

A fair deal for consumers

One of our objectives is to secure an appropriate degree of consumer protection. To achieve this, we authorise firms and approve individuals, set standards, monitor compliance and enforce the rules.

Authorisation

Consumers need to have confidence that they are dealing with authorised individuals and firms. Authorisation by the FSA provides a baseline standard for firms (which must show, amongst other things, that they have adequate financial resources) and individuals (who have to be fit and proper to carry out their roles). Detailed figures on authorisation are contained in Appendix 11.

In over 80 cases, applications for individual approval were refused or withdrawn while under investigation this year.

Authorised firms are listed on the Register on our website. It gives the name and full contact details for all authorised firms and in future it will include other material such as a firm's disciplinary record. A simpler version of the Register, the FSA Firm Check Service, is available on the consumer section of the website. We encourage consumers to check the Register to ensure that their firm or provider is authorised and has the necessary permissions to do business.

Policing the perimeter

As under the previous regimes, FSMA establishes boundaries between activities that require authorisation and those that do not. We detect unauthorised activity through preliminary enquiries. We also establish if there have been breaches of the financial promotion regime and the restrictions on persons making false claims to be authorised. Cases involving possible breaches may be subject to more detailed investigation. We take legal action against offenders and can prohibit unfit individuals from taking jobs with authorised firms.

During the year, 581 of these types of cases were opened. Of these, 413 were closed after preliminary enquiries. Of these closed cases, 98 were dealt with by warning, 13 were referred to other external agencies and 302 were kept for intelligence purposes. Of the remaining 168 cases, 81 were the subject of ongoing preliminary enquiries and 87 were referred for more formal investigation.

An example of a case concluded this year is shown on the next page.

Treating customers fairly

Our rules set clear standards for firms when dealing with different types of consumers. Retail consumers, who are less experienced than professional investors, benefit from the greatest protection under our rules.

Our rules focus mainly on what consumers are told whilst they are choosing products and at the point they buy. We are increasingly concentrating on what happens after the point of sale, as unfairness can also arise there. In June 2001 we published the results of our theme project 'Treating Customers Fairly After the Point of Sale'. We found that:

- some products and information are difficult for consumers to understand;
- customers are not kept appropriately informed after the point of sale;
- products and firms don't always deliver what consumers are led to expect;
- customers are discouraged from changing products and providers; and
- customers cannot always get their complaints dealt with fairly.

We have worked in a number of ways to help address these issues through our supervision of firms, focusing on specific areas where problems can arise and by looking to future developments in policy to support the fairness agenda.

Fairness: marketing and advertising

Firms spent £1.4 billion on advertising and promotion in 2001, resulting in 103 million communications with consumers. These financial promotions play a significant role in the decisions

Unauthorised deposit taking

Doreen Steggles ran an unauthorised deposit taking scheme that continued until the FSA obtained injunctions against her in 1998. £3 million had been deposited in the scheme and, despite some repayment of deposits and interest, the deficit amounted to some £3.5 million. The courts imposed a custodial sentence totalling three and a half years.

Supervision: consumer protection

A major provider of financial services was offering high-yield derivative-based products to consumers through its high street network. Our monitoring suggested that consumers' risk profile was not being adequately explored at the point of sale. The firm was told to undertake a large retrospective business review, providing restitution where appropriate. We are also examining the firm's internal procedures for product development and approval to try and identify where weaknesses may have existed, to reduce the risk of a repeat.

Supervision: financial promotions

We identified a problem with a financial promotion by IFAs which included potentially misleading references about the product and the nature of the relationship with the wholesale provider, a major high street firm. Besides acting swiftly to ensure that the problems were rectified by the IFAs, we worked closely with the wholesale provider to establish their responsibilities and how they could exercise greater control over product literature issued to retail consumers.

consumers take, so advertisements need to be clear, fair and not misleading. Our proactive monitoring resulted in around 100 cases against firms. We focused on areas of particular risk, for example on ISAs during the ISA season and on the use of past performance data. We also dealt with more than 360 complaints from consumers, most resulting in the advertisements being changed or withdrawn.

