Briefing note 15 April 2013

This week at the UK regulators

On 1 April, the long awaited separation of the FSA into the new Financial Conduct Authority ("FCA") and Prudential Regulation Authority ("PRA") took place.

This new Clifford Chance publication provides a weekly update on key developments at both new regulators and reports on stories of interest from further afield

Thirty second guide: The week in overview

The new regulators continue to take steps to differentiate themselves from the FSA.

The FCA has issued several reports examining the reasons why consumers in the financial services sector make flawed decisions. Its behavioural economics study gives important insights into how it is approaching its consumer protection responsibilities.

Other than a joint paper with the FCA which sets out proposals for a 15 per cent rise in regulatory fees and levies for the coming year, the PRA has not issued any publications this week. However, Andrew Haldane has confirmed the Bank of England's and its wish for simpler regulation in a speech questioning whether UK financial services regulation has become too complex.

Further afield, the new Chair of the US Securities and Exchange Commission has been sworn in and the Australian financial services regulator has demonstrated similar levels of commitment to credible deterrence to those shown by the FSA (and which will be continued by the FCA), including through criminal prosecutions for market misconduct and other financial services offences.

To err is human...FCA delves into the psychology of consumers' decisions

In the first of a series of occasional papers, the FCA has taken a detailed look at what drives decisions by consumers of financial services.

The FCA's paper on behavioural economics concludes that retail consumers in the financial services sector are particularly prone to making irrational decisions. It cites the inherent complexity of products, the need to make trade offs between present and future and assessments of risk and the input of emotion into the decision making process as key reasons why consumers often make the wrong choices.

A separate paper setting out the results of a study of the factors affecting consumers' decisions as to whether to claim redress supports these findings. In a field trial, the FCA found that minor changes to the timing and content of correspondence with consumers often had a significant effect on whether they pursued claims. It found, for example, that factors such as whether letters were signed from the CEOs of companies, the number of reminders sent and even what was printed on the envelope affected consumers' decisions.

The FCA is not the first regulator to study how and why consumers make irrational decisions. In the UK, Ofcom and the Office of Fair Trading have used behavioural economics in the context of particular enforcement cases and to assist them with understanding markets at the macro level. Similarly, the US Securities and Exchange Commission ("SEC") has previously (in 2010) associated itself with a study into US investors' most common mistakes.

However, where others have previously regarded these studies as interesting asides or used them sparingly in specific cases, the FCA has clearly stated that it intends behavioural economics to inform and underpin its approach to its consumer protection remit. The paper looks at how the FCA intends to spot issues, understand the root causes of problems and design interventions to help it protect consumers.

It acknowledges and looks at some of the questions which a better understanding of consumers' patterns of behaviour will bring. In particular, it recognises that deciding how far to intervene on behalf of consumers whilst still respecting their right to make their own decisions (and, to some extent, their own mistakes) will, in many cases, involve difficult judgments.

Addressing these questions, it sets out, in broad terms, the responses which it may use where it identifies risks of detriment occurring. At the less interventionist end of the spectrum, this may take the form of "nudges" such as providing more information to consumers or changing the way in which such information is presented. More proactive solutions will include "changing the choice environment" by imposing requirements as to how choices are presented to consumers or, in more extreme cases, rule making to restrict the promotion of particular products. The paper makes clear that the exercise of these powers in cases where products appear designed to exploit consumers' propensity to make ill-judged decisions may, in some cases, involve positive obligations to include particular features or, in the most egregious cases, may lead to products being banned altogether.

The FCA identifies payment protection insurance as the paradigm example of consumers making irrational decisions to purchase products which, when viewed rationally, are expensive and ineffective. The paper refers (in passing) to products currently being widely marketed to retail consumers, including packaged bank accounts and pensions. However, it does not give specific indications of the FCA's policy on these or particular products or risks. Instead, as Martin Wheatley made clear in a speech accompanying the release of the paper, it is designed to clearly illustrate the FCA's new, much more paternalistic, approach across its consumer protection remit.

The detail of how it will put this approach into practice, and which particular products it will target, will become clearer in time, particularly as it begins to use its new intervention powers. However, all the indications, both in these papers and the FCA's other early public pronouncements, are that the control environment for firms marketing products to retail consumers is only going to get tighter.

http://www.fca.org.uk/your-fca/documents/occasional-papers/occasional-paper-1

http://www.fca.org.uk/your-fca/documents/occasional-papers/occasional-paper-2

http://www.fca.org.uk/news/speeches/human-face-of-regulation

www.sec.gov/investor/locinvestorbehaviorreport.pdf

http://www.oft.gov.uk/shared_oft/economic_research/oft1224.pdf

HM Treasury starts review of Money Advice Service

Although it does not go into detail, the FCA's paper on behavioural economics echoes doubts which have for some time been voiced about the effectiveness of the Money Advice Service ("MAS"), the body responsible for financial services consumer education.

In a separate announcement, the FCA has agreed a framework document with HM Treasury ("HMT") and the MAS. This will involve regular reviews and constant assessment (led by HMT) of whether MAS is achieving its objectives and using its resources efficiently.

http://www.fca.org.uk/your-fca/documents/mas-fca-hm-treasury-framework

PRA chief calls for cut in "red tape"

In a speech given on 10 April, Andrew Haldane, the Executive Director for Financial Stability at the Bank of England, has called for less and simpler financial services regulation. He pointed to the upward trajectory in the length of UK and US financial services legislation, and argues that, as the UK economy slowly emerges from recession, "*the time has never been better*" for regulators and legislators to ask "*big questions*" such as whether banks internal risk models are "*more trouble than they are worth*" and whether "*complexity unduly advantages large incumbents over small new entrants*".

