

**Association of Mortgage Intermediaries (AMI)
Response to FSA Discussion Paper 06/5
FSA Confirmation of Industry Guidance**

AMI is the trade association that represents UK regulated mortgage intermediaries. Membership of AMI is voluntary. AMI currently represents over 70% of Mortgage Intermediary firms in the UK.

Summary

AMI does not support the proposed process for FSA confirmation of Industry Guidance (IG). We do not believe it sits well with FSA's approach to principles-based regulation and will only serve to confuse and divide industry views. There are considerable risks attached to the proposals: for consumers, firms, those who may wish to produce guidance and, indeed, the regulator. These have not been fully discussed in the paper and to proceed without a greater investigation of the "downside" risks would be a regrettable decision. We have teased a number of these risks out, in our response, but others will also be able to identify risks we have not considered (e.g. from the perspective of providers or the banking community). Indeed, a keynote that runs through this paper is that of "risk". Much has been publicly stated about "risk transfer": is the regulator transferring its risk to the industry? It must be acknowledged that the risk profile of any firm opting to follow IG from one source rather than another (when there is competing IG), will increase.

As a parochial point, for any trade body (but especially those at the smaller end of the scale), the risks associated with the transfer of liability, the risk of losing member support if publications are freely available and the additional resource required to deliver IG make the proposals unviable. This is as true for AMI as it is for any other smaller body. We are also concerned that IG could lead to competitive disadvantages for sectors represented by smaller trade bodies.

AMI does not believe there is any clear benefit to consumers in replacing regulatory guidance with a plethora of industry guidance, written with the interests of the IG provider foremost and without the safeguard of open consultation with others who may be affected by the guidance.

We are further concerned that the IG process is predicated on a notion that trade bodies either are, or will become, impartial entities. One of the essential roles of a trade body is to bring about a position which directly benefits its membership and their customers or clients. This can, and does, place them in a position of competition with other trade bodies. A role of a regulator is to judge between the competing positions in order to bring about the best outcome. Even with a requirement for trade bodies to undergo a form of open consultation in the production of IG, we are not convinced that the ultimate output would be as fair to those who are not members of the trade body as it is to those who are.

Additionally, if the only way to challenge the views set out in IG is to query them with the IG provider, and with FSA having no part in the process, what reassurances can any firm (or other stakeholder) have that their views would be listened to and acted upon?

As a final point, if IG proceeds as proposed, we would hope that the current interaction we have with FSA when producing member communications is not disrupted. It would be

a severe blow to AMI and its members if IG intervenes in the productive and professional working relationship that we have experienced with FSA to date.

Current practice

Since its inception, AMI has provided members with information on regulation, legislation and industry matters. This information is provided in different formats, according to its subject matter and objectives. Many communications are to seek members' views on specific consultations or to make members aware of impending changes to regulation. But we also produce what could be described as industry guidance, although we never seek to set standards or dictate how firms should or ought to implement regulatory requirements within their individual businesses. When producing such guidance we invariably ask for FSA's comments to ensure we have interpreted any grey areas or ambiguity correctly and also not overlooked any points that FSA feel would be beneficial to include for members.

This system works effectively and provides an invaluable service to AMI members. Indeed, it could also be argued that FSA have benefited from AMI's ability to clarify matters of importance to members in a timely manner. This has worked to improve the market and ensure firms behave both compliantly and benefit their clients.

We are repeatedly praised by members for the quality, promptness and clarity of our communications. Most important is that many members, particularly smaller firms, value this service far more than the lobbying and representational work that AMI undertakes on their behalf as it is a direct benefit of membership that they see and use on a daily basis. Any dilution of the service will not be welcome and risks loss of membership.

Making our publications freely available would certainly have an impact on membership and could threaten the financial stability of AMI along with other smaller trade bodies. Membership of bodies such as ours is voluntary and firms need tangible reasons to join and remain as members. Our ability to assist them to better understand the regulatory agenda and its direct implications for them is a significant member benefit. If this were to be freely available, firms would not join and that would hinder our ability to assist the sector. Indeed, there is a strong view expressed by many of our members that, if they were to continue to support a trade body, they would be putting themselves at a competitive disadvantage for two reasons. First, firms who are not members are saved the expense of AMI membership – this is money they can use for other purposes (marketing, IT spend etc.). Second, members gathering together to help develop IG, means time away from the business: this is time their competitors can use for the benefit of their own commercial activities. There is no "pay back" for the firm involved in developing the IG, as it must be offered to the industry as a whole for free. Thus, we have had overwhelming member feedback against IG.

