

FCA Discussion Paper on Improving Consumer Communications (DP15/5)

In July 2015, the FCA published a discussion paper exploring smarter approaches to consumer communications. The regulator acknowledges that many firms are trying to comply with expectations around transparency and information, but sets out several areas where improvement is necessary.

The FCA undertook several strands of research to support discussion paper, including a literature review; roundtable discussions with several key stakeholders; reviews of practices in other countries; and reviews of practices in other sectors, and other research initiatives. The discussion paper then examined six specific areas where there is scope for improving consumer communications:

- **Terms and conditions:** typify consumer concerns about information complexity and overload. The DP encourages the industry, working with relevant stakeholders, to focus on bringing about improvements in this area.
- **Fees and charges:** the research found that consumers are best able to assess the quality of a product or service and whether it meets their needs when they are fully informed about its key benefits and features.
- **FOS/FSCS:** there is more the industry can do to help consumers to identify who is the most appropriate person to speak to when they have a comment or query about a product or service that is not operating in line expectations.
- **General insurance common terminology:** the regulator has identified a number of issues in the general insurance market that can potentially be addressed through effective consumer information.
- **Complexity at retirement:** consumer inertia and lack of engagement are particularly prevalent when it comes to retirement planning and saving.
- **Investment advice:** even post-RDR, there is an opportunity to improve the information consumers receive about the scope and cost of investment advice services to enable them to choose a service according to needs and budget.

Next steps:

- The Discussion Paper closes on 25 September, and a feedback statement will be published later this year. The FCA use the responses to this paper, where relevant, to inform ongoing interactions with the EU and domestic regulators on disclosure issues.
- work with firms to test new ideas. The results of this testing, if effective, could inform the regulatory approach, lead to consultation on rulebook changes and could also influence our negotiating strategy when European directives are (re)negotiated.

Background

In July 2015, the FCA published a discussion paper exploring smarter approaches to consumer communications. <http://www.fca.org.uk/static/channel-page/dp-smarter-comms/dp-smarter-comms-index.html>

The regulator recognises that communications play a fundamental role in helping consumers to make informed decisions. Effective, engaging information can be a key tool in promoting effective competition to supply products and services that consumers want.

The Chartered Insurance Institute

Financial services consumer protection over the last decade has relied heavily on information to help improve competition. This has led to types of information firms should disclose to customers and the format it should take. While the FCA will continue to do this where it feels this is necessary, the regulator also recognises that information itself does not necessarily empower the consumer. We know from behavioural economics that too much information can overwhelm, confuse, distract or even deter people from making effective choices:

- behavioural biases, low levels of financial literacy and the complexity of some financial services and products can limit people's ability to take appropriate action;
- firms tend to use financial and legal jargon, which can make the materials they produce lengthy and impenetrable for the consumer; and
- in some firms, marketing material is much more consumer focused than other consumer communications
- greater transparency in firms' communications with consumers can also lead to greater efficiency for the industry, with less time spent handling complaints.

Regulatory context

When outlining how the FCA would advance its objectives, the regulator signalled that it would place considerable emphasis on greater industry transparency, in the form of clear pricing and clear information helping consumers make informed decisions. It investigated the difference between its expectations of firms and firms' understanding of what is required of them, particularly what impedes making informed decisions:

- regulatory disclosure material that does not provide consumers with the information they need in an accessible and understandable format;
- information overload and excessive use of financial and legal language that stops consumers from engaging; and
- a 'tick-box' approach to communication that is driven by uncertainty about our expectations and fear of action being taken against them

FCA expectations of firms

Firms must:

- understand and recognise the importance of communicating effectively with consumers;
- create product and service information for consumers with at least as much behaviourally informed creativity as is applied to business development, marketing and financial promotions; and
- create communications as an integral part of the product or service design process.

The FCA acknowledges that many firms are doing this, and the discussion paper conveys its support and encouragement for firms that are taking steps pursuant to this:

- writing for the consumer first and then ensuring communications are compliant, rather than the other way round
- moving away from a box-ticking approach to communication design, or the perception that communications driven by regulation are the responsibility of compliance and legal staff
- building a wider understanding of their customers' information needs and objectively considering not only what consumers actively demand to know, but also:
 - what the consumer needs to know;
 - how much they need to know; and
 - when they need to know it.