Although no substantive steps have been taken to "*peel back*" the layers of regulation as he suggests, his comments follow attempts by the FSA in its last days, which will be carried forward by the FCA and the PRA, to rationalise levels of regulation and improve accessibility for new entrants (see, for example, "Barriers to entry for new banks relaxed" in This week at the regulators – 8 April).

http://www.bankofengland.co.uk/publications/Pages/speeches/2013/646.aspx

https://onlineservices.cliffordchance.com/online/freeDownload.action?key=OBWIbFgNhLNomwBl%2B33QzdFhRQAhp8D%2BxrIGReI2crGqLnALtlyZe1JZh6KRd%2F2WabPRkKQK0wnp%0D%0A5mt12P8Wnx03DzsaBGwsIB3EVF8XihbSpJa3xHNE7tFeHpEbaeIf&attachmentsize=219797

FCA signs up to greater co-operation with FRC

In a memorandum of understanding entered into with the Financial Reporting Council ("FRC") entered into on 2 April (but published last week), the FCA has set out how they will work together to set standards and share information.

The FRC's responsibilities include maintaining accounting and auditing standards in the UK.

http://www.fca.org.uk/your-fca/documents/mou/mou-frc

FCA warnings

Firm	Date of warning	Details
Aston Forex/Aston Markets	12 April	Not authorised
http://www.fca.org.uk/news/warnings/aston-forex		
Able Capital	12 April	Not authorised
http://www.fca.org.uk/your-fca/documents/able-capital-pdf		
KBP Insurance Service Limited	12 April	Clone of FCA authorised firm
http://www.fca.org.uk/your-fca/documents/kbp-insurance-service		
Greenfield Securities Limited	10 April	Not authorised
http://www.fca.org.uk/your-fca/documents/greenfield-securities-ltd		
Eventus Consultancy JLT trading as Eventus Alternatives	10 April	Not authorised
http://www.fca.org.uk/news/warnings/eventus-consultancy-jlt-trading-as-eventus-alternatives		
Hanover Associates Financial Services AG	10 April	Not authorised
http://www.fca.org.uk/news/warnings/hanover-associates-financial-services		
Bforex	10 April	Not authorised
http://www.fca.org.uk/news/warnings/bforex		

Policy developments				
	FCA		PRA	
Proposed developments				
		Deadline for responses		
Consultation papers	Regulatory fees and levies On 9 April, the FCA and PRA issued a consultation paper setting out their joint annual funds requirement ("AFR") for 2013/14. This totals £646.3 million, a 15 per cent increase on the FSA's AFR for 2012/13. http://www.fca.org.uk/your-fca/documents/consultation-papers/cp13-01	9 June	9 June	Regulatory fees and levies On 9 April, the FCA and PRA issued a consultation paper setting out their joint annual funds requirement ("AFR") for 2013/14. This totals £646.3 million, a 15 per cent increase on the FSA's AFR for 2012/13. http://www.bankofengland.co.uk/publications/Documents/other/pra/policy/2013/regulatedfeesleviescp3-13.pdf

Further afield

SEC chair confirmed

On 10 April, Mary Jo White was sworn in as the new Chair of the SEC. She replaces Mary Schapiro, who stepped down in December 2012.

http://www.sec.gov/news/press/2013/2013-56.htm

Going down...under: Australian authority continues to take tough action on market misconduct

On 10 April, the Australian Securities and Investments Commission ("ASIC") succeeded in its appeal against a suspended sentence handed down to the former CFO of a payment processor for misleading the market. **Peter Coupar** was instead sentenced to 22 months imprisonment and ordered to pay a fine of AU$10,000 for his part in falsifying a company's accounts and for lying to ASIC.

The case is not the most significant by value which has been pursued by ASIC. However, it, and other developments this week, are illustrative of the uncompromising approach that it takes towards market misconduct (and the other areas of its regulatory remit).

Also last week, on 9 April, it published an update on its enforcement activity for the second half of 2012, which disclosed that, as at the end of December, it was pursuing criminal prosecutions against 22 individuals. Nine of these related to insider trading and market manipulation. The same number are currently being prosecuted by the FCA for similar offences.

http://www.asic.gov.au/asic/asic.nsf/byheadline/13-077MR+ASIC+appeal+sees+former+CFO+jailed?openDocument

http://www.asic.gov.au/asic/asic.nsf/byheadline/13-073MR+ASIC+releases+policy+on+cooperation+and+third+enforcement+report?openDocument

Authors

Roger Best
Partner

T: +44 20 7006 1640
E: roger.best
@cliffordchance.com

Matthew Newick
Partner

T: +44 20 7006 8942
E: matthew.newick
@cliffordchance.com

Martin Saunders
Partner

T: +44 20 7006 8630
E: martin.saunders
@cliffordchance.com

Carlos Conceicao
Partner

T: +44 20 7006 8281
E: carlos.conceicao
@cliffordchance.com

Luke Tolaini
Partner

T: +44 20 7006 4666
E: luke.tolaini
@cliffordchance.com

Chris Stott
Lawyer

T: +44 20 7006 4231
E: chris.stott
@cliffordchance.com

102827-4-219-v0.4 UK-0010-BD-CCOM