Principles-based regulation

AMI supports the general move towards principles-based regulation and accepts that this will mean a reduction in prescriptive rules and detailed Guidance. We welcome the outcomes-focused approach and the flexibility it provides for firms to operate in a way best suited to their business.

The introduction of a formal process for the 'confirmation' and distribution of IG, as proposed in the DP, risks undermining this move and creating uncertainty, confusion and

possible conflict of interest. When should firms follow IG? Whose IG should they follow? What are the consequences of ignoring IG?

It is obvious that under the IG proposals, the risk profile of firms increase.

Consumer confusion?

There are issues that need to be addressed not only in how firms chose to adopt the, potentially, competing sets of IG but also what happens if a consumer complains about a firm. For instance, will a firm chose to disclose that it is following IG, as a marketing-tool? Will there be an implied “seal of approval” in stating that IG exists and the firm is following it? What then, if the firm opts-out of IG or fails to apply it correctly (either through an honest mistake or deliberate action)? Indeed, what if the IG the firm has applied is inappropriate for its circumstances? The question has to be answered of whether IG helps improve the consumers position or worsens it.

There are two schools of thought as to whether IG should be made available to the public. One will say that IG, to be effective, must be publicly available so that consumer can check it and its application against their position. However, there seems to be a growing body of evidence that suggests consumer do not even read the information they receive today, let alone any new texts – which are not even produced by the industry’s watchdog. The second school of thought will state that IG should not be made available to consumers as it is for firms to decide which set of IG they pursue – and not for consumers to second guess their management and risk decisions. On balance, and based on the fact that we are concerned that IG could be mis-communicated to consumers (by being presented as a regulatory protection for them), misunderstood by them, and indeed, ignored, we feel IG should not be publicly available.

If consumers have access to IG they may well provide an unknowing “drag” to the firm: asking if it is complying with a well known provider’s stated view. This makes for interesting competitive tensions which the regulator would do well to examine.

Further, we see little value in the industry producing guidance which is then ‘confirmed’ by FSA, yet has no official status and cannot realistically be relied on as a ‘sturdy breakwater’ when it can be disregarded by an Ombudsman and Compensation Scheme. Consumers could find the IG a firm had relied upon, and explained provided better protection, actually failed to deliver any benefit. For instance, it is easy to imagine a scenario where IG has been produced to help consumers understand the links between a product manufacturer and a distributor in relation to a particular product. This IG sets out the respective responsibilities alongside the rights of the consumers. However, how would the Ombudsman then treat a consumer complaint if a product failure occurred? Given the current regime, the complaint would rest with the intermediary and not be shared with the provider. Thus, a consumer who felt action could be taken against both firms could find themselves misled. This also raises some interesting questions around contract law that the FSA would do well to investigate in connection with IG.

It should be noted that the PI community will also have a view on IG and on whose IG firms should rely. This may drive and shape behaviour, especially in smaller firms. It is easy to imagine a situation where a PI provider feels more able to take comfort in seeing a firm adopt IG which is sponsored by a large trade body, endorsed by major PLCs, and communicated via a PR campaign. A recent example of a lender trade body promoting its view of acceptable practice in equity release is a useful comparison: the guidance

was entirely appropriate for the lending community but entirely wrong for the intermediary sector – yet this did not stop intermediaries coming under pressure to conform to it.

FSA resources and risk

We do not see how FSA can avoid being judgmental and selective in its confirmation process if it is to maintain an orderly market. We find it difficult to believe, for example, that FSA will confirm conflicting guidance where each represents the views and interests of a particular sector.

FSA will need to consider its own resourcing for IG. The process by which it declines to support IG must be open, transparent, and fair on all. However, it is AMI's view that the regulator will be asked to approve IG that is neither “guidance” nor representative of the “industry” – but instead seeks to support the narrow interests of specialist communities or those with particular vested interests.

The appeals process that must be offered to those who complain their IG was not proceeded with will be both costly and a reputational issue for FSA. The number of Freedom of Information requests around the IG decisions will, alone, be considerable.

An interesting question has been raised by members regarding a trade body's relationship with the regulator. Currently, trade bodies are free to engage with the regulator fully on behalf of their members: this means having a constructive and (when appropriate), critical relationship on both sides. However, does this relationship change if a trade body needs to gain FSA's support for IG? Does it hinder the trade body's ability (and prerogative) to criticise? Whilst those well connected with the regulator/trade body relationship will know this could not be the case, those who are more distant could worry about the independence of their trade body.

Finally, we also feel that FSA cannot walk away from its duty to offer firms assistance in complying with its rules. To state that those who take issue with IG must raise it with the producers of the guidance risks allowing firms to be misled: with the ensuing consumer detriment.

In summary, we believe that IG is a weak substitute for FSA Guidance and that it presents a transfer of responsibility from the regulator to industry. The move to a more principles-based regulation is supposed to encourage regulated firms to take more responsibility as appropriate to their individual businesses; these proposals risk undermining that flexibility.

Liability and reputational risk

The parameters proposed by FSA require IG providers to:

- Take responsibility for the content and updating of IG. *This represents a clear shift of responsibility to the industry and exposes providers of IG to legal liabilities beyond those currently incurred. For example, all AMI publications carry a disclaimer that we cannot be held responsible for firms following, or deciding not to follow, any considerations, suggestions or recommendations set out in our publications. Any change of practice that incurs liability will require additional finance and resource. This alone creates a legal and financial barrier to smaller trade bodies with limited resources, in addition to the potential impact of making*

IG freely available. Larger organisations producing IG to suit their market will not suffer from the same constraints and the impact could be to create a two-tier system, which could be viewed as anti-competitive.

- *Relate IG to specific rules or principles and directly link to FSA requirements. The appropriate application of FSA rules or principles is a basic compliance function that should be undertaken by all regulated firms.*
- *Highlight any 'gold-plating' i.e. best practice. Whilst we support raising standards we question whether it is appropriate for FSA to confirm IG that provides examples of higher standards even if it mentions that they exceed regulatory standards?*
- *Consider liaison with consumer bodies. Aligning consumer interests with those of our members is a natural process in the IFA sector but any requirement to consult consumer bodies will inevitably delay provision of IG, which could be detrimental when we need to communicate quickly with members.*
- *The process for obtaining confirmation will involve prior notification, and "review and sign-off by several areas within FSA". This raises further issues of delays and there will inevitably be instances requiring discussion and negotiation before confirmation is granted. Once in the system, should there not be agreement, a firm will have no option but to withdraw the guidance. To publish IG with a disclaimer that FSA confirmation had been sought but declined, would be a high risk strategy. If discussions become protracted and compromises reached, is this not 'closed door consultation'. (We have already experienced larger trade bodies being supported by FSA in producing IG without open consultation through MiFID Connect). Will this process represent fair allocation of FSA resources?*
- *IG should help firms meet their regulatory obligations, not tell them what to do. We fully support this approach as it is what we currently do but without the onerous process.*
- *IG must be publicly available. As stated, we firmly believe that this would potentially reduce membership as members will be reluctant to pay fees when they are able to receive a valuable benefit free of charge. The impact could create a vicious circle of - less resource leading to fewer publications leading to fewer members leading to less resource etc.*

Electing not to seek confirmation of IG raises concern about the public perception of those who chose not to participate. Will the absence of FSA confirmation on trade body guidance reduce its value? Will 'confirmed' IG carry more weighting than unconfirmed in the eyes of firms, consumers and FOS?

Practical implications

As stated, AML produces a significant amount of information to members. Our factsheets have been especially well received by members, providers and commentators. Most of the content is factual, although we may express our views on market practice and options, and recommend that firms consider whether and how they might conduct business. This falls short of setting standards, examples of good and bad practice or recommending a 'one size fits all' approach to business as we firmly believe that firms must make decisions appropriate to their particular business model. This is particularly important in the retail intermediary sector where there are significant differences in the types of firms, nature of business and customer base.

But we also cover, where relevant, clarification of regulatory requirements. A good example would be our factsheet on Pension Term Assurance which provided clarity to a very confused market on the rules applicable to the sale of this product.

We have no idea how FSA will deal with publications which include material which would not be defined as industry guidance, such as factual and market commentary but also includes clarification of FSA rules. We do not think attempting to divide comprehensive information into that which could be defined as guidance and other is either practical or desirable.

Costs

Specific mention must also be made of the costs of producing IG. We are greatly concerned about the additional costs trade bodies and others are being asked to shoulder in producing IG. Factors to be considered include: additional PI cover, extra legal expense (for drafting and review), member and executive time, production/publication costs, etc. The expectation that trade bodies would consult each other, consumer groups, the regulator, in steering the process to produce IG comes with a heavy costs.

As part of the costs/benefit analysis which any proposals to introduce IG must be accompanied by, the FSA should set out how much it spends on the consultative process to arrive at its guidance and rules. Given the expectation that there will be more guidance, from far more organisations than just the FSA, the costs of the exercise will become hugely significant for the industry – as they will ultimately be picked up by the consumer. A full CBA is essential in determining whether IG should proceed.

An example of a specific costs related worry can be seen in the establishment and operation of MiFID Connect. This organisation, consisting of trade bodies and other interested parties, played a significant part in the development of thinking on MiFID. It has been judged as playing an influential role in assisting policymakers implement the Directive's requirements in the UK. However, entry into the group was only possible via a significant payment (£10,000).

If further groupings were to be established as regular "IG fora", smaller trade bodies could easily find themselves unable to serve their members interests. Whilst this could lead to poorer IG being produced, the domestic and European competition authorities may become concerned about the market impact of such groupings and the regulator's attitude to their lobbying.

Specific questions

Q1. Do you anticipate the demand for 'FSA confirmation' from providers of Industry Guidance will be significant?

From our discussions with other trade and professional bodies, there appears to be mixed views, with some far keener to produce guidance than others. From AMI's perspective, if industry guidance proceeds as proposed, we intend to continue to produce supporting material for members but are only likely to seek confirmation in exceptional cases.

This could create a distortion in the market with FSA confirming guidance from one part of the value chain without the opportunity for comment or agreement from another part. Consultation on FSA Guidance allows views from all affected parties to freely state their support or opposition to change. On many occasions, consultation has highlighted impracticalities or unintended consequences of proposals, even at Guidance level, and it is essential that this transparency and ability to comment continues. Will, for example, FSA allow AML to see or comment on guidance produced by another trade body (where the guidance may impact on our sector) before 'confirmation'?

We strongly recommend that FSA restricts access to a confirmation process to providers of industry guidance to not for profit organisations. It should not be assumed that those with commercial interests will not wish to seek confirmation as making their guidance publicly available would not be attractive. Compliance and legal firms who allow a limited amount of 'FSA sanctioned' guidance into the public domain will no doubt use this to add credibility and standing to their services. An FSA 'seal of approval' should not be used to promote or market commercial activities.

Q2. Do you agree with our proposed parameters for considering whether we should grant 'FSA confirmation'? If not, why not?

No. The parameters proposed create a formal approach to producing guidance which appears to place all responsibility on the provider without the reassurance that the guidance carries the same immunity as FSA Guidance. Providing IG puts increased liability on the organisation by exposing it to wider risks and potentially, unintended consequences as detailed above.

Q3. Do you agree with our proposed approach to facilitate the use of Industry Guidance? If not, why not?

There are particular areas where we fear FSA's approach could create problems. FSA produces a significant amount of support material for small intermediary firms. This is helpful for members and we hope this will continue. FSA publishes case studies, examples of good and bad practice, and more recently 'key rules' to help firms focus on areas where FSA feels firms need the most support. This is initiated by thematic work and monitoring. How does IG fit into the picture? Are firms to consider all examples of good and poor practice? Which is more important, FSA information produced for small firms or FSA confirmed IG? IG may be confirmed at a point in time but if it is no longer appropriate the provider has to withdraw or amend it. What will happen if a provider decides to stop providing IG? FSA can withdraw IG if it considers it no longer appropriate but at what point does it no longer hold good?

Q4. Do you have any other comments on our proposals?

FSA's desire to enable IG to flourish is positive. However, this can only be achieved if it is produced in a timely, efficient, cost-effective manner which then allows firms a greater level of certainty in their decision-making than existed without IG.

Regulatory guidance is best produced by the regulator. The FSA has the resources, impartiality and confidence of the industry. Recent moves, such as the key rules, are where resource should be applied. If individual trade bodies, or parts of the regulator's flock, require specific guidance, it should be for them to make the case to the regulator in

the channels that already exist. Establishing a formal pathway for IG simply diverts FSA resource that would be better employed elsewhere.

A final thought is that IG could lead to a worsening of consumer protection and a growing misunderstanding of the regulatory safeguards consumers enjoy. For these reasons we do not support the proposals on IG.