We undertook a major review of our approach to promotions during the year. Most firms meet the spirit of the rules, but action is needed to help tackle unfair practices like making unrealistic claims and burying important information in

small print. We have developed a series of measures which should help highlight good and bad practice and encourage consumers to raise potentially unfair advertisements with us. The report of our Past Performance Task Force was published in September. We are following this up by proposing a second phase of action on the use of past performance data in financial promotions. Our aim is to secure a more balanced presentation of the benefits and the risks of a product, rather than a simple description of the risks in the small print. Our proposals on past performance will be developed on the basis of wider consultation with the industry.

Disclosure

We have learned a great deal through our consumer research about the way consumers use the information they are given at the point they buy a product. We are currently working on proposals for a new document to replace ‘Key Features’, designed to encourage consumers to think about whether the product on offer is right for them and represents good value for money. Our objective is to help consumers make informed decisions about the products that they buy. This work has also helped us identify some of the common areas where jargon is used and consequently how ‘reason why’ letters – the other important element of point of sale disclosure – might be improved. We will be publishing our views on reforming disclosure later this year.

We are also in the early stages of work to consider the standard of information consumers receive once they have bought a product, such as annual statements. In the interests of fairness such material should be clear and consistent, enabling consumers to understand, for example, what returns they should expect. Better information would also help consumers decide whether to switch providers or move to new products as they are developed.

We worked on fairness issues where there were concerns about specific products including annuities, with-profits policies and endowments.

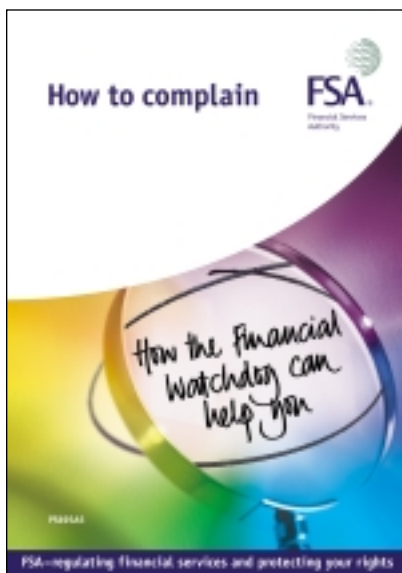
- We consulted on changes to disclosure rules to strengthen the position of consumers buying annuities. Firms will have to tell policyholders that they can buy an annuity on the open market, rather than from their pensions company. Proposed new guidance also encourages firms to include an FSA Factsheet in their communications with consumers on this topic, which contains impartial information on their annuity options. We believe these proposals empower consumers to make up their own minds and promote competition, consumer choice and fairness.

- We also consulted on new disclosure rules that will require firms to tell consumers that they can trade their endowment on the secondary market as an alternative to surrendering it.
- We reviewed key aspects of with-profits policies, particularly fairness, transparency, governance and discretion. The review has considered how to increase consumers’ understanding of the way with-profits funds are run and increase confidence in how directors will meet, and have met, their obligations to treat consumers fairly. We have consulted widely on issues surrounding with-profits policies and will publish a final report on our work.

Complaints

It is important that consumers can get their complaints dealt with fairly. We have introduced new rules in the complaints sourcebook that should help ensure that consumers have proper access to complaints procedures. Firms will have to report to us on complaints handling and we will monitor whether they treat consumers fairly when handling complaints.

FSMA establishes two independent bodies for providing redress to consumers. The Financial Ombudsman Services (FOS) resolves consumer complaints against firms – and it shares information with us to help identify where major problems may be arising within firms. The Financial Services Compensation Scheme (FSCS) provides compensation for consumers where authorised firms are unable to meet their liabilities. FOS and FSCS publish separate Annual Reports describing their work.



The FSA produces a wide range of information to help consumers, including information on how to complain.