- prioritising efforts to ensure that information is effective for the intended audience and testing communications among real consumers.

FCA handbook review

Mandated disclosure is one of the regulatory solutions that regulators use to address market failures. A key work stand related to smarter consumer communications has been to consider the extent to which our disclosure requirements have been effective at empowering consumers to make informed decisions about their finances, and whether changes can be made to certain Handbook disclosure requirements to improve their effectiveness.

The FCA Handbook contains product disclosure requirements for investment products, mortgages, general insurance, banking and consumer credit products, among other specific areas. The information required to be disclosed differs depending on the complexity of the product and risk to consumer outcomes.

Some Handbook disclosure requirements stem from European Directives or Regulations, which constrain amendments solely in the name of better communications. However, there are still opportunities to improve disclosure particularly during legislative reviews.

The FCA considered whether we can change any of our non-European Handbook disclosure provisions to improve their effectiveness. We have also reviewed our Handbook rules to ensure they do not inhibit effective competition. Through this work and our discussions with firms and other regulators, we have identified sections that have not been as effective as we first envisaged in terms of informing consumers, and therefore we intend to consult on their potential deletion.

Name	Description	Issue
The ‘Consumer-Friendly Principles and Practices of Financial Management’ (CFPPFM)	Customer disclosure document setting out the firm’s approach to managing and operating its with-profits business, including its approach to setting bonus rates and smoothing and market value reductions.	Anecdotal evidence and previous reviews suggest that most consumers do not read the CFPPFM and, if they do, complex wording or superficial explanations inhibit understanding making the communication not as effective as first envisaged.
The Initial Disclosure Document (IDD)/ Combined Initial Disclosure Document (CIDD)	Guidance in COBS, MCOB and ICOBS suggests that firms can, if they wish, use a template to disclose their services and how much these cost.	The template duplicates information to consumers and firms adopt a ‘tick-box’ approach to these disclosures.
Short report	Half-yearly, post-sale disclosure produced for investors in retail authorised funds.	May not meet original aim of providing clear and focused information about the fund.

Research into smarter communications

The FCA undertook several strands of research in support of this discussion paper:

- **Literature review by Oxera Research:** this examined the broad academic literature and presents cases where changes in the disclosure regime have been evaluated and tested: what works well and what does not. Methodological tools to evaluate those changes involve both lab and field experiments, as well as ex post assessments of changes in disclosure rules. The review highlights the main themes of disclosure that apply to most products, including financial services products, including design of summary disclosure; engagement of consumers, and presentation of product information.
- **Roundtable discussions with several key stakeholders:** this revealed that all industry sectors have some awareness and common agreement around what good practice might look like, there is a real willingness to find new ideas and

solutions, and there appears to be common agreement that consumers and firms could benefit from making communications as effective as possible.

- **Review of practices in other countries:** this involved opening conversations with other financial services regulators in jurisdictions such as Australia, the US, Sweden, Denmark and Norway.
- **Review of practices in other sectors:** the FCA also gather examples in other sectors through contact with for example Ofcom, Ofgem and Ofwat - to understand the practices and developments in these sectors.
- **Other research initiatives:** the FCA took in other activities and initiatives by other organisations including the European Supervisory Authorities and the European consumer association BEUC.

The research identified a number of common behaviours among firms or perceived barriers that were limiting the development of effective communications. These included:

- firms adopting a 'risk-averse' approach to communication design, by using consumer disclosures as a risk-management tool to mitigate potential action against the firm – although little evidence was provided to suggest this had any effect
- a view that the prescriptive nature of EU and domestic legislation leads firms to produce jargon-filled and lengthy disclosures that firms can do little to improve – again no examples were given of requirements that prevented firms from considering how else or additionally to convey important information in a consumer-friendly way
- the view that the costs and operational challenges of changing existing communications outweighed the benefits
- firms treating communications about products and services as of secondary importance compared to the design of the product or service

Opportunities for change: specific issues

Terms and conditions

Terms and conditions (T&Cs) typify consumers' concerns about information complexity and overload. The DP encourages the industry, working with relevant stakeholders, to focus on bringing about improvements in this area.

