

9th Conference – 4th April 2019

Consumer Protection

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Good afternoon.

A few weeks ago, the Financial Times ran a headline claiming that conduct had replaced capital as the key current focus for regulators. Whether or not you agree with this claim, it does make the topic today apposite and timely.

What is conduct regulation or protection? If you google these terms, you find no answers. This applies even to the FCA which has Conduct in its title. The dictionary definition of conduct refers to behaviour. Perhaps the closest we can come to a practical definition today is that conduct refers to the way in which a financial firm behaves, especially towards its customers.

Is the Commission a conduct regulator? Yes it is. For example, the Commission's Mission Statement says that the Commission will work to deliver 'high quality prudential, financial crime and conduct regulation'. By this statement, the Commission places conduct at a high level as one of its three objectives.

As this is still a high-level perspective, let me try to make the scope a bit more specific. By conduct regulation or protection, we primarily mean the way in which Guernsey licensed firms treat the 'general public'. This is not to say that conduct regulation does not apply to financial professionals and companies; it is rather that these categories tend to be more sophisticated and more able to look after themselves. The Commission's focus therefore is on financial products and sales to people whose everyday life does not involve thinking about finance. This may be clear enough but I would also like to draw out two points here. The 'general public' covers everybody irrespective of wealth or income. It also extends beyond the Bailiwick to those people who may live overseas but who buy Guernsey financial services.

In other respects, conduct regulation is just like prudential and financial crime regulation. To be effective it needs a sound legal and policy framework, appropriate everyday supervision and an enforcement capacity. We apply the same philosophy for conduct as for other types of regulation; that is a principles-based approach. That is not to say that we do not have specific rules; rather we prefer in general to set out a series of high-level principles that we expect firms to follow.

Having established the nature and centrality of conduct for the Commission, I would now like to spend time undertaking two tasks. Firstly, I want to set out here the Commission's overall view of how well particular sectors in the Bailiwick follow good practice around conduct and where improvements – both sector-specific and general - might be still made. Secondly, I want to

explain how the Commission might enhance the quality of its own conduct regulation in the future.

I aim to cover the industry sector by sector before moving onto some general observations. You will forgive me however if I do not cover all financial sectors; for example I am not going to talk here about market regulation.

Let us start with the provision of investment advice by private banks and high-end investment advisers to better-off clients under the Protection of Investors Law. Here licensees generally behave well. Advice is generally thorough, targeted and clear. However, licensees need to get better at documenting advice. This is for their own protection and it is good practice both for compliance and business purposes.

The next sector is the provision of long-term investment advice under both the Protection of Investors Law and the Insurance Managers and Insurance Intermediaries Law to local retail customers. This was an area of weakness in Guernsey and the Commission used to come across some poor practices. After several years of remediation and the imposition of much tougher regulatory requirements, standards have improved greatly. If I had to choose one area of improvement, it would be that more care be taken to shape advice and products to the circumstances of individual clients.

The next sector is the provision of general insurance services to local residents. The Commission used to worry about the way add-ons were sold in this area but licensees have since cleaned up practices. Last year we conducted a thematic on general insurance intermediary practice in Guernsey and the results were positive.

I would now like to move on to retail banking practices. The Commission has noticed a sea change here from a culture based on sales to one based on the decent treatment to customers. This is due to regulatory pressure in the UK and a change of thinking at the banks themselves. More locally, Guernsey retail bank heads take local complaints seriously, possibly as a means of personal self-preservation. The local retail banking community has also been supportive of Guernsey Community Savings. I do not intend here to talk in detail about financial exclusion other than to say that this is a long-standing problem in Guernsey and it is to be hoped that Guernsey Community Savings addresses this issue.

Returning to banks, it is worth talking about mortgages and loans. In recent years the provision of mortgages had become a little too tied-up in red tape but this has now eased somewhat; and it is good to see affordability at the heart of mortgage decisions. On credit conduct generally, local banks look fine but we have less clarity as to whether credit is provided to customers in a fair way outside the banking world. This is because the Commission does not regulate this area although this is something that States Committees are currently considering.

The Commission has recently introduced a new licencing requirement under the fiduciaries law in relation to pension and gratuity schemes. This has enabled the Commission to introduce new rules, aimed at the fair treatment of pension and gratuity scheme members. It is still early days

but the message here is that some providers tend to point to any other entity except themselves as being responsible for the fair treatment of customers.