Handling of customer complaints

In November 2001 GL&P Plc (formerly Gan Life and Pensions Limited) was fined £1.4 million by the PIA for failure to deal fairly and responsibly with customer complaints. The failures took place prior to the company's acquisition by Life Assurance Holding Corporation (LAHC) in March 1998.

The PIA found failures in GL&P's standard of complaints handling between April 1988 and March 1998. Complaints handling was compromised following a deliberate change of policy aimed at minimising the costs arising from complaints. The company instructed handlers to focus only on the specific complaint being made rather than assessing the case as a whole. Even where financial advisers who advised on the original sale appeared to corroborate the client's complaint, the company generally failed to disclose this to complainants and refused complaints. The company failed to compile management information that might have identified trends and it had no written procedure for handling complaints. The number of cases referred to the PIA Ombudsman was manipulated to avoid attracting attention.

During the period in question three types of GL&P plan had been sold as ten-year plans when they were in fact long-term (25 years) or whole-of-life plans. Following its acquisition of the business LAHC worked in an open and co-operative manner with the regulator and assisted in resolving all outstanding issues and ensuring that no investors suffered harm.



Unfair Terms in Consumer Contracts

During the year we took on powers under the Unfair Terms in Consumer Contracts Regulations. These enable us to challenge a firm which is using a standard contract term we consider potentially unfair to consumers. We have taken over responsibility for applying these Regulations to financial services from the Office of Fair Trading (though the OFT continues to cover personal loans and credit cards). The OFT have handed relevant outstanding cases on to us to take forward, and we are also considering new cases sent to us by the public. In addition to handling individual complaints, we will be undertaking proactive reviews of contracts for certain types of product. The first of these reviews focused on with-profits policies, and the results were published in a Paper 'Discretion and Fairness in With-profits Policies'.

By using our powers under the Regulations we can help to improve the content and clarity of contracts in financial services. This helps achieve a fair deal for consumers and also helps them get a clearer idea of the services, rights and obligations in the terms and conditions they are signing up to.

Redress: mortgage endowments

We have continued work on past sales of mortgage endowments. Our role is to ensure that consumers receive appropriate information from firms. This should help them to decide whether they need to take action and make them aware of how to complain if they believe they may have been mis-sold. We also investigate instances of systemic mis-selling by individual firms and seek redress for consumers where this has occurred. During the year we have also focused on:

- examining firms with a high proportion of 'red' letters (i.e. cases predicting a material shortfall in the policy pay-out) to check for previously undiscovered issues or problems;

- negotiating redress where firms had used Lautro* charges to set their premiums, and where redress has not been paid;
- monitoring firms' handling of complaints where the consumer alleged mis-selling. We take action where complaints have not been handled fairly;
- investigating individual firms where there may have been systemic mis-selling;
- negotiating redress where firms used unduly optimistic growth rates when setting premiums, without warning consumers of extra degree of risk involved; and
- getting consumers the information they need. For example, an FSA Factsheet will accompany the next round of re-projection letters.

So far more than £330m has been paid out or set aside by firms for redress for mortgage endowment mis-selling.

Controls on suitability of recommendations

Winterthur Life was disciplined by the PIA for breaches that resulted in mis-selling of endowment policies. The investigation found that the firm's procedures did not ensure that suitable recommendations would be made. Specifically, a computerised system used between March 1998 and December 1999 allowed advisers to recommend mortgage endowments where they were not suitable for consumers (who had said that certainty of loan repayment at the end of the term was very important to them). There were also failures to ensure that consumers had a clear explanation of recommendations in the 'reason-why' letters they were sent and there were failures in monitoring. Around 10,000 policyholders may have been affected and the firm set aside £10 million for redress. A fine of £500,000 was imposed in September 2001.

In deciding the case, account was taken of the commitment the company demonstrated in addressing these matters. With the help of external consultants to review its mortgage endowment policies sold during the period in question the company is contacting those policyholders affected and offering redress where appropriate, including to policyholders who have surrendered their policies.

