FINANCIAL REGULATOR
Rialtóir Airgeadais

Consumer Protection Code

REGULATORY IMPACT ANALYSIS

December 2005

This document does not form part, or provide an interpretation, of the Consumer Protection Code or any other code, requirement or provision of law or regulatory practice the subject of the exercise by the Financial Regulator of its functions.

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1 PREFACE

In July 2005 the Department of the Taoiseach published a Report on the Introduction of Regulatory Impact Analysis (RIA). This was followed by more detailed guidelines in October 2005. The application of that report and guidelines is specifically directed at Government Departments and Offices, and consequently the guidance that it contains is of direct relevance only to those entities. Nevertheless the Financial Regulator, cognisant of the value that an RIA exercise can bring to bear on decision-making, and in light of the significance of the Consumer Protection Code (the Code) for both industry and consumers, decided to conduct and publish an RIA.

The Department of the Taoiseach's report envisages that, in relation to any new regulatory initiative, an RIA should be conducted as early as possible. However, as the Financial Regulator commenced its review of the current codes in 2003, many of the processes and consultations relevant to the development of the Code had already been undertaken by the time the Department's report was published.

The approach that the Financial Regulator has adopted in relation to this RIA, and perhaps more particularly in relation to looking at the costs and benefits of the Code, was influenced by a number of sources, principally:

- The Department of the Taoiseach's report on the introduction of RIA in the Civil Service,
- Best international practice in relation to RIA and financial consumer protection and information regulations, and
- A review of the academic research and papers published in this field.

The use of RIA as an analytical tool is only commencing in Ireland and the approach will no doubt evolve over time.

2 INTRODUCTION

The introduction of the new Code has been the subject of a comprehensive consultation with all interests affected (see Section 4). This meets a fundamental principle of the approach set out in the Government's "Better Regulation" initiative.

The Financial Regulator published a draft Consumer Protection Code (the Code) in February 2005. Following a consultation process the Financial Regulator is now moving to finalise and implement the Code. It is intended that the Code will come into effect in mid-2006

The Code will replace the various sectoral codes that currently apply to regulated firms, most of which were introduced prior to the establishment of the Financial Regulator, namely:

- credit institutions;
- insurance companies;
- insurance and investment intermediaries;
- investment business firms;
- deposit agents;
- mortgage intermediaries; and
- moneylenders.

The Code will apply to all financial services providers when operating in the State[1]. In line with the structure of the European single market in financial services these firms fall into three main groups:

- those authorised by us, the Financial Regulator;
- those authorised in another European Union (EU) or European Economic Area (EEA) country that have at least one branch in Ireland ('establishment firms');
- those authorised in another EU or EEA country that provide services into Ireland without setting up a physical presence in the country ('passporting firms').

The types of financial services providers to whom the Code will apply are:

- Credit Institutions (Banks and Building Societies)
- Insurance Companies (both Life and non-Life)
- Stockbroking Firms[2]
- Investment Business Firms
- Insurance Intermediaries
- Moneylenders
- Mortgage Intermediaries
- Credit Unions when providing financial services other than core savings and loans to members.

[1] As noted in the Public Response document, the Markets in Financial Instruments Directive (MiFID) may have an, at this point unquantifiable, impact upon the Code.

[2] The advertising section of the Code will apply to stockbrokers. Supervision of compliance with the conduct of business rules for stockbrokers, other than advertising rules, is currently undertaken by the Irish Stock Exchange as provided for by the Stock Exchange Act, 1995. The rules are subject to the approval of the Financial Regulator. The Irish Stock Exchange is aware that the review of codes by the Financial Regulator is underway and that the outcome of the review and public consultation will have implications for the provisions set out in its rules. The Financial Regulator will, in conjunction with the Irish Stock Exchange, review the conduct of business rules applicable to stockbrokers with a view to ensuring an approach and level of protection for investors consistent with this Code.

Statutory Basis of the Code

The Code is issued in accordance with Section 33S(6) of the Central Bank Act, 1942 (as amended) and applies to entities regulated by the Financial Regulator by virtue of powers derived from the following pieces of legislation:

- Central Bank Acts 1942 – 1997
- Investment Intermediaries Act 1995
- Consumer Credit Act 1995
- Stock Exchange Act, 1995
- Insurance Acts 1909 – 2000
- Relevant Statutory Instruments

Background and Scope Of This Regulatory Impact Analysis (RIA)

As mentioned above the approach adopted by the Financial Regulator in the development of the Code, and the structure of this RIA, is influenced by the model set out in the Department of the Taoiseach's report. It should be borne in mind however that the development of the Code was well advanced by the time the report was published.

The Department of the Taoiseach's report provides that an RIA should, inter alia, consider enforcement and compliance issues. The Financial Regulator is aware that a code can only be effective when it is properly enforced and if compliance with it is monitored regularly. The Code will require all regulated entities to have adequate systems and controls in place to ensure compliance with the Code and other applicable consumer protection legislation. Responsibility for compliance rests with the board and management of a regulated entity. The Financial Regulator will monitor compliance by various means including a consumer focussed inspection programme, mystery shopping, through information brought to its attention by customers and by ensuring that directors and managers are fully responsible for compliance with the Code. A breach of the Code will be liable to be the subject of an administrative sanction under Part IIIC of the Central Bank Act, 1942.

Prior to the publication of the Department of the Taoiseach's report the Financial Regulator had decided that the issues surrounding enforcement of and compliance with the Code were of sufficient significance and complexity to warrant a separate consultation.

In November 2004, the Financial Regulator published a consultation paper entitled "Financial Services Regulation: Administrative Sanctions Procedure" (consultation paper CP8). This paper sought the views of the financial services industry, their advisors, the Financial Services Consultative Industry and Consumer Panels and all interested parties. The paper concentrated on the approach to be taken to the application and implementation of the new administrative sanction powers and sought views on policies which the Financial Regulator was considering applying. Draft guidelines were included in the consultation for comment. We received 23 written submissions to that consultation: 12 from industry representative bodies, 4 from regulated entities, 5 from advisors to the financial industry and 1 each from the Financial Services Consultative Industry and Consumer Panels.

On 19 August 2005 the Financial Regulator published its response to the feedback received in relation to consultation paper CP8 on Administrative Sanctions Procedures. In October 2005 the Financial Regulator published the final version of An Outline of the Administrative Sanctions Procedure, which is a general summary of the process that will be followed. The Financial Regulator also published an Administrative Sanctions Guideline which governs the conduct of the Administrative Sanctions Procedure.

3. OBJECTIVE AND RATIONALE FOR THE CONSUMER PROTECTION CODE

3.1 Objective of the Code

The objective of the Code is to promote high standards of behaviour on the part of regulated firms and to promote appropriate outcomes for consumers of relevant financial services.

The Code is not intended to displace competitive pressures or normal market mechanisms, but to correct for market imperfections and failures that produce sub-optimal outcomes and distort consumer choice.

While the Code is intended to protect consumers, it is not the purpose of the Code to protect consumers from all possibility of losing money from, for example, adverse market movements, or from making mistakes.

3.2 Why is a Consumer Protection Code needed?

The Financial Regulator's Code will be part of the overall regulatory and supervisory regime applied to relevant financial services in Ireland. The wider question of why it is necessary to regulate financial services should include a consideration of issues such as the potential for systemic risk and fraud. We try to address these risks through the Financial Regulator's prudential supervision framework including the authorisation process and competency and probity standards, and it is not considered necessary to address this wider question in the context of this RIA. It is accepted however that the rationale for a consumer protection framework, expressed in a formal code, needs to be justified on its own merits, separately from systemic risk and fraud concerns.

The Financial Regulator considers that the principal factors that warrant a Consumer Protection Code are:

1. The process of delivering financial services is particularly prone to issues of asymmetric information. Consumers are far less well informed about financial products than the providers of those products. In fact many potential buyers of retail financial products may not even know what it is that they do not know. In the absence of complete information necessary to make informed choices, competition alone will not produce optimal outcomes for consumers;

2. Many financial contracts (e.g. insurance, pensions etc) are long term in nature, and the consumption of the service is at a time other than the point of purchase. Consumers may have particular difficulty in ascertaining the quality of financial products at the point of purchase. This gives rise to particular concerns to ensure the suitability of sales, and that vendors act in the long-term best interests of their clients; and

3. Financial services, by their nature, may be more susceptible to fraud, malpractice and misrepresentation than other services. Consumers generally release control of an asset (e.g. their cash) but do not take control of the purchased asset, relying on the periodic statements issued by financial firms confirming their purchase. Retail consumers are generally not in position to critically evaluate the competence and probity of those working in the financial services sector[3].

(These points are expanded upon in Chapter 5, Policy Options)

[3] The Financial Regulator has issued a consultation paper (CP11) entitled: Comprehensive Framework of Standards for testing the probity and competence of Directors and Managers of Financial Services Firms. This consultation paper focuses in greater detail on issues of competence and probity, however this theme is also reflected throughout the Code.

The Financial Regulator considers that a single Code, containing general principles that apply to all regulated firms, and detailed rules for certain financial services where appropriate, is preferable to a series of codes for each sector for a number of reasons:

1. A single Code is consistent with the Government's "Better Regulation" initiative, particularly the principles of transparency and consistency;

2. The Financial Regulator considers that whether a consumer buys, for example, an investment product from a bank or an insurance broker, the duty of care to the consumer should be the same; and

3. By focussing on types of financial services rather than types of financial firms the Financial Regulator is facilitating the creation of a level playing field among financial firms, and minimising the impact of the Code on competition between different types of firms.

4 CONSULTATION

The Financial Regulator has engaged in extensive consultation with industry and the public in general during the Code development process. This process has comprised of a restricted consultation in relation to interim codes, two full public consultations, and consultation with the statutory Consultative Industry and Consumer Panels. In addition the Financial Regulator has held over thirty meetings with industry and consumer representatives on the Code.

4.1 Interim Codes Consultation

Prior to the establishment of the Financial Regulator on 1 May 2003 the Central Bank of Ireland had put in place Codes of Conduct for credit institutions, insurance and investment intermediaries, investment business firms, stockbroking firms[4] and deposit agents. In December 2003 the Financial Regulator introduced interim codes for insurance companies, mortgage intermediaries and moneylenders. Because of the interim nature of these Codes the Financial Regulator conducted a restricted consultation in relation to those interim Codes. The trade bodies representing the affected sectors were the principal consultation partners.

4.2 Public Consultations

In March 2004 the Financial Regulator published a public Consultation Paper CP2 entitled "Review of Conduct of Business Rules for Financial Services Providers". This paper sought the views of the financial services industry, its customers and consumer representative groups on codes of practice that would help protect consumers in their dealings with financial services providers. The paper concentrated on the structure, application and general content of future consumer protection codes rather than on the detail of the individual rules. The Financial Regulator received 42 submissions on that paper - 18 from regulated entities, 13 from trade representative bodies and 5 from consumer groups. Six individuals also made submissions. The submissions received are available on the Financial Regulator's web-site www.financialregulator.ie. The Financial Regulator's response to the submissions made was set out in Consultation Paper CP10.

Consultation Paper CP2 asked two key questions:

1. should the Code be principles based or rules based?
2. should the Code be structured by reference to products or regulated entities?

On the question of principles versus rules there was an almost unanimous preference for a principles based approach but most respondents felt that the principles should be supplemented with more detailed rules that would more clearly facilitate an understanding of the Code by both the practitioners and customers.

Most respondents favoured a Code structured under various product types rather than by regulated entity type. The key arguments in favour of this approach were:

a) there has been a blurring of the distinction between providers of financial services;
b) our stated aim to provide the same level of protection for customers regardless of the type of financial services provider they choose; and
c) customers are interested in the service provided rather than the legal classification of the provider or seller.

[4] The Irish Stock Exchange was, and continues to be, involved in the implementation and monitoring of the Code of Conduct for member firms.

The third phase of consultation was the publication in February 2005 of a draft Consumer Protection Code (Consultation Paper CP10). Consultation Paper CP10 developed the Financial Regulator's proposals in relation to the detailed content of the Code. It comprised a set of general principles and some rules common to all regulated entities. It then addressed different types of financial services such as banking, lending, insurance and investments. Rules relating to the advertising of financial services were also included.

Sixty one submissions have been received in relation to Consultation Paper CP10. The submissions, which have been published on the Financial Regulator's website, can be broken down as follows:

	Number of submissions
Bodies representing financial services firms	19
Individual firms	27
Consumer groups and groups representing social and community interests.	9
Members of the public.	3
Other statutory bodies[5]	3
Total	**61**

The Financial Regulator has published a document giving feedback on the most significant issues raised in the consultation process at the same time as it has published this Regulatory Impact Analysis. We accept that the detailed Code requires further technical work to avoid misinterpretation and to allow for it to be implemented in the most efficient way. This work is continuing and the final Code will be published in the first half of 2006.

4.3 Consultation with the Consultative Industry and Consumer Panels.

The fourth element to the Financial Regulator's consultation process has been its discussions with the statutory Consultative Industry and Consumer Panels. These Panels were established with effect from 1 November 2004 under the Central Bank and Financial Services Authority of Ireland Act, 2004.

Both the Consultative Consumer Panel and the Consultative Industry Panel made written submissions to the Financial Regulator in relation to the Code. The Financial Regulator has met with each of the Consultative Panels in order to discuss their inputs and to give them structured feedback. Prior to the publication of the final Code the Financial Regulator will respond formally to both panels, and these responses will also be published on our website.

[5] The Advertising Standards Authority of Ireland, The Pensions Board and The Competition Authority.

5 POLICY OPTIONS

An important element of an RIA is an assessment of the various policy options available to the regulator and an objective evaluation of the merits and demerits of each option. At a conceptual level there are three possible approaches to regulation:
a) do nothing;
b) self regulation; and
c) statutory regulation.

For the purposes of this RIA it is suggested that the policy option of doing nothing does not warrant extensive consideration. An Implementation Advisory Group appointed by the Ministers for Finance and Enterprise, Trade and Employment considered the arguments for and against creating a single regulatory authority in Ireland, and the roles and functions of such an authority. The report of that Group was published in May 1999 and the Government subsequently moved to establish the Financial Regulator. A significant factor in the Governments decision was the desirability of providing better information and protection to consumers.

The rationale for conduct of business rules has already been discussed briefly and is expanded upon hereunder. This chapter also considers the question of self-regulation versus statutory regulation. The policy options of principles versus rules-based regulation are also examined.

The merits and demerits of various policy options discussed in this chapter are common to many markets and are not specific to the financial services industry in Ireland.

5.1 Rationale for Conduct of Business Rules

The logic for the introduction of conduct of business rules is based on a number of arguments:

I The correction of market imperfections and failures.

Among the market imperfections observed in retail financial markets are:

- the inadequacy of information possessed by consumers;
- the fact that consumers of financial services are less well informed than the suppliers of those services;
- the difficulties that consumers face in ascertaining quality at the point of purchase;
- imprecise definitions of products and contracts; and
- the difficulties faced by consumers in trying to assess the safety and soundness of financial institutions.

It is the view of the Financial Regulator that these market imperfections cannot be addressed by consumer information and education alone, and that conduct of business rules must of necessity form part of the Financial Regulator's approach to addressing these issues.

II Professional Standards

Aside from deliberate mis-selling[6], consumers can be mis-sold a financial product because the person selling the product does not fully understand the product in question, or because he/she does not fully understand the consumer's needs.

[6] Deliberate mis-selling is addressed by the Financial Regulator's requirements that regulated firms must know their clients and only sell suitable products to those clients.

The Financial Regulator is currently addressing this issue in a number of ways. A consultation paper (CP11) was published in February 2005 seeking views on the development of a comprehensive framework of standards for testing the probity and competence of directors and managers of financial services firms.

The Financial Regulator has also co-operated with the financial services industry in the development of minimum training standards within the industry. However these initiatives need to be complemented by conduct of business rules that impose standards requiring firms to adequately know their clients and to recommend suitable products for them.

III Fraud or misrepresentation

The very nature of financial services, dealing in the financial assets of consumers who are sometimes poorly informed about financial issues and processes, means that financial services offers greater opportunities to those who would defraud or misrepresent themselves to consumers than many other industries. One of the effects of conduct of business rules is to make it more difficult for the unscrupulous to operate in the financial services industry.

IV Conflicts of interest

The process of delivering financial services to consumers gives rise to a number of potential conflicts of interest. The interests of consumers are not necessarily the same as the interests of the financial service providers. It is in the interests of financial services providers, in order to protect their reputations and in order to promote repeat business, to ensure that consumers are satisfied with their products. However the interests of other stakeholders must also be taken into account by each firm in determining its business strategy and practices.

There is also the scope for a mis-match in the time horizon of consumers and financial service providers, especially in the area of pensions and investments, where the consumer's desire for medium to long-term benefits can conflict with the financial service provider's needs to meet shorter term income and/or profitability targets.

Further potential for conflicts of interest arises from the fact that many categories of retail financial intermediaries who, though they act on behalf of the consumer in their dealings with product providers, are in the main remunerated by the product providers by way of sales-linked commissions.

The Code gives firms guidance on how to address conflicts of interest in a uniform manner.

V Consumer Confidence

In a market where consumers know that there are good products and bad products, and also know that they do not possess the expertise to differentiate between the two, demand for these products can be weak, and risk-averse consumers can fail to participate in or exit the market. The response on the part of financial services providers can sometimes be to place a greater emphasis on selling than on improving the quality of products offered. Regulation can give risk-averse consumers confidence about the quality of the advice they receive and the quality of the products on offer (albeit that the Financial Regulator does not approve or endorse particular financial services and products).

5.2 Self-Regulation or Statutory Regulation

Section 33S(6) of the Central Bank Act 1942[7], provides that, with the approval of the other members of the Regulatory Authority, the Consumer Director of the Financial Regulator may issue codes or impose requirements under regulatory legislation.

The effect of this provision is to enable, but not to require, the Consumer Director to implement provisions such as are contained in the Code. The Consumer Director could, in theory, hold back from exercising this power, and in those circumstances self regulation could continue to play the pre-eminent role in guiding the behavior of financial firms in their dealings with consumers.

The most significant positive attributes of self-regulation can be summarised as follows:

- it capitalises on the expertise of market practioners;
- it has a professional interest in ensuring that standards and public confidence are sustained; and
- the consent of the regulated is more likely to be secured.

The more significant negative attributes of self-regulation are considered to be that:

- it can prove to be anti-competitive in nature[8];
- it can be vulnerable to regulatory capture[9];
- not every firm may subscribe to the self-regulatory framework;
- it may lack credibility, accountability and public confidence; and
- it may lack effective enforceability.

Turning to Statutory Regulation, the principal advantages of placing a code of conduct on a statutory footing are;

- the regulator is independent of the industry that it regulates and is in a better position to balance the interests of consumers and firms appropriately;
- an impartial regulator is more likely to be able to engender consumer confidence;
- a statutory code, with an enforcement dimension, is more likely to be effective;
- a statutory code is more likely to be designed to enhance competitive pressures; and
- a statutory code enjoys legal clarity.

The more significant negative attributes of statutory regulation are considered to be that:

- the regulator does not have market experience comparable to that of practitioners;
- as with self-regulation, the regulator is vulnerable to regulatory capture;
- a statutory regulator may be slower than a self regulatory body to react to market developments.

The Financial Regulator addressed the question of the appropriate role of voluntary codes in consultation paper CP2, published in March 2004. Many respondents felt that voluntary codes have a role in a regulatory framework by complementing the statutory codes. There were concerns however, about the effectiveness of the enforcement of voluntary codes.

[7] As inserted by The Central Bank and Financial Services Authority of Ireland Act, 2003
[8] For example, membership of a self-regulating body may constitute a barrier to entry to a market.
[9] 'Regulatory capture' is a phrase commonly used to describe a situation in which an industry that is regulated controls a regulatory agency's policies.

The Financial Regulator considers that, going forward, there will continue to be an important role to be played by voluntary codes, and that the optimal regulatory matrix lies at neither end of the spectrum between exclusively self-regulation and exclusively statutory regulation. The Financial Regulator considers that the Code represents an appropriate degree of statutory regulation.

Following the introduction of the Financial Regulator's Code there will most likely continue to be a number of industry codes in operation. Examples include:

- the Irish Bankers Federation/Irish Mortgage Council's code of ethics; and

- the many Codes of Practice of the Irish Insurance Federation in relation to issues such as genetic testing and life insurance medical reports etc.

5.3 Principles Vs Rules

A principles based approach sets out high level requirements within which financial services firms operate, while a rules based approach is more prescriptive in relation to the requirements that should be implemented in specific circumstances. The codes that were in force at the time that the Financial Regulator was established were primarily principles based rather than comprising a set of detailed rules. They set out how each regulated entity should behave in a particular set of circumstances, although certain requirements were presented in more detail than others.

The Financial Regulator has expressed a preference to continue with this principles based approach and to supplement those principles with specific rules where it is considered to be in the best interests of consumers to do so. This issue was raised by the Financial Regulator in consultation paper CP2 published in March 2004. In that consultation paper the arguments for and against principles and rules based regulation were summarised as follows:

The arguments in favour of a principles based approach are that:

- it allows financial services firms a certain flexibility to develop their own compliance ethos within the context of their own markets, legislative backgrounds and cultures;
- it encourages firms to embed the ethos of the Codes within the firm rather than develop a box-ticking culture of compliance with detailed rules;
- it is more likely to encourage new entrants into the market, particularly from outside the State, and thus foster competition.

The main arguments against a principles based approach are that it may create uncertainty:

- for firms that may be unsure if the approach adopted fully complies with the codes; and
- for consumers who are faced with different approaches to compliance from different firms.

The arguments in favour of the rules based approach are that:

- it makes it clear to financial services firms how they should comply with rules in specific cases; and
- it is more likely to lead to a consistent approach between different firms, so consumers are aware of the level of compliance they can expect.

The arguments against a code comprising detailed rules are that it:

- may lead to an unthinking mechanical compliance culture rather than a realisation that the purpose of the codes is to promote the fair treatment of consumers;
- may prompt firms to seek ways around rules rather than complying with the principles of consumer protection;
- can restrict innovation and impose additional costs on financial services firms and perhaps ultimately consumers;
- might create uncertainty for companies that are faced with a situation for which no specific rule or requirement has been decided, This will invariably happen as no set of rules could cover every conceivable eventuality.

Consultation paper CP2 sought views on:

- the merits of a principles based versus a detailed rules approach; and
- any areas in which more detailed rules would be more appropriate or could be used to supplement the high level principles.

There was an almost unanimous preference for a principles based approach but most respondents felt that the principles should be supplemented with more detailed rules that would more clearly facilitate an understanding of the Code by both the practitioners and customers. Some industry respondents felt that with the development of the administrative sanctions programme it was important that the Code be drafted in such a way to enable them to develop compliance systems that would withstand regulatory scrutiny.

The Financial Regulator continues to favour a principles-based code. A rules-based Code would impose considerable costs on honest and reputable firms but would not adequately deal with firms that do not subscribe fully to the spirit of the Code.

The final Code therefore sets out both general principles and some detailed rules, which are an elaboration of those general principles, where this is considered necessary.

6 COSTS AND BENEFITS

6.1 Methodology

The most compelling rationale for considering the costs and benefits of initiatives in the area of financial regulation lies in the nature of regulation itself, in that because regulation is not provided through a normal market mechanism consumers are unable to signal how much or what quality of regulation is required. Consumers are also unable to signal how much they are prepared to pay for regulation. This represents a major loss of information to the provider of any service, financial regulation included.

For the vast majority of financial firms providing services to retail consumers the opportunities to engage in regulatory arbitrage are non-existent. The absence of meaningful arbitrage opportunities means that a second possible source of information on pricing is also unavailable.

In approaching this examination of the costs and benefit it is important to define the baseline relative to which the costs and benefits of the Code are measured. The Financial Regulator considers that the most relevant baseline is what would happen if there were no regulation of conduct of business, and therefore it is the same as the "do nothing" policy option.

When we began to look at costs and benefits in the context of financial regulation generally it quickly became apparent that while it can be relatively easy to quantify a small number of costs, the same does not hold true for benefits, which at best can be assessed in qualitative terms. Without prejudice to the outcome of an examination of costs and benefits the Financial Regulator recognised this limitation, which is also evident from the work of other regulators and from relevant economic literature. The difficulty of quantifying costs and benefits is acknowledged in the RIA Guidelines issued by the Department of the Taoiseach.

Our approach to the issue of identifying the costs and benefits of the Code is to focus on the incremental costs that compliance attracts and the incremental benefits that the Code brings, over and above the costs and benefits that would be likely to obtain if there were no Code. We believe that this approach is the most appropriate and valid for considering the costs to industry of implementing a new and industry-wide consumer protection Code.

The Financial Regulator engaged with the Consultative Industry Panel, with industry representative bodies and with individual firms to see if the incremental costs to industry of implementing the Code could be quantified with an acceptable level of accuracy.

We have found that estimating these costs is not easy - one of the obvious difficulties with this approach is that there may not be consistency of views within industry on the level of activities covered by the Code that would still be undertaken absent a Code.

Estimates of set up and ongoing implementation costs in respect of a sample of provisions were put forward by the industry. These estimates suggest a significant cost attaching to the implementation of CP10.

Both the industry and the Financial Regulator acknowledge that the cost exercise was conducted in an extremely tight timeframe, which only allowed a minimum of discussion on devising the cost template to be completed, and which did not allow for validation of the data. It has not therefore been possible to verify the robustness of the cost data provided.

We accept that implementation of new provisions and the extension of existing provisions to new sectors or business lines will have tangible cost impacts. We will seek to minimise these cost impacts where possible.

Arising therefore from our communications with industry, and also cognisant of the similar difficulties experienced in other jurisdictions in estimating the costs and benefits of financial consumer protection measures, the Financial Regulator has accepted that, despite its efforts and the efforts of industry, it would not be possible to offer precise, or even reliably approximate figures describing the incremental costs to the industry of the Code.

The Financial Regulator acknowledges that the application of RIA, and in particular costs and benefits analysis, to consumer protection measures is at an early stage of evolution. We will continue to endeavour to keep abreast of international best practice in this area, and we will also continue be open to suggestions from industry on how appropriate analytical tools can be developed.

The Financial Regulator considers that in the case of future Codes initiatives it would be appropriate to use the costs and benefits analysis in this RIA as a baseline, and that accordingly the costs and benefits of future initiatives will be measured against the standards imposed under the Code.

The reliable quantification of costs to consumers of financial products of having a Consumer Protection Code also presents similar difficulties at the practical level as the quantification of industry costs.

Turning to benefits, from the outset it appeared to the Financial Regulator that the possibility of quantifying the benefits of the Code, both to consumers and to industry, was an even more remote prospect than quantifying costs. For example, one of the purposes of the Code is to help ensure that consumers are only sold appropriate products, but it would not seem possible to ascribe a monetary value to a mis-selling event that does not take place. Similarly, a proportionate and effective code should benefit the regulated industry by enhancing consumer confidence in the products and services offered. Offering a reliable measurement of this benefit is however probably not feasible.

The only costs that could arguably be described accurately are the direct costs incurred by the Financial Regulator in devising, monitoring and implementing the Code. These costs, which are borne in the first instance by the industry and the Central Bank and Financial Services Authority of Ireland, and ultimately by consumers, could be stripped out of the Financial Regulator's budget and be presented in this RIA. The Financial Regulator considers however that it would be invidious to do so as it would arguably deflect focus towards these definable costs and away from the indefinable costs and benefits.

Given that the draft budget of the Financial Regulator is subject to scrutiny by the Consultative Industry Panel and the Consultative Consumer Panel, and is subject to the approval of the Minister for Finance, and given that the accounts of the Financial Regulator are reviewed by the Comptroller and Auditor General, and are published, it is considered that no additional transparency or benefit would accrue from expressing these costs in this RIA.

Taking all of these factors into account the Financial Regulator considers that approaching the question of the costs and benefits of the Code from a purely accountancy perspective is not feasible. We note that this has also been the conclusion arrived at in other jurisdictions. In a review of the efficacy of financial regulation in the United Kingdom one noted expert has expressed the view that "it is difficult to come to any other conclusion except that the achievement of the objectives which have been set for the FSA are non-operational in the sense that no measurement of success can be achieved" [10].

Notwithstanding this, we consider that it is best practice to try, in a structured way, to identify, and where possible, to comment on the significance of the principal market impacts of the proposed Code. Not to do so would run the risk of implementing a Code that might address the given policy objectives, but was not as efficient as it could be.

[10] Charles A.E. Goodhart, "Regulating the Regulator – An Economist's Perspective on Accountability and Control, published in Regulating Financial Services and Markets in the Twenty First Century (2001) (Eilis Ferran & Charles A.E. Goodhart, eds).

6.2 Summary of main costs and benefits

Some of the principal costs and benefits of the Code are summarised in the following table, and then discussed in more detail.

	COSTS	BENEFITS
CONSUMER	▪ Reduction in choice because of harmonisation of products; ▪ Funding costs ultimately borne by the consumer.	▪ Assists in delivering to consumers what it is that they think they are buying; ▪ Creates a greater number of close-to-optimal outcomes; ▪ Fewer incidents of product mis-selling; ▪ More competition leading to better value for consumers.
INDUSTRY	▪ Information technology costs; ▪ Staff costs, including training; ▪ Supervision fees.	▪ Market stability, facilitating long-term planning; ▪ Greater consumer confidence; leading to greater business volumes; ▪ Internationally recognised regulatory standards.

The costs of the Consumer Protection Code can be considered in terms of four categories:

1. direct costs to industry;
2. compliance costs to industry;
3. implementation timeframe; and
4. costs to consumers.

6.2.1 Direct Costs to Industry

These are the costs, borne in the first instance by the Financial Regulator, of designing, monitoring and enforcing the Code.

The Financial Regulator's estimates of these costs are set out in its draft budget and for the reasons already cited it is not proposed to quantify these costs in this RIA.

At present the Financial Regulator is funded by levies raised on the financial services industry and by subvention from the Central Bank and Financial Services Authority of Ireland (CBFSAI), (roughly 50% from each).

Levies raised on financial institutions represent part of the costs structures of those firms and will therefore be likely to be reflected in the prices of financial products and services. Ultimately, therefore, the consumer of financial products and services pays the part of the direct costs met through levies.

To the extent that the Financial Regulator is part funded by subventions received from the CBFSAI, those sums are not available for the calculation of the CBFSAI's annual profits, which in turn dictates the level of funds transferred annually by the CBFSAI to the Exchequer. At the hypothetical level the Exchequer must either replace these funds from another source or moderate spending. Ultimately, therefore, the taxpayer/citizen bears the cost of the part of the Financial Regulator's direct costs met through CBFSAI subvention.

6.2.2 Compliance Costs to Industry

These are the costs to regulated firms of performing activities required by the Code. These costs have been borne in full by intermediaries for some time and will now also apply in full to all other regulated firms including banks and insurance companies.

The Financial Regulator believes that there is a significant overlap between the obligations proposed under the Code and the standards that responsible firms would adopt, for reasons of risk control, internal governance and reputation management, if there were no statutory Code.

We set out below a consideration of the cost implications for firms under each of the chapter headings used in CP10.

Chapter 1 General Principles	The Financial Regulator considers that these General Principles reflect best practice for the retail financial services industry. As discussed in more detail in the accompanying public response document we have taken cognisance of submissions made and therefore in a number of respects the final wording of the General Principles may be refined. We consider that these General Principles do not, of themselves, attract additional net costs to firms over and above the costs that would be incurred by responsible firms absent a Code.

Chapter 2 Common Rules for all regulated entities	**1. Access**

Chapter 2 Common Rules for all regulated entities

1. Access

The Financial Regulator's rules in relation to access reflect the reality that full participation in modern society cannot be achieved without fair and reasonable access to financial services.

To the extent that the rules on access may impose additional net costs upon firms these costs are considered to be outweighed by this public policy imperative.

2. Clients Best Advantage;

3. Information to be provided to Customers; and

4. Preservation of Customer's Rights

The Financial Regulator is satisfied that the standards imposed under these sections are appropriate and necessary, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

5. Knowing the Customer

The Financial Regulator believes that the know your customer requirements are a necessary corollary of the requirement to act in the best interests of clients and of the requirement to ensure that products and services are suitable for the customer.

The public response document makes it clear that these requirements can be at the level appropriate to and proportionate to the product or service to be provided.

By adopting this approach the Financial Regulator believes that this provision is appropriate and does not of itself impose additional net costs on firms.

6. Suitability

This provision represents a significant initiative, one that requires regulated firms to behave in a manner that many firms might not if there were no regulation. The rule effectively means that the principle of *caveat emptor* cannot be the central tenet of the approach of regulated firms to their relationship with the consumers of the products and services they provide.

The rule is a tangible expression of the principle that all firms must, within the context of their authorisation, act in the best interests of their clients.

In the discussions and correspondence between the Financial Regulator and industry representative bodies prior to the completion of this RIA this provision was cited as one that would impose very high costs upon regulated firms.

Those costs, which were defined in terms of information technology costs, staff training costs and additional administrative costs were estimated to amount to tens of millions of Euro per annum. The difficulties that measuring these costs presents have already been referred to in this RIA, nevertheless, without prejudice to the estimates offered, the Financial Regulator accepts that, in the context of the Code, the suitability provision represents a significant cost to the industry.

The Financial Regulator believes that the suitability requirement is an appropriate initiative, and one that reflects its statutory remit to promote the best interests of users of financial services in a way that is consistent with:

(a) the orderly and proper functioning of financial markets; and

(b) the orderly and prudent supervision of providers of those services.

The balancing benefits to the industry and the consumer of a suitability rule are even more difficult to quantify than the potential costs to the industry. The benefits would, however, also seem to be of significant magnitude in terms of countering the risks of mis-selling and engendering confidence in the financial services industry – which is a benefit to both the industry and the consumer.

In considering the merits of this suitability provision, the Financial Regulator believes that it is appropriate to refer to our High Level Goal 1[11], which is "Helping consumers to make informed choices through education and codes of practice in a fair financial services market". We believe that the suitability requirement gives expression to the policy stance inherent in that High Level Goal.

It is our view that while the suitability requirement will impose costs on industry, the objectives of the provision are valid and the costs are not disproportionate relative to the benefits.

7. Unsolicited Contact (Coldcalling)

The industry's broad comments on the provisions dealing with unsolicited contact are dealt with in public response document. On the specific issue of costs the industry has not commented on the significance of this rule. The rule is unlikely to give rise to direct costs nor to significant compliance costs. However the restrictions imposed on coldcalling may give rise to opportunity costs for firms that currently employ this marketing tool.

[11] Building a New Regulatory Structure. Strategic Plan 2004-06.

8. Disclosure Requirements

The Financial Regulator accepts that the disclosure requirements in general will impose costs on firms in terms of IT systems and staff training. We also accept that the disclosure of regulatory status in advertisements, particularly on radio, will cost firms money.

Balanced against this are the benefits to firms of being recognised as operating under a regulator, including enhanced consumer confidence. We also believe that the disclosure by firms of tied agency status is consistent with best practice.

While accepting that there are costs associated with this provision the Financial Regulator believes that it is worthwhile and appropriate measure.

9. Charges

The Financial Regulator accepts that this provision will give rise to once-off costs to firms arising from changes to IT systems and staff training. We believe that the ongoing costs are likely to be moderate.

The Financial Regulator considers that this rule is justified on the grounds that it will foster greater transparency and allow consumers to make more meaningful comparisons between products and services.

10. Charging/Pricing Errors, and

11. Terms and Conditions of Financial Products

The Financial Regulator is satisfied that the standards imposed under this section are appropriate and are those that would be observed by responsible firms were there no Code and that accordingly no additional net costs accrue.

12. Handling Complaints

The Financial Regulator's proposals in relation to complaints will be refined as set out in the public response document, however, perhaps particularly in relation to oral complaints, the provisions in the Code are likely to represent a standard higher that that which would be adopted if there were no Code.

It would seem fair to observe that complaints handling is an aspect of a firm's operations that responsible firms, for reasons of reputation management, would allocate resources to if there were no Code.

The Financial Regulator considers that the complaints rules are justified on the grounds that they will foster greater transparency and fairness for consumers.

13. Customer Records

The accompanying public response document provides some clarification in relation to concerns raised during the consultation process. The Financial Regulator considers that the final rules in relation to maintaining customer records are broadly consistent with best practice and that accordingly no significant cost accrues.

The provision to consumers of copies of their records is governed by the Data Protection Acts which allow that a charge be levied for this service.

14. Timely Execution/Allocation;

15. Fees Commissions and Other Rewards;

16. Conflicts of Interest; and

17. Chinese Walls

The Financial Regulator is satisfied that the standards imposed under these sections are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

18. Compliance with the Code

The Financial Regulator believes that this provision does not impose any costs on firms over and above the net costs of complying with the Code and best practice.

1. Statements;

2. Branch Restructuring/Withdrawal of Services; and

3. Changes in Interest Rates

The Financial Regulator is satisfied that the standards imposed under these sections are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

4. Accounts

The Financial Regulator is satisfied that in the main the standards imposed under this section are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

We recognise that the obligations imposed under Rules 6 and 7[12] are not currently observed by many banks and may result in a net increase in the cost of banks' books of deposit business. We believe however that these requirements are appropriate and are consistent with the General Principle requiring firms to act in the best interests of their customers

5. Deposit Agents

The Financial Regulator is satisfied that the standards imposed under this section are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

[12] Rule 6 requires that a credit institution must, at least once a year, advise existing deposit holding customers, of the different interest rates that are being applied to its deposit accounts, together with details of the rates applied to their savings account during the previous year. Rule 7 requires that where a customer has a variable rate savings account and the credit institution has reduced interest rates, the credit institution must contact the customer within a reasonable period of time to:
(a) advise the customer of the change in the interest rate,
(b) inform the customer about other savings accounts operated by the credit institution, offering to help the customer switch to one of these accounts, if the customer so requires,
(c) inform the customer that he/she can withdraw all the money in their account.

Chapter 4 Loans	**11. Unsolicited Credit Facilities** The Financial Regulator considers that opportunity costs represent the most significant element of the costs to industry of this provision. We are however satisfied that unsolicited credit is a contributing factor to over-indebtedness and that it is in the best interests of consumers to prohibit these practices. We believe that the public good aspect of this requirement is of sufficient merit to outweigh the potential costs to the industry. **2. Non-Mortgage Personal Lending;** **3. Mortgages;** **4. Mortgage Re-Financing/Equity Release; and** **5. Moneylending** The Financial Regulator is satisfied that the standards imposed under these sections are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.
Chapter 5 Insurance Products and Services	**1. Collateral Business;** **2. Quotations and Proposals; and** **3. Premium Rebates** The Financial Regulator is satisfied that the standards imposed under these sections are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue. **4. Renewal Notices** The Financial Regulator accepts that the requirement to ensure that customers receive renewal notices 15 or 20 business days (as appropriate) in advance of the policy renewal date is more onerous, and therefore more costly, than the standards currently considered to be best practice. We believe that most of these costs will relate to recalibrating IT systems when the Code is introduced and that the ongoing costs, if any, will be relatively modest. We believe that enabling customers to shop around more effectively is an appropriate objective for the Code and we believe that the benefits of this provision, in terms of fostering competition and assisting customers to obtain better value, outweigh the costs to the industry. The Financial Regulator considers that the disclosure requirements specified in relation to motor insurance renewal notices are appropriate and, apart from initial IT set-up costs, that the costs on an ongoing basis will be negligible.

5. Insurance Policies

The Financial Regulator is satisfied that the standards imposed under this section are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

6. Disclosure

In general the Financial Regulator is satisfied that the standards imposed under this section are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

We acknowledge that compliance with Rule 21[13] will attract additional net costs to firms, however we believe that this information will not be difficult to generate in a well-organised firm and accordingly that these cost will be modest.

7. Premium Handling; and

8. Tied Insurance Agents

The Financial Regulator is satisfied that the standards imposed under these sections are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

9. Life Assurance Policies

The Financial Regulator considers that the obligations imposed under this provision, relating to the explanations that must be given to customers are consistent with the obligation of insurers to act in the best interests of their customers.

We believe that the benefits of this provision, in terms of ensuring that customers fully understand the nature of the products they purchase, and are consequently less likely to be dissatisfied with those products, outweigh the costs to the industry.

10. Motor; and

11. Employers Liability

The Financial Regulator is satisfied that the standards imposed under these sections are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

12. Claims Processing

The public response document indicates that the Financial Regulator will consider this provision further in order to ensure a high level of customer protection without sacrificing the overall efficiency of the claims handling process.

[13] Rule 21 requires that an insurance intermediary must, on request, submit to the Financial Regulator, a schedule of specified commission income received.

Chapter 6 Investments

1. Rules1-8 inclusive

The Financial Regulator is satisfied that the standards imposed under this section are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue.

2. Cooling-Off Period

Cooling off periods do not currently apply to some investment products that will be covered by this provision. Because they represent an additional systems feature cooling-off periods will impose costs on firms. Some customers will cancel during the cooling-off period giving rise to a loss of business. The systems costs will however be largely of a one-off nature while the benefit of not creating dissatisfied customers must be set against the possible loss of business.

The Financial Regulator considers that this provision provides a strong and necessary protection to customers and that it is a proportionate measure.

3. Investment Risk

The various risk warnings required under this provision may go beyond what firms would do if there was no regulation. As these risk warnings will be incorporated into product promotional material the cost of carrying them is once-off in nature. The Financial Regulator considers that these warnings are appropriate and proportionate and that the benefits, in terms of creating more informed customers, outweigh the costs to firms.

4. Policy/Account Alteration by the Regulated Entity;

5. Contract Notes and Confirmation Notes;

6. Averaging of Prices;

7. Allocation of Transactions;

8. Discretionary Accounts;

9. Periodic Information; and

	10. Customer Borrowing; The Financial Regulator is satisfied that the standards imposed under these sections are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue. **11. Tracker Bonds** The public response document advises that Key Features document envisaged under CP10 will be retained, but that in the final Code discrepancies identified in the consultation process will be addressed. The Financial Regulator acknowledges that the requirement to devise and produce a Key Features document, broadly as envisaged by CP10, will impose costs on regulated firms however we believe that the benefits, in terms of greater transparency for customers, mean that this measure is appropriate and proportionate

Chapter 7 Advertising	**1. General Requirements** The Financial Regulator is satisfied that the standards imposed under this section are appropriate, and are those that would be observed by responsible firms were there no Code, and that accordingly no additional net costs accrue. **2. Lending** The public response document indicates that the final Code will take cognisance of the costs that some of the disclosure requirements envisaged by CP10 would have imposed and will also only require warning statements where the benefits of a particular product are featured in an advertisement. The Financial Regulator is satisfied that the standards imposed under this section are appropriate and proportionate and that the benefits , in terms of creating more informed customers, outweigh the costs to firms. **3. Investing** The public response document indicates that the Financial Regulator will consider again the level of information disclosure and warnings required for advertisements in some areas. Notwithstanding this the Financial Regulator is satisfied that the standards imposed under this section are appropriate and proportionate and that the benefits , in terms of creating more informed customers, outweigh the costