CP19/12 – TISA response

June 2019

About TISA

TISA is a unique, rapidly growing, consumer focused membership organisation. Our ambition is to improve the financial wellbeing of all UK consumers. We work with our members to deliver practical solutions and devise innovative, evidence-based strategic proposals for government, policy makers and regulators that address major consumer issues.

TISA membership is representative of all sectors of the financial services industry. We have over 200-member firms involved in the supply and distribution of savings, investment products and associated services, including the UK's major investment managers, retail banks, online platforms, insurance companies, pension providers, distributors, building societies, wealth managers, third party administrators, Fintech businesses, financial consultants, financial advisers, industry infrastructure providers and stockbrokers.

Complementing our consumer policy development, TISA has become a major industry delivery organisation for consumer focused, digital industry infrastructure initiatives (TeX/STAR, Digital ID, MiFID II and Open Savings & Investment). This reflects TISA's commitment to open standards and independent governance.

TISA's current strategic policy and industry solution developments include:

- **Financial Guidance**: Making guidance more widely available to support financial decision making for those consumers who currently do not have access to advice.
- **Digital ID:** Development of a secure Digital ID for consumers of UK financial services. This will be key enabler for the digitisation of financial services.
- **Open Standards Development - Digitisation**: Building on TISA's range of open standards development projects (inc. TeX, MiFID II), TISA's members have launched a project to further open up UK financial services to consumers. This project - Open Savings & Investment – is aligned to the aims of Open Banking and has the core objective of enabling access to all savings and investments through the development/governance of industry open standards.
- **Financial education**: Helping young people manage finance, including KickStart Money - a three-year programme delivering financial education to 18,000 primary school children.
- **Retirement saving**: Strategic proposals for a holistic approach to saving for retirement.
- **Consumer engagement:** Focusing on vulnerable customers and millennials.

TISA also provides its members with support on a range of operational and technical issues targeted at improving infrastructure and processes, standards of good practice and the interpretation and implementation of new rules and regulations. This work currently includes: MiFID II, CASS, SM&CR and addressing cybercrime.

Q1: Are you aware of any material obstacles firms may face in implementing the proposed requirement that consumers moving investments in units in funds common to the ceding and receiving platforms should be given the option of an 'in-specie' transfer (in addition to other options the platform may offer)?

TISA is generally supportive of the FCA's proposals here. As the paper discusses, different platforms will face different costs and challenges in meeting this requirement but we are not aware of any insurmountable obstacles to achieving the FCA's broad aims.
As you know, TISA are closely involved in and support the work being undertaken by the Transfers and Re-registration Industry Group ("TRIG") and the STAR initiative. TISA published recommended practice for the industry in 2014 on the processes firms should adopt in the scenarios described in the CP, a copy of which is attached.
TISA has convened an industry meeting to discuss how these changes sought by the FCA can be implemented in a speedy and efficient way, building on the TISA paper. The meeting will be on 27th June, and we will keep you updated with progress. .

Q2: Are you aware of any material obstacles firms may face in implementing the proposed requirement that ceding platforms should request conversions on behalf of consumers, where this is necessary to support the consumer's request to transfer their units to a new platform on an 'in-specie' basis?

No.

Q3: Are there any circumstances where platforms would not be able to take the necessary steps to bring about the conversion of unit classes to enable an 'in-specie' transfer? For example, would our rule need to apply to other firms that may be involved in the process?

We are not aware of any such circumstances, although there is a concern that platforms will sometimes be dependent upon other firms - such as fund managers - to facilitate this process. The FCA should, in applying its interventionist powers across the retail industry, ensure that those firms are also brought into compliance with the FCA's objectives here.

Q4: Do you agree that receiving platforms, as part of the transfer process, should give consumers the option to request conversion of their units into a discounted unit class, where this is available to them at the receiving platform? If not, why?

Yes.

Q5: Do you agree with the planned implementation date of 31 July 2020? If not, why not, and what alternative timeframe would you suggest?

The proposed timetable seems reasonable.

Q6: Do you agree that an exit fee should be defined as in paragraphs 4.10-4.11 above, and should include all charges associated with consumers' exit from the service?

We are comfortable with the proposed definition, but please see our response to Q8.

Q7: If you do not agree with our proposed definition, what charges should be excluded and how should exit fees be defined?

We are comfortable with the proposed definition, but please see our response to Q8.

Q8: To what extent would the banning of exit fees mitigate barriers to switching in relation to platforms and firms offering comparable services?

We are not convinced, on the evidence presented, so far as platforms are concerned, that the FCA has succeeded in demonstrating that exit fees, per se, as opposed to unreasonable or unfair burdens on customers switching are a significant barrier to switching, and therefore we are also not yet convinced that banning exit fees would achieve much in the way of mitigating the stated (but in our view undemonstrated) problem.

In our first response to MS17/1.2[1], in relation to the FCA's initial proposals in the context of the platform industry, we said:

"We do not support the FCA's proposal to ban exit fees. The transfer process is a costly one for platforms and it is reasonable for firms to ask clients to pay for the service, in the same way they pay for other services they enjoy. It is likely that banning exit fees would have the 'waterbed' unintended consequence of forcing firms to recoup such costs through other fees, which would be unfair to those clients who do not leave; it would effectively be a punishment for loyalty, which in itself is a fairness issue. There may however be some scope for the FCA to regulate exit fees where the amounts set are arbitrary, or not related to cost, or not easily disclosable in advance, but which act as a competitive barrier. This would require careful consideration; the issues are too complex for discussion here. Exit fees are often a mirror of entry fees and banning them retrospectively might cause graver harm than the potential benefit to customers."

The FCA's new comments have not given us cause to move significantly from this position.

The FCA has now adopted a new proposition in which it is seeking to ban (or cap) exit fees across the retail investment industry generally, using its arguments in relation to platforms as a stepping-off point.

This is a big step to take.

This broader proposition is, therefore, one the FCA needs to ensure is well-supported by evidence. As explained below we are still not sure the FCA has provided evidence that there is a problem as stated, either for platforms or for the wider retail industry, and therefore it is difficult for us to support the FCA's proposals for a solution, particularly when it is proposing the double-edged sword of price regulation as its only weapon.

As a general comment, we accept that there are some market situations in which the FCA, as a last resort, will act as a price regulator. This will be in response to situations where there are a small number of commercial players, sometimes operating behind high barriers to entry, with unfair positions of power over their customer in situations where it is difficult for the

[1] http://www.tisa.uk.com/publications/912_MS17ResponsefromTISA.pdf

customer to change provider or where the customer can be vulnerable in other ways. To put it in the words of Mary Starks, the FCA's Director of Competition: *"Price regulation in the context of utilities or financial infrastructure is primarily motivated by concerns about monopoly or market power - companies that enjoy a privileged and unassailable position, and whose ability to over-charge their customers must therefore be reined in."* [2] It was easy to recognise these situations in the short-term high-cost credit market, for example, where often unsophisticated and sometimes desperate customers have undoubtedly been taken advantage of. The pensions market was another area where the FCA quite reasonably reached for price regulation tools; it was essential that customers be allowed to change their pension provider without undue penalty in order to access the new pension freedoms, and the early exit fee cap of 1% has demonstrably achieved its aim. In these situations we recognise that the FCA had little choice but to address obvious and urgent customer detriment.

However, none of the features of a dysfunctional market, as described above, exist here. We are concerned that the FCA is seeking to apply its interventionist powers purely in response to a subjective and undemonstrated view that exit fees are by definition anti-competitive.

We accept that exit fees are difficult to like. It is easy to assume, at face value, that they are anti-competitive and unfair, even after proper disclosure at contract inception. Assumptions, however, are not an adequate basis for the FCA taking the important and hopefully rare action it is proposing; we look for evidence. What concerns us is that the only evidence the FCA has so far presented to justify its conclusion that customers are inhibited by exit fees from switching platforms is in section 1.6 of MS17/1.2: "*But we found that 7% of consumers have tried to switch at some point but failed mainly because of the time involved, the complexity of the process and exit fees."*[3]

This evidence itself suggests that exit fees are a relatively minor causal factor, coming third behind time and complexity. It is indeed our view that time and complexity are the critical factors at play here, and we fully support the FCA's objectives in reducing these factors as far as can be practicably achieved.