Turning to insurers, there are two areas of current focus. The first is the provision of travel and health insurance to the global ex-pat community. The products are mostly straightforward but the Commission has some doubts as to whether the sector is as up-to-speed with regulations as it ought to be; not least around governance. We worry whether insurance managers are giving the sort of expert advice on local compliance that they should as General Representatives.

Another area relevant to insurers is the provision of long-term investment services under a contract of insurance to people outside Guernsey. This is undertaken reasonably well but this sector needs to gear up more to meet the challenge of higher regulatory expectations in the treatment of customers as set out in our recent Conduct of Business Rules. The need to navigate around conduct regulation in multiple regimes can be challenging for this sector.

That completes my overview and feedback on each sector. I will now outline the general areas where the Commission thinks improvement could be made in all or most sectors.

However, before I talk about specific issues it is worth saying that, in order to achieve good conduct standards, a financial firm has first to achieve certain standards in more general areas such as governance, systems, operations, data management, human resources and so on. If a firm fails in these respects, it is unlikely to be able to achieve good conduct standards. In such cases – and the Commission periodically comes across them - it is not that the firm does not want to achieve good conduct standards, it is rather that it simply cannot do so because for example its governance is bad, or its systems are inadequate and so on. So conduct is interwoven with wider aspects of a firm and can be a barometer of a firm's health; not least its culture.

Turning now to more specific issues, one area of general improvement around conduct is the treatment of vulnerable customers. Some time ago, when higher standards around financial crime mitigation were first being implemented, the banks took a while to amend procedures to take special care of their vulnerable clients. Since then the concept of vulnerability, and its definition beyond the infirm, has become reasonably well embedded amongst Guernsey financial firms. However, the Commission still comes across examples of weak procedures and even occasionally of actual abuse. I suggest that everybody here hopes that in future the Bailiwick's reputation will be spotless.

Another area is the treatment of complaints. During our general insurance intermediary thematic in 2018, we came across a firm that used complaints to improve customer service in a positive way. It did this by treating even off-hand comments by customers as a complaint. This is in contrast to other firms we came across during the thematic who incentivise staff to do almost anything to avoid accepting that a customer is unhappy. Licensees need to look at improving this area because listening to reasonable customer feedback is a good way of improving conduct.

To move on, another area for some improvement is language. Although finance is not a rocket science, you all work in an industry where those outside the industry find even the everyday

terms you use sometimes baffling. The insurance industry is particularly bad at using complex terms – often for some reason in French – for the simplest concepts. Licensees need to speak and write clearly to clients in plain English.

Another area is transparency. Although things have much improved, costs and commission can still be opaque. A simple example of this is the preference of some firms to express cost as a percentage rather than an absolute sum; and in so doing making it less easy for some retail customers to grasp how much they are actually paying for a service. More generally, although in Guernsey we do not specify a key features document, it would be reasonable to expect at least for some retail financial products an up-front summary of the product on sale.

A related point to transparency is disclosure. Suppose you are buying a retail financial product from a Guernsey company. It is a reasonable expectation that you should have access on the web to at least an abridged balance sheet, the company's address, the names of the people on the board, who to complain to and an indication of your rights under the financial ombudsman. It is surprising that, for many such licenced firms in Guernsey, this information is not currently on the web.

I now come to how we may need to develop; albeit I will limit my remarks to specific supervisory rather than general issues.

In terms of sectors, the most difficult current area on conduct for us at present – and it will differ over the years - is the insurance managers; especially when they work with insurers who sell products to the public. Insurance managers are key to several aspects of the insurance sector in Guernsey. Last year we undertook a thematic on the quality of regulatory reporting, not least by managers. The results were disappointing in that the accuracy of returns was often low. By the way, this was even after auditors has signed off on the returns, so auditors have remedial work to do in this area too. Accurate reporting is important for a regulator as we rely on regulatory returns to flag up actual or potential problems – a point already made by Gillian. Looking forward, we will undertake more thematics and these will look at specific operational areas where insurance managers provide services.

There are also certain supervisory approaches that we may need to think about more. One is the oversight of products. We already authorise funds, which we regard as products. However, we are increasingly looking at products in other sectors in more detail, who they are aimed at, and how they are sold. Therefore, products have come more into our focus.

Another area is the use of the concept of 'fairness'. What should, in your opinion, the regulator do if a firm insists that a customer abides by the terms and conditions of a product, but one which might seem to most of us as blatantly 'unfair'? We can of course remonstrate with the company. However, if it refuses to offer redress, what should the regulator do? The Commission's paper on Lending Credit and Finance considers this issue in relation, for example, to affordability with the implications those contractual terms are no defence for inappropriate lending.

Another area of focus is service standards. Traditionally regulators have concentrated broadly

on two areas – solvency and mis-selling. However, imagine the following scenario. There is a solvent firm where no critical customer abuse has occurred. However, the customers receive financial data that is difficult to understand, payment mistakes are periodically made – even if eventually corrected – and the customer can only talk on help lines to staff who may be pleasant but who lack the training to help. In a textbook free-market environment, a firm with higher service standards would soon replace such a firm. However, for various reasons, such an environment is more constrained for financial services and, in practice; such a firm can survive for a long period. Therefore, perhaps this type of poor service should also be subject to greater regulatory focus – in addition to the routine focus on complaints.

More widely, the Commission will keep its eye on developments elsewhere and consider whether these should be incorporated into its supervision. For example, should we publish leagues around say insurance payout rates – a concept in trial in the UK? I can see that some firms may not like that; but it may offer a useful guide for consumers.

So far, I have talked about the industry and the Commission. Of course there are other players and they too have an important role to play.

First, there is the government in its various guises. The political authorities in Guernsey have in recent years taken significant action. They have introduced a Depositor Compensation Scheme, the Guernsey Financial Advice Standards and a financial ombudsman. I should like to note the increasing contribution made by the financial ombudsmen towards investor protection and I am sure this will become only more important over time.

A key player is the customer. He or she too has responsibilities. There is only so much that an adviser can do – ultimately the customer has to make decisions that will affect his or her financial well-being. It is true that the quality of education specifically around financial literacy should be higher. The Commission is delighted that financial literacy is now included as a key component in the Bailiwick curriculum across all school years and is supportive of Education Services and the schools in this regard. The Commission tries to plug the financial literacy gap with its consumer advice pages but the impact is inevitably limited. Please feel free to refer your customers and your staff to these pages on our website <https://www.gfsc.gg/consumers> as they too may find them a helpful resource. Nevertheless, adults have to accept adult responsibilities. For example, we periodically receive complaints from people who say that they thought stock markets always go up and it has come as a shock to them that they are poorer, rather than richer, due to other stock markets going down. It is difficult to be sympathetic in such circumstances. High regulatory standards do not absolve customers from personal responsibility.

Finally, it is worth noting today that conduct regulation has risen in importance both in Guernsey and more widely across the world – as indicated by that FT headline cited at the start of this address. Conduct regulation is also here to stay at least for the immediate future. One reason for this is public confidence in the financial services industry, which is – not least in the UK – a long way from being restored. Another reason is that we are still seeing cases of customer mistreatment emerge that post-date the global financial crisis, having been enacted by executives

after the crisis

Given that conclusion, I hope that you have found this talk of some use. I have outlined some of the strengths and weaknesses around conduct of the Guernsey financial services industry. Some parts are reasonably strong around conduct; others need more work. Broadly speaking, the following questions might be asked of themselves by licensees, at least selectively and based on their particular business – and these questions are in your self-assurance pack:

- How sure am I that my firm treats vulnerable customers properly?
- Am I listening to my customers and improving service?
- Does my firm speak to customers in a way they understand?
- Can customers easily access key data about my firm?
- Are the products my firm sells easy-to-understand and are they being sold to the right people?

In addition, a question that I would also like you to ask of yourself because it is one close to the heart of the Commission:

- Am I sure that the regulatory returns I submit to the Commission are correct?

In this talk, I have also set out where the Commission is going in the near future. I have talked about the accuracy of regulatory returns, an increased interest in products, fairness, and service standards. The Commission will keep an open mind as to how it can improve and develop. Your views will be important in that respect. Our overall commitment to a pragmatic and principle-based approach will also remain unchanged. In the meantime, please accept my thanks for coming here today and for listening