Current practice:

- The FCA industry roundtables revealed a widespread belief that there is little scope to improve the accessibility of T&Cs because lengthy complex information is required by regulation.
- While it is accepted that T&Cs constitute (part of) the legal contract between the firm and the consumer, there are many cases that look as though firms use them to over-disclose information in such a way to mitigate risk of consumer action. Other firms also take the view that their obligations are met when the customer views (or clicks) their T&Cs.
- Research by BEUC also found that many provisions in T&Cs are clearly meant for third parties, such as the consumer's lawyer... relevant primarily in case of conflict'.

Scope for improvement:

- **content:** the inclusion of the core minimum information that legally must be communicated to the consumer in the contractual 'terms & conditions'. Other good practices include only including information about legislation and regulation where actually necessary or relevant, rather than as a 'just in case' compliance measure. In one example we have seen, a firm reviewed their T&Cs to ensure it included only the essential information and presented this in a way their target audience could understand and engage.

- design and delivery: firms could explore additional or alternative mechanisms for highlighting the most critical information for the consumer that might better: alert them to their rights and responsibilities, enable them to take into account materially important information, or improve their ability to avoid or minimise poor outcomes.

Fees and charges

Oxera's review found that consumers are best able to assess the quality of a product or service and whether it meets their needs when they are fully informed about its key benefits and features. The most important information for consumers to be aware of is the price or charges associated with the product or service.

Current practice:

- requiring firms to disclose price information clearly, at an appropriate time and through a suitable medium helps minimise "present bias" (when consumers ignore costs that are not in the here and now) and therefore help inattentive consumers, according to research by the FCA.
- in the general insurance sector, it is not clear whether the existing approach to providing total fee information (including additional costs to make mid-term administrative changes) effectively addresses other bias such as 'overconfidence', empowers consumers to fully consider the impact of aspects on the total cost of their insurance, hence there is little pressure on the level of fees insurers charge to make administrative changes to a policy.
- in the mortgage market, Which? highlighted concerns that a consumer's ability to compare products and to understand all associated costs is made particularly difficult by the significant number of additional fees that a consumer can incur.

Scope for improvement:

- There are a number of regulatory initiatives aimed at addressing, or seeking to address, cost transparency. This includes initiatives in the investment, consumer credit and mortgage markets. But there is more the sector can do to help consumers: appreciate the total costs they could incur; do not ignore potential additional charges that could apply to a financial product; consider all the relevant factors when shopping around
- Depending on the nature of the market and the costs, there are a number of potential ways to help present clearly the full costs associated with a product or service in the information given to consumers. These include:
 - (re)informing the consumer clearly at the point at which it becomes apparent that an additional charge may be incurred, and not exclusively at the point of sale;
 - quantifying or expressing in monetary terms where limits or caps apply;
 - for long life-cycle products including a generic timeline with payment points noted against the various stages might be a simple and easy way to present the costs consumers are expected to pay and at what point; and
 - including the cumulative impact of the charges on the value of the consumer's investment in the longer-term.

FOS/FSCS

There is more the industry can do to help consumers to identify who is the most appropriate person to speak to when they have a comment or query about a product or service that is not operating in line with their expectations, how to escalate this to the Financial Ombudsman Service (FOS), and where a product or service is potentially covered by the Financial Services Compensation Scheme (FSCS).

Current practice:

- The FOS currently receives enquiries from consumers who are not looking to have a complaint investigated, but are trying to identify what to do when they have a comment or query about a product or service that is not operating in line with their expectations.

- Typically, what matters to the consumer is the quick and effective resolution of an issue. In many cases, the most appropriate and efficient resolution could be delivered early by direct contact with the firm itself, often by frontline staff. Many ‘complaints’ are caused by misunderstandings that the business could quickly put right if the matter was brought to their attention.
- Most consumers seeking deposit recovery from the banking financial failures in 2008/9 were unaware of the existence of the FSCS. As a result, the Tripartite authorities and FSCS sought to address this via detailed disclosure rules, an FSCS consumer communication campaign, and PRA rules requiring the use of stickers and posters in branches, and the provision of key information and signposts on websites

General insurance common terminology

The regulator has identified a number of issues in the general insurance market that can potentially be addressed through effective consumer information.

