Resolution Foundation Response to HM Treasury consultation on
Reforming Financial Markets, July 2009

1. Summary

The Resolution Foundation welcomes the opportunity to respond to the Reforming Financial Markets white paper. The Foundation is an independent research and policy organisation that aims to improve the well-being of low earners. Our work is mainly relevant to chapter 8 of the white paper – Supporting and Protecting Consumers – and in particular the progress being made on Money Guidance. This response, therefore, comments on a number of issues in chapter 8 and specifically addresses consultation questions 15 to 21.

Key points:

- We congratulate the government on progress on Money Guidance. We would suggest that, so long as the evaluation demonstrates that the service is helping consumers, then not all operational issues need to be resolved before a national roll-out proceeds next year. Some operational issues will only be resolved through enabling the service to evolve flexibly as it is rolled out nationally.
- We welcome the establishment of a new consumer education and information authority and the inclusion of consumer credit companies in funding Money Guidance via a levy. How this new levy fits with the existing FSA levy should follow clarification of the remit of the new authority.
- In addition to the consultation questions, we would also suggest that there needs to be clarity over:
    - What the establishment of the new authority means for the objectives and responsibility of the FSA in relation to consumer issues
    - The name of the authority given its remit and in particular that it will be covering guidance and advice
- The new authority needs to be on the side of consumer, and could act as a ‘consumer voice’, but must balance this with a positive view of the financial services industry.

In additional to the Foundation’s work on financial health, we are currently undertaking a programme of work on *Low Earners in Recession and Recovery.* This covers work relating to household finances and housing. We have included initial thoughts in this response, but will forward our fuller findings later in the autumn.

2. General response to issues raised in Chapter 8

a. Money Guidance

Following its creation in October 2005, the Foundation focused on how people access and use the financial services system. We identified early on the existence of an “advice gap” for those on low to median incomes, a gap in advice provision which left low earners vulnerable to the consequences of poor decision making. The Foundation conducted extensive research into the nature of the advice gap and into a service that could meet the needs of low earners. Our main findings are in the Foundation’s 2006 report *Closing the Advice Gap*. This work fed into the Thoresen Review and we were delighted that the government adopted the recommendations of the review and launched the Money Guidance pathfinders earlier this year.

The Foundation wants to congratulate the government on its intention to roll out the Money Guidance service nationally from 2010, subject to the evaluation. Given the current economic climate, it is vital that a service that can aid consumers to stay financially healthy and seek advice before they reach a crisis point is available as soon as possible.

The Foundation understands that this roll out is subject to interim evaluation findings from the pathfinder, but urges the Treasury to consider that a “perfect” solution to delivering Money Guidance need not be achieved before a national service goes live. The pathfinder should make good progress in resolving many delivery issues, but some issues can only be addressed once a national service is up and running and able to evolve.

The Foundation would also point out the crucial importance of coordinating the role that Money Guidance has to play across government departments so that it becomes a holistic service linked in to changing economic conditions and new government services and initiatives. For example, it must be fully integrated into the roll out of Personal Accounts from 2012.

We respond in detail to the consultation questions in section 3 below.

b. Comparison websites

Money Guidance will support consumers to make sound choices when it comes to selecting and managing consumer credit products. In order to do this the government’s consumer white paper, published on 2 July, set out plans to include a credit card comparison tool on the Moneymadeclear website.

This is welcome. However, users of Money Guidance are likely to turn to comparison websites for a whole range of products or to check whether they are getting good value from their existing mortgage, credit card, savings account, so the market must be accessible and transparent in its operation across all these areas. The Foundation’s 2007 report *Compare and Contrast: How the UK comparison website market is serving financial consumers* argued that there needed to be a code of conduct established in order to achieve this.

The recently launched Comparison Consortium has gone some way to meeting this need. However, many of the big players in the comparison website market are absent. The Foundation believes that there may now be scope for making this code of conduct compulsory so consumers can feel confident in comparing financial products online. The Foundation would also be keen to see how any code will be policed as some standards may be hard to measure and might be open to interpretation. The Foundation would suggest that a set of guidelines against which to assess adherence to elements of the code might be a helpful step. This might be a role that falls under the proposed consumer education and information authority.

c. *Strengthening the FSA's work on financial capability*

The Foundation welcomes the establishment of an independent consumer education and information authority with its own levy-raising powers.

The Foundation has championed a *Financial Health Service* model for coordinating all activity relating to individuals' financial health. This model has three core strands of activity: preventative (e.g. financial education), remedial (e.g. debt advice) and primary (e.g. money guidance.) The Foundation believes the new authority could adopt this model, which would then ensure that there is strategic oversight of all the initiatives relevant to financial health. This has implications for the breadth of the new authority which we cover in our response to the consultation questions below.

The Foundation runs a *Financial Health Forum* which brings financial capability and inclusion experts together with financial services practitioners. This Forum has demonstrated the benefits of a strategic overview of personal finance policy and practice. Further details of the Forum are available on our website.

d. *Mortgages and consumer credit*

The Foundation is currently running a programme of work *Low Earners in Recession and Recovery.* We will be publishing the first set of findings from this work in November which looks at three key issues - housing, work and household finances. Our comments below draw on early analysis from the housing research strand.

The White Paper observes that, despite falling house prices, tighter lending practices have led to the exclusion of many people who would have been able to access mortgages prior to the credit crunch. This is largely a result of higher deposit requirements and has disproportionately affected people on lower incomes, who are less likely to have access to the 'bank of mum and dad'. 80 per cent of first time buyers are estimated to be assisted in this way.

Measures to help this group of 'would be' homeowners to sustainably purchase are welcome. By reducing the risk of a mortgage (to lender and borrower), the Canadian insurance model is one way of achieving this. The Foundation would be keen to see this model explored further in the UK context. But, as the White Paper suggests, there are a range of other methods including:

- Measures to reduce and help with the cost of purchase (Low Cost Home Ownership Schemes, changes to Stamp Duty, Assisted savings schemes);
- Improving sustainability through a better safety net;
- Raising awareness of the true risks of lending to people on low incomes through alternative credit scoring systems;
- Securing a commitment from lenders to serve certain groups.

Measures to assist people into home ownership must be coupled with initiatives to help sustain it. A significant number of low earners who entered home ownership in the last five years have overstretched themselves and, following the recession, have had their homes repossessed, or are at risk of having them repossessed.

As unemployment continues to rise and the housing market stabilises there is a danger that this risk of repossession will increase, particularly for low earners who have borrowed from certain parts of the market. For example, the research shows that the non-prime and second charge lenders have shown less forbearance. Therefore, initiatives to further protect consumers, namely consumer protection when lenders sell on mortgage books and the transfer of regulation of second charge lenders to the FSA, are welcome.

We also welcome FSA regulation of the buy-to-let market, which accommodates many low earners. Low earners are more likely than other income groups to be living in the private rented sector; too poor to access home ownership and too rich to access social housing. One of the implications of the recession for them has been heightened insecurity when their landlord is repossessed.

The FSA's Mortgage Market Review provides a good opportunity to reflect on the lessons learnt from the financial crisis. From the perspective of people on low to moderate incomes, getting the balance right between improving sustainability and access is critical. Clearly over-regulation of mortgages in the pursuit of more sustainable outcomes will have a detrimental impact on access for those on low and moderate incomes. Although there seems to be open dialogue with CLG, the FSA has been clear that they do not do housing policy and will maintain a tight focus on regulation (and therefore not be exploring wider implications.) This approach risks further excluding people on low to moderate incomes from mortgage finance.

3. Response to consultation questions 15 to 21 on money guidance and the new consumer education and information authority

(15) What are the advantages and disadvantages of the relevant consumer credit firms contributing to the costs of Money Guidance?

The Foundation welcomes this positive step towards funding the national roll out of a money guidance service next year. We believe it is right that Financial Services companies contribute to the cost of a national advice service, and that this cost is shared fairly across the full range of companies.

Including consumer credit firms is not straightforward but providing a mechanism by which they can contribute is necessary.

(16) The Government believes that some organisations, such as free and impartial debt advice providers, should be exempt from the levy on consumer credit licence holders – do you agree? Are there other cases where an exemption is appropriate?

The Foundation agrees that there should be exemptions for organisations that provide free and impartial debt advice. There might be other not-for-profit organisations involved in financial capability or inclusion work where an exemption might also be appropriate.

(17) What factors should be considered in designing an appropriate levy scheme for consumer credit firms?

There is not yet detail on how the extension of the levy to consumer credit firms will work. The Foundation believes the levy for consumer credit firms should, like the existing FSA levy, be proportionate to the size of companies. The Foundation would urge that the design of a new levy takes into account the need for clarity, transparency and predictability of fee level for companies which will be important in gaining their support. Predictability of income will of course also be critical for the operation of services.

The Foundation suggests that the question of whether the new consumer credit firm levy is limited to funding Money Guidance or extended to funding wider financial capability activities (as with the existing FSA levy) needs to be examined further.

The best way forward would seem to be to determine the remit of the new consumer education and information authority and then to map and determine how the full range of activities will be funded using existing and new sources of funding.

(18) What issues need to be resolved to establish a successful consumer education authority set up by the FSA?

Many of the key issues that need to be resolved are covered in the additional consultation questions, such as the scope, funding and governance of the authority. The following questions also need to be resolved:

- What does the establishment of the authority mean for the FSA? We need to ensure that a concern with consumer awareness, understanding and access is integral to the FSA's work and is not seen in the future as the sole responsibility of the new authority.
- What will be authority be called? This will need to reflect its scope (e.g. why is 'guidance' or 'advice' not included in the working title?) and the degree to

which it is consumer-facing (and therefore needs to have a name which resonates with the wider public and is easily understood.)

- How will the authority work with other organisations? Critical to the authority's success will be its ability to coordinate activities and delegate activities to other organisations better placed to deliver. This will require a very clear framework for partnership working.

(19) What are your views on the scope of the new authority? Should it also, for example, champion consumer interests and act as a consumer voice in financial services?

The Foundation believes the authority should have a broad remit, which covers existing financial capability activities but which extends beyond this to services/initiatives which currently fall outside of this, such as debt advice. We refer back to the *Financial Health Service* model above which could be adopted.

It has been clear from the work of our *Financial Health Forum* that it does not make sense to separate financial capability and relevant financial inclusion activities. The Foundation believes that the new authority will need a financial inclusion objective, but that the scope of this needs to be clarified.

The Foundation thinks that the authority needs to be on the side of the consumer, but that it also needs to be positive about (and not antagonistic towards) the financial services industry. This need not exclude the authority being a 'consumer voice' but will require governance arrangements to represent both the consumer and industry.

(20 & 21) What are your views on the governance and funding proposals for the authority? To what extent should the authority be independent of the FSA?

On governance, the Foundation thinks further thought should be given to who appoints the board and chairman to ensure the authority is truly on the side of the consumer and is operationally independent from the FSA.

On funding, as discussed above, the scope and remit of the authority needs first to be agreed. Clarity on how the activities will be funded via new and existing levies (and the scope of these levies) would then be easier to resolve.

The new authority should be entirely operationally independent of the FSA.

30 September 2009