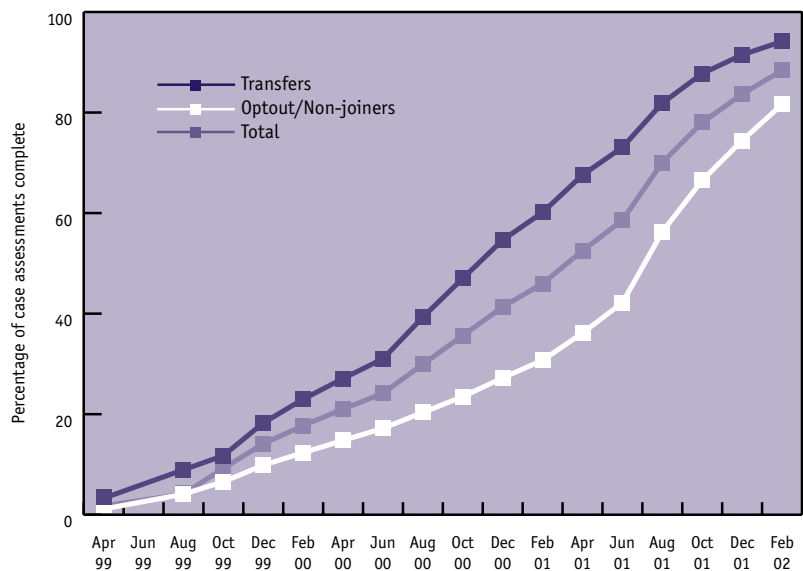
* Life Assurance and Unit Trust Regulatory Organisation

Redress: the Pensions Review

The review of personal pensions mis-selling is nearly complete. As at the end of March 2002, 91% of offers of redress had been made to consumers. Firms should have made offers in all cases by 30 June 2002. Figure 4.1 shows progress on cases being reviewed by the industry. So far redress of £9 billion has been offered to consumers.

We carry out reviews where a firm is no longer in place to do so ('departed firms') and pass cases showing a loss to the Compensation Scheme. We have completed all the cases in our original Phase 2 caseload (more than 46,000 reviews have been carried out to date). However, we already have an extra 25,000 cases, from firms that have gone out of business since 1998. We expect to receive another 15,000 cases by the time the industry review is complete, but we will not know the final total of additional departed firms' cases until the industry review is finished. Disciplinary action has been launched against a number of firms for failure to pursue the review properly. Since the beginning of the review we have taken disciplinary action against 345 firms resulting in fines in excess of £9.5 million – more than £1 million of which have been imposed during 2001/02.

Figure 4.1: Pensions Review – Percentage of industry cases complete



Major theme project: impact of an ageing population

As part of our new risk-based approach, each year we identify a small number of themes to examine in depth. These relate to issues which cut across several industry sectors or consumer categories (or both) and which affect a number of our statutory objectives. In July a new theme began to consider the effect of an ageing population on our work. The project's objectives are to:

- consider the implications of increasing life expectancy for consumers' financial needs
- identify potential risks to our objectives from particular products
- examine the implications for firms and consumers of an ageing population and increasing life expectancy; and
- identify areas where FSA intervention may be required to help ensure that consumers and financial services providers are preparing properly for these changes.

This theme's importance has been underlined by several developments since July – a report commissioned by the ABI into the savings gap; well-publicised decisions by a number of companies to close their defined benefit pension schemes; Government consultation on annuity reform; and other reviews commissioned by Government, for example by Ron Sandler and Alan Pickering.

In January we published an initial report on how consumers plan their finances and accumulate wealth. Our continuing work is geared towards two outcomes: first, that consumers are better equipped to make informed decisions when planning for, at the point of, and during retirement; and, second, that the industry takes its consumer responsibilities seriously when manufacturing, marketing and selling retirement products as well as embracing the opportunities ahead. We plan to publish a Discussion Paper in summer 2002 exploring some of these issues in more detail and making proposals for follow-up work.