Current practice

The FCA’s thematic work highlighted a number of disclosure-related challenges. These include concerns that information provided to consumers often did not help them make an informed decision. A number of shortcomings were identified where information could be insufficient, incomplete, provided at the wrong time or presented in a potentially misleading way.

- Consumers often had poor understanding of products: they made significant mistakes when asked questions about cover. Although many participants indicated they were happy with the information given, these were participants who had never had to make a claim; on review, they were surprised by their policies.
- Household and travel insurance customers who had their claims rejected were less likely to have understood or read their policy documents compared to those who had their claims paid out.
- Consumers find it difficult to compare products and the different elements of cover.
- Consumers were very driven by price, but often did not understand that different prices might reflect different levels of cover, instead assuming higher prices meant a firm was just charging more and making more profit.
- Consumers found language confusing, though the general insurance add-ons market study qualitative consumer research also highlighted that language that appeared clear could give rise to a false sense of security, if accepted at face-value without close scrutiny of ‘clauses in documentation that might, should occasion arise, cause problems subsequently’.

Scope for improvement

- For a consumer who assumes there is no difference in cover, or does not engage fully with the product sales information, the risk of purchasing something not appropriate for their needs, and therefore opening the expectations gap is significant.
- Core personal lines general insurance, such as motor or home insurance, is heavily price-focused with firms keen to appear at the top of comparison tables. However, we are concerned that this form of competition in the general insurance market does not necessarily work in the best interests of consumers if it is not supported by information that facilitates consideration of cover and quality. Our discussion paper DP15/4 explores options for introducing a market wide transparency measure to encourage competition on aspects other than price, such as product value.
- The FCA are interested in ideas for how firms could provide better explanations of key features, benefits and exclusions, which are accessible to consumers when they are making decisions.
- There are different ways of achieving this aim. One is to define single, consistent meanings for features such as courtesy car, meaning that consumers can have a clear idea that when a policy states it has such a feature, that it

will mean the same thing. Alternatively, or in addition, firms could demonstrate clearly to consumers where their cover differs from the agreed definition

Complexity at retirement

Consumer inertia and lack of engagement are particularly prevalent when it comes to retirement planning and saving. Until recent changes in the pensions landscape, choices made at retirement were typically irreversible. The need for consumers to engage has never been more acute. The pension reforms place more responsibility on individuals to make decisions about their pensions savings at retirement. They also introduce a host of new terminology in a market where complexity already deters some consumers from engaging.

Further progress is needed to improve the language used by the industry when it communicates with consumers. In FCA industry roundtables, some firms representing the life, pensions and insurance sectors acknowledged there was a lack of consistency in terminology that made it difficult for consumers to understand and compare products and their features.

The regulator welcomes and supports industry efforts to reduce jargon and to communicate with customers in a language they can understand. Drawing on the combined experience of their distinct customer bases, these organisations could for example:

- establish the most common features and technical terms directly linked to the pension and the performance of the investment that consumers need to understand and, just as importantly, those that are most commonly misunderstood
- agree a single consistent explanation for each that is a more fitting and relevant description of what it is, what it does, what it means for the consumer
- work by the National Employment Savings Trust (NEST) developed eight ‘Golden Rules’ for talking about pensions in the context of the workplace pension reforms and automatic enrolment, could provide a starting point.

NEST Golden Rules for Pensions Communications

- **Keep it real:** Use examples people can relate to and avoid abstract concepts.
- **Rights not responsibility:** Tell people what they're entitled to not what they should be doing.
- **Out with the old:** Make pensions relevant to their lives now and don't focus on the details of retirement.
- **One for all:** Make it clear automatic enrolment is happening to most workers, not just them.
- **Tell it like it is:** Present the facts and avoid 'spin'- people want to make up their own minds.
- **Give people control (even if they don't use it):** Tell people about their choices and not that everything's done for them.
- **Take people as you find them:** Give people access to information that matches their knowledge and interest.
- **Be constructive:** Tell people about solutions, not problems or scare-stories.

