regulation is increasingly considered as an 'anomaly' in financial services regulation, particularly in the context of the current economic crisis.
2. Self-regulation has traditionally been largely successful and has had a big role to play in delivering better consumer protection, but it is now difficult to envisage self-regulation having an even greater role to play, particularly in financial services, which has recently come under more legislative and regulatory scrutiny.
3. It is difficult to envisage what further benefits that self-regulation would provide, in addition to the protection consumers already receive through legislative and regulatory interventions. However, an industry code of conduct/practice or some form of industry guidance can and does provide additional benefits where:
  - i. it fills the gaps or loopholes in legislations;
  - ii. it goes beyond existing legislative requirements;
  - iii. it clarifies any grey areas or requirements that are only 'implied' in legislation;
  - iv. the key or main provisions that need to be adhered to are all in one place.
4. We note that, where there is legislative oversight or backing, the OFT refers to this as 'co-regulation' on the range of the self-regulatory spectrum. However, consumer protection legislation in the UK is fragmented across numerous statutes and responsibility for regulation

and enforcement lies with various different bodies resulting in much overlap. The current fragmented regulatory landscape causes overlaps between regulators and enforcers. We would classify this as 'shared-regulation', which is characterised by inconsistency in interpretation, not least by the regulators, and confusion regarding application by all parties concerned, including businesses, consumers and regulators. Businesses are then susceptible to different interpretations of similar requirements by various regulators and this poses the risk of double jeopardy.

5. We note that the OFT has to ensure that its limited resources are used efficiently and, whilst self-regulation and industry-led compliance may appear a cost-effective model, we do not think this should allow the OFT to transfer its enforcement responsibility onto the industry. For self-regulation to work effectively, an adequate and appropriate governance structure needs to be set in place. However, it should be noted that what regulators or consumer bodies may want in terms of regulation is not necessarily the same as what consumers' want or require in terms of protection.
6. We believe that a good regulatory model would display the following key attributes:
  - Better supervision and enforcement;
  - A safe and sound system - clear and unequivocal primary/secondary legislation;
    - (i) Rigorous application of HM Government's Better Regulation Principles to all new legislation and good practice guidance would ensure that any unintended legislative consequences are avoided. The layering of legislation introduces complexity and confusion for businesses, consumers and regulators alike;
    - (ii) Legal loopholes would be closed;
    - (iii) Existing 'grey areas' would be addressed. Existing grey areas of legislation are potential future loopholes and a review of areas open to interpretation would be a welcome preventative measure;
    - (iv) No 'gold plating' - implementation of EU legislation that is consistent with all EU member states;
  - Customer responsibilities, including; reading documentation – and ask if not sure, provision of accurate information, self-review of circumstances periodically and give early advice of changing circumstances; and
  - Readily accessible dispute resolution role.

We have already elaborated on these points above.

7. We would support a system that adopts better regulation principles recommended in the Hampton Review, for more effective regulatory inspections and enforcement. This would involve strict regulatory adherence to better regulation principles, including clear and unambiguous rules and regulations. For such a kind of scheme to work a clear Memorandum of Understanding (MoU) would need to be established between relevant bodies to ensure consistency, reduce overlap and the risk of double jeopardy. A lead regulator principle must be agreed and established and the arrangements to be subject to regular monitoring.
8. A risk-based approach to regulation, where attention is focused on problem areas and high-risk activity would help, rather than imposing prescriptive requirements on all complying businesses. However, our concern about a self-regulatory model is that it is ultimately voluntary and that membership/participation is not mandatory, thereby creating an artificial division within a particular industry and any subsequent regulatory changes or enforcement powers would apply only to the members of the body which sponsors the self-regulatory

consumer code. This would create a two-tier market structure and facilitate competitive tensions. A recent example of this was the well publicised debate around transparent pricing within the travel industry, where the OFT worked with The Travel Association (ABTA) in 2007 on misleading pricing of holidays, which resulted in ABTA requiring its members to address the issue or face action under the Code of Conduct, but the OFT was less effective in encouraging the low-cost or 'no frills' airlines industry to adopt similar transparent pricing, ultimately leading ABTA to withdraw from OFT's Consumer Codes Approval Scheme (CCAS).

9. We note that the OFT's Consumer Codes Approval Scheme (CCAS) was set up a number of years ago, as an initiative for business sectors to propose self-regulatory arrangements to the OFT for approval and this is currently being developed to form a mechanism for 'established means' under the CPRs through 'compliance partnerships'. We also note that since the launch of CCAS, there are currently only 8 bodies or 'sponsors' with approved consumer codes and a further 6 more working towards completion (stage one completed). We also note that The Travel Association (ABTA) has since withdrawn from CCAS and, therefore, hold reservations about the effectiveness of any proposed new self-regulatory model, particularly in complex markets like financial services.