Nor is the 7% figure quoted above a compelling statistic suggestive of a large population of customers who feel trapped by their current provider. Its low number seems to correlate to the Financial Ombudsman Service's limited experience of complaints relating to exit fees. In October 2015, and reflecting on the first six months of then new pensions freedoms, the FOS said this: "*To date, we have not received many enquiries and complaints concerning exit charges and fees. 14 of the 760 enquiries between 6 April - 6 October and seven of the 150 pension freedom complaints from 6 April- 6 October were about fees. In a very small number of complaints, consumers are complaining about the level of the fees being too high. However we have found that in the majority of these complaints, consumers were unhappy about the very fact of being charged a fee, which they considered to be unfair and unreasonable …. Given the small numbers and nature of these complaints, we have limited insight to share at this stage on the issue, but we will continue to monitor this issue."* [4]

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[2] Speech by Mary Starks, Director of Competition and Chief Economist at the FCA, delivered at the Social Market Foundation lecture, London, 27 Feb 2017: https://www.fca.org.uk/news/speeches/diocletian-pay-day-loans-what-can-we-learn-successful-and-unsuccessful-price-regulation

[3] https://www.fca.org.uk/publication/market-studies/ms17-1-2.pdf

[4] https://www.financial-ombudsman.org.uk/publications/consultations/consultation-pensions-transfers.pdf

The FOS, to date, has still not identified exit fees as a noteworthy cause for complaint. One might expect it to have done so, if exit fees were indeed acting as a primary inhibitor.

However, bearing in mind the FCA's stated intention of banning exit fees across the retail investment industry we recommend that the FCA seeks firmer evidence that exit fees are genuinely a ***material*** inhibiting factor preventing consumers from switching provider.

We also bear in mind that platforms by definition tend to attract relatively sophisticated and financially comfortable customers; there is no evidence that platforms are exploiting the vulnerable. Nor are there any signs of firms enjoying a monopoly position; the platform market itself is wide, buoyant and attracting new players with increasingly varied propositions. Where platforms compete for business from professional advisers there can be no doubt they are operating in a price-sensitive market.

As the FCA notes, Investment platforms have become a significant distribution channel for retail investments in the UK, with over £500 billion in assets under administration. The number of consumers using platforms rose by about 2.2 million between 2013 and 2017.

Indeed, the FCA 'found that the market is working well in many respects, for both advised and non advised consumers. Consumers who pay more typically get access to a greater range of non price features and they are, overall, satisfied with their platform. Platforms also appear to help consumers and financial advisers make informed investment decisions free of investment product bias. This suggests that platforms are competing in the interests of most consumers.'

These features, of a growing market, used by millions of customers, working well for both advised (the vast majority) and non advised customers and where the platforms are competing in the interests of most customers, are not obviously consistent with a market where the FCA should take price regulating powers, preparatory to extending these powers across retail financial services as a whole.

This is, therefore, in our view, not a situation in which it automatically seems reasonable for the FCA to use its *"control…of absolute last resort"* (to quote Ms Starks).

We dislike exit fees. We oppose price regulation, except in very limited circumstances – those set out by Mary Stark.

Price regulation inhibits competition, reduces supply and supposes that a regulator has a better idea of costs than the market as a whole. And price regulation has a very unhappy history.

Therefore, the FCA should put itself on firmer ground before employing price regulation tools across a significant swathe of the industry. We believe there is a real risk here that the FCA will be seen to be employing its considerable interventionist powers to address what has so far only been expressed as a dislike, rather than indisputable market failure. If nothing else the risk of unintended consequences increases significantly, the more broadly the solution is applied.

We note that many providers have scrapped exit charges, or announced their intention to do so. We believe the right way to see the changes the FCA is proposing is through the interplay of forces in a competitive market, not forced by an external regulator.

We therefore recommend that the FCA review the market place in a year to see if there has been sufficient change to avoid the need for compulsion. This would not stop the FCA taking action in cases where exit fees seemed egregious and unfair.

Q9: If we introduce a ban or cap on exit fees, should it apply to firms offering comparable services as scoped in paragraph 4.16? If not, what are the reasons why a ban/cap should or should not apply to particular types of firm or service?

We support the FCA's decision to consider these issues in relation to the broader FS industry, although as stated in our response to Q8 we suggest that the FCA should have much stronger evidence before it takes this important step.

And then consider whether there are alternative solutions.

The platform industry, which the FCA recognises as competitive and where customers are broadly satisfied, does not seem to us to be a reliable proxy for the myriad investment industry.

Q10: If your firm is in the wider scope of comparable firms as described in paragraph 4.16, do you currently apply any exit fees associated with these services? If so, please describe the nature of these fees.

Please see our response to Q9 above.