Investment advice

There is an opportunity to improve the information consumers receive about the scope and cost of investment advice services to enable them to choose an advice service which best meets their needs and budget.

- The Retail Distribution Review (RDR), which was implemented on 31 December 2012, was a once-in-a-generation change to make retail investment markets work better for consumers.
- Since implementation, the regulator has assessed whether the reforms are delivering the intended outcomes. Early findings were very concerning, with a large number of firms failing to provide their customers with the appropriate information about the scope of advice offered and the cost of that advice.

One solution identified was the use of labels, such as the US Environment Protection Agency's fuel efficiency label.

- the FCA consider that a variation of this label could be used by investment advisers to help consumers understand whether the advice is independent or not, and the cost of this advice.
- whether the investment advice a firm offers is independent or restricted and what this means in practice (MiFID II, due to take effect from January 2017, will require firms to inform the client whether investment advice is provided on an independent basis or not);
- as outlined in the RDR post-implementation review, the FCA’s Smaller Business Practitioner Panel is currently looking at developing proposals for a simple label as indicated below.

ABC Investment Advisers ABC Logo

At ABC Investment Advisers we offer:

Independent Advice
We will advise, make a recommendation and arrange any suitable products for you after we have assessed your needs. Our recommendation will be based on a comprehensive and fair analysis of the market.

Restricted Advice
Restricted advisers make a recommendation for you having assessed your needs but adviser will consider recommending suitable investments from a limited range of products and/or providers.

How much will our service cost?

1. Initial charges to make recommendations and arrange any suitable products:
X% on the first £100,000 of your investment, and then **Y%** on any amount over that
This is only payable if you proceed with the recommended product.

2. Ongoing charges
Gold service to monitor recommendations and products: **A%** per annum
Platinum service to monitor recommendations and products plus an annual review: **B%** per annum.

Example Costs
To set up a £50,000 investment would cost: £X,XXX (X% of £50,000).
To set up a £200,000 investment would cost: £X,XXX (X% of first £100,000 PLUS Y% of the remaining £100,000 = £X,XXX).
One year of Gold on going service on the £200,000 would cost: £X,XXX
The amount of the annual ongoing charge may increase as the fund grows

More details about our services are available in our XX document available on our website: www.XX.XX.X\XX

ABC Investment Advisers is authorised and regulated by the Financial Conduct Authority. Further details about ABC Investment Advisers is available on our website: www.XXXXXXX/aboutus

ABC Investment Advisers ABC Logo

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What are the upfront costs of our service?

Initial meeting to discuss our services, your objectives and assess your financial circumstances **At our cost**

Financial planning report and recommendations where we:
• fully assess your financial position
• provide a strategic report and recommendations covering your investment and retirement planning needs **£X fixed fee**

Implementing recommendations to set up or make changes to your investments **A%** on the first £100,000 of your investment, and **B%** on any amount over that

Example of our costs: To set up a £200,000 investment would cost: £X (A% of first £100,000 = £X PLUS B% of the remaining £100,000 = £X).

More details about our services are available in our XX document available on our website: www.XX.XX.X\XX

What are the costs of our optional ongoing services?

ABC's Gold ongoing service provides:
• an annual review of the performance of your investments and whether they continue to be suitable **Y%** per annum
• access to our online portal providing up-to-date valuations
• our quarterly newsletter

Example: One year of Gold on-going service on a £200,000 investment would cost: £X

ABC's Platinum on going service is the same as our gold ongoing service but also provides:
• an annual meeting with an adviser to assess your financial position and recommend any changes to your investment portfolio - if necessary make any changes to your investments. **Z%** per annum

Example: One year of Platinum on going service on a £200,000 investment would cost: £X

More details about our services are available in our XX document available on our website: www.XX.XX.X\XX

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- work with firms to test new ideas. The results of this testing, if effective, could inform the regulatory approach, lead to consultation on rulebook changes and could also influence our negotiating strategy when European directives are (re)negotiated.
- consult later in the year on proposed changes to some of the Handbook disclosure provisions in this paper.

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