### **Industry-led compliance**

However, we welcome the OFT's proposal to work more closely with stakeholders and actively engage with businesses and trade associations on self regulation, governance and compliance. To ensure that this engagement is reflected in the OFT's policies and procedures, flexible and proportionate enforcement work, we make the following suggestions to help reduce unnecessary burdens on businesses and to help encourage industry-led compliance:

#### Minimising regulatory burdens on business

The current regulatory framework is particularly burdensome for businesses on:

- information provision requirements;
- the requirement for businesses to argue the case for no need of new regulations, rather than regulators to justify its reasons for regulation providing relevant evidence, appropriate impact analysis and cost-benefit review;
- the cost of implementing regulatory changes and the associated cost of changes in procedures and systems.

A lot of regulatory changes are forced through relatively quickly, for almost immediate implementation. Regulators do not always appreciate the different practical scenarios businesses face and do not always allow adequate time for those changes to be made or to be bedded-in. For instance, allowing depletion of current printed material/stock and waiting until the next print-run for changes to be made. Changes lead to uncertainty and confusion for both businesses and consumers for a period of time. This not only affects current business operations but also stifles innovation.

Strict regulatory adherence to better regulation principles should include no retrospection, active consideration to sunset legislation and/or review periods coupled with a bedding in/implementation period where regulatory change can only be made under certain circumstances.

Another way to help reduce the burden would be to align UK consumer law with EU consumer protection legislation to ensure consistency and reduce overlap. Given the level of current EU prescription, particularly in the area of consumer protection, UK regulators should refrain from the practice of 'gold-plating' EU legislation. Gold plating is where there are additional requirements in the UK compared with our fellow EU countries. This can arise as a result of:

- bringing in requirements earlier than elsewhere;
- interpreting the requirements differently;
- enforcing the requirements with zeal; and
- adding extra requirements.

As well as working with the European Commission (EC) in its review of the key EU directives that make up the 'Consumer Acquis', including the Consumer Rights Directive published in October 2008, we would encourage the OFT to work with BERR, particularly on the Consumer Law Review to ensure harmonisation of consumer policy and protection in the UK.

#### Reducing information provision requirements

Information provision requirements on businesses impose large amounts of information to be provided to consumers, most of which they do not read, some of it overly complex and difficult for them to understand. Examples of excessive and/or burdensome legislative requirements in banking are:

- provision of complex Annual Percentage Rate (APR) information in credit agreements;
- failure to give required information can invalidate credit agreements;
- the Distance Marketing Regulations require warning potential customers that additional taxes may be payable, even when it is unlikely any will fall due;
- the Unfair Commercial Practices Directive (UCPD), implemented through CPRs, makes failure to give any required information a 'misleading omission'; and
- the Consumer Credit Directive (CCD), in contrast to the Consumer Credit Act (CCA), would require full information to be provided pre-contract rather than in the credit agreement.

Too much information can be confusing and detrimental to consumers. Generally, consumers only need more information when there are problems, for example, about how to make a complaint. It would be helpful for businesses if regulators could draw distinction between necessary information and useful further information. Further information could instead be sign-posted, referring consumers to websites or other sources of information.

Information provision needs to be better targeted. 'Summary boxes' within financial services, which came into force from October 2008 under the Banking Code requirements, is a good example of the provision of specific information that all consumers should be aware of. However, regulators usually impose additional requirements, which generally cause unnecessary complication.

Consistent terms and definitions should be adopted for ease of understanding. Plain language should be used as far as is possible, to maintain clarity, and technical and legalistic terms must be kept to an absolute minimum. This would help reduce the potential for confusion by businesses, consumers and regulators alike. Wherever possible, consumers should be given information in plain language, although regulators must appreciate that some technical and/or legal terms cannot always be simplified.

### Treating all customers fairly

Our members are required to treat all customers fairly, under the Banking Code requirements, FSA's Treating Customers Fairly initiative, as well as various other legislations and regulations. Current legal protections adequately address vulnerable consumers and provide protection for the physically or mentally incapacitated, the poor and the financially excluded.

Furthermore, BBA are actively engaged with members to identify and implement initiatives to assist consumers in financial difficulty, which include flagging accounts, monitoring unusual spending patterns and treating those customers sympathetically and positively. We also support the FSA initiative to improve financial capability, through the Money Guidance scheme, following from the recent Thoresen Review of Generic Financial Advice.

It must be remembered that all consumers are different and not all businesses can be expected to tailor their processes to suit each individual. It is therefore important that consumer protection measures continue to use the concept of the 'average consumer', such as defined under the CPRs, so that firms are able to aim their approach at an achievable middle-ground.

There are a number of 'fairness' related regulations which could be simplified by replacement with a single Treating Customers Fairly principle, as per financial services. The advantage would be to give businesses an overarching principle to achieve rather than a plethora of requirements to comply with. Ultimately, the results should be the same. Any principles approach must have adequate guidance so that firms can be confident in their approach and confident that they will not face retrospective regulation in the light of hindsight.

### Industry developed codes of conduct, practice or guidance

Guidance could take the form of detailed, consumer accessible industry developed codes of practice containing minimum standards, whilst remaining flexible and user driven. We recommend acceptance of long-standing and recognised guidance, proposed and supported by industry, as 'established means' to determine fair practices. One such example would be the Banking Code, a long-established and reputable voluntary code with wide industry support from members, which covers areas where there has been little or no such regulatory provision previously. Furthermore, adherence to the Banking Code by member firms is monitored by an independent organisation, the Banking Code Standards Board (BCSB).

We support the idea of a principles-based approach to consumer law, with a set of high-level general principles, supported by additional guidance. However, the role and status of guidance would need to be fully debated, with the concern that it could amount to regulation by the back door and be susceptible to frequent changes by designated bodies responsible for the guidance, without adequate cost-benefit or impact analysis. We support adoption of the better regulation principles recommended in the Hampton Review, for more effective regulatory inspections and enforcement. Strict regulatory adherence to better regulation principles includes no retrospection and clear and unambiguous rules and regulations. Consumer responsibilities would also need to be established.

Recognition of codes of practice, proposed and supported by industry, as industry guidance to act as minimum standards would help in reducing legislation and implementing high-level general principles such as 'fairness', especially if recognised as 'established means' to determine fair practices. In addition, this would allow full implementation of risk-based-regulation, in line with the principles-based objectives, to tackle high-risk business sectors and activities that pose the greatest consumer detriment, allowing complying businesses to reduce the burden and cost of further regulation.

However, there are some potential problems and challenges with principles-based-regulation (PBR):

- Consistency in decision-making. It would be difficult to identify outcomes under PBR and design credible evaluation for them.
- 'Regulation in hindsight' would be a problem for businesses.
- Constant flow of informal guidance at an inappropriate high level would introduce new regulatory requirements "*via the backdoor*", not subject to formal consultation or cost benefit review.

For successful enablement of PBR, businesses would require:

- PBR material to be clearly sign-posted.
- Regulators would need to adopt an '*open door*' policy, with senior and supervisory staff prepared to convey views. The approach should be based on industry sectors, to ensure that regulatory teams are knowledgeable and easy to do business with.
- A range of acceptable approaches that firms could potentially take (subject to the 'reasonableness' condition) in order to achieve '*safe harbour*', as opposed to taking the '*best practice*' approach, as a measure of '*minimum*' acceptability.
- Examples of case studies of minimum standards, for meeting the principle-based objectives.

However, some principles alone are insufficient in regulation and should be complemented by minimum standards. Trade-offs between rules and PBR will of course exist; uniformity versus variety and certainty versus flexibility. However, simplicity and harmonisation of *minimum* standards is the least costly regime for business. Advantages include:

- Simplification and the removal of the need to run parallel procedures to serve the same purpose in different jurisdictions.
- The sector bodies would recommend minimum standards to the regulator for endorsement.
- Variety offers a safety valve where regulation is onerous and flexibility offers options where regulation is lacking.
- Flexibility provides room for competitive manoeuvre within minimum provisions and may help adjustment to changing market practices and technology.
- Standards should require a short, clear description of what the product is, who it is aimed at, the risk and the charges.
- Consumer responsibilities need to be established. For example, consumers should be willing to sign "I have read and understood" statements.
- Firms complying with the standards would have safe harbour from prosecution, although individual cases would still have access to Alternative Dispute Resolution.

### Regulatory sanctions

We would welcome regulators being given access to new civil sanctions, intended as alternatives to criminal prosecution and to allow regulators to be more consistent, flexible and proportionate in their enforcement work. The criminal enforcement sanctions in consumer protection legislation, even for minor offences, are unduly onerous and disproportionate. This highlights the need for a different approach to sanctions in different sectors and that civil sanctions would be more appropriate than criminal enforcement in certain circumstances. Criminal sanctions should be reserved for deliberate or reckless contraventions that foreseeably cause significant actual detriment, such as fraud. Otherwise, civil sanctions should be used where appropriate for more proportionate sanctions.

## Summary

As the FSA assumes responsibility for regulation of retail banking activities currently under the Banking Code from 1 November 2009, and we seek an appropriate solution that does not leave credit orphaned, we outline the 3 key points which we believe characterise a successful regulatory regime:

- The development of secure, agreed minimum standards for banks' retail activities, which provides adequate 'safe-harbours' for industry.
- A framework for a closer working relationship between regulators/enforcers - particularly between the FSA, OFT and FOS - for clarifying, interpreting and agreeing the standards required to meet important principles such as fairness to customers, including customer responsibilities.
- Regulation should be without hindsight, as businesses should not be expected to review past business, which adhered to the good industry practice in force at the time of the sale, in line with current requirements. Also, FOS to revert to its dispute resolution role – given the extent of legislative change, banks should be confident that FOS will judge complaints against the standards at the time of the sale.

We are keen to continue our engagement with the OFT in these areas of interest to our membership and I hope that you will find our comments on self-regulation and industry-led compliance helpful.

Yours sincerely,

**Eric Leenders**  
*Executive Director*