Q11: If your firm currently charges exit fees (as defined in paragraphs 4.10-4.11), what would be the impact of a ban on these fees? For example, do you envisage that other charges would be implemented or raised to compensate for the loss of income?

As we said in our response to the Market Study it seems to us inevitable that firms will seek to recover costs that are currently borne by exit fees, in other ways. Obviously the impact will vary from firm to firm depending on the level of contribution the firm has previously raised via exit fees; for some firms the impact on their customers will be negligible, or nil.

There is an argument that spreading fees through the contract lifecycle in this way is to the long-term detriment of customers in that the inflated fees would in effect act as a loyalty penalty, at a time when the FCA and the industry is working hard to build business models in which customer loyalty can be rewarded. It is worth reminding the FCA here that firms with high persistency are able to reward customer loyalty by keeping its cost base (and therefor its fees) low, and over time create new products and services that are better able to meet its customers' needs. It is in the FCA's interests to allow an industry to build healthy long-term relationships with its customers. For some firms, however, we accept that this impact will be small, or nil, for those who have hitherto not charged exit fees or who prepared to absorb them.

Q12: If your firm is a product manufacturer as well as a distributor as defined, what exit fees are applied within the products and services you offer to clients? If such fees exist, please provide a rationale for this charging model.

TISA is unable to respond to this question.

Q13: How might a ban on exit fees be defined in such a way as to avoid a 'waterbed effect' whereby firms are able to replace them with new product/wrapper-related exit charges?

We can see no realistic means by which such 'waterbed' effects can be avoided, as explained in our response to Q11, although we accept that for some firms the waterbed effects will be limited. We cannot see how this risk might be avoided by alternative 'definitions' of a ban. A ban is a ban.

The FCA should not need to go to significant lengths to anticipate all the possible alternative ways in which firms might seek to apply a de facto exit fee by describing it as something else. If firms play games with definitions we suggest that the FCA has more than adequate powers to bring to bear, based on the FCA's principles for fair customer treatment.

Q14: How prevalent are cases where product-related exit fees pose a similar or greater barrier to switching in the investment platforms and comparable services market?

We have no evidence that they are 'prevalent' at all.

The current position is that the FCA, in our view, has not yet presented convincing evidence that exit fees are a barrier to switching in the platform industry, and we are not aware that it has sought or obtained any equivalent evidence in relation to comparable service providers.

As suggested, this is a situation the FCA should address before going further.

Q15: What is your view on the IPMS Final Report's conclusion that a ban on exit fees would be more appropriate than a cap? If you disagree with the proposal, please provide your reasons.

Note that the following comments should be read in the context of our response to Q8.

We agree that in the context of the platform industry, and assuming there is a problem as stated by the FCA (i.e. that exit fees are a primary inhibitor for switching), a ban is more appropriate than a cap. Obviously this would depend on where the FCA might set the cap. A high cap would be unlikely to resolve anything. A low cap could act as a mitigant (on the same assumption) but we suggest that for simplicity and ease of disclosure, if nothing else, the industry is more likely to accept a ban. A cap would be a more complicated thing for the FCA to define, impose and police, and potentially more prone to manipulation.

In the context of the wider retail industry, we reserve all comments. There may well be sectors of the industry where a cap would be a viable and even more appropriate solution, as for example has seemed to be the case in relation to the pensions market. Again, we suggest to the FCA that its ambition to apply price regulation across the retail industry is a bold one that needs careful research; there will inevitably be more complicated, or at least different, situations than presented by the platform industry.

Q16: What is your view on the reasonableness of allowing the recovery of third party costs?

It is reasonable.

One of the advantages of a firm's fixed and disclosed (at contract inception) exit fee is that it can be set at a level where all anticipatable third party costs will be recovered, and requires no further disclosure. The FCA's proposals to ban exit fees carries with it the risk of creating further customer confusion and concern; platforms will be obliged to disclose piecemeal any third party costs they incur at exit, not having had the realistic opportunity to do so at inception. It is difficult to see how this more detailed and complicated disclosure will necessarily add to the customer's understanding and acceptance. In mitigation of this concern we expect that some firms will choose to absorb anticipatable third party costs via contract lifecycle fees. For those firms that do seek to recover them at exit and disclose them, we assume that consumers will be unlikely to demur, so long as they are properly disclosed and explained.

Q17: Do you agree with our Cost Benefit Analysis? If not, please explain why and provide details.

We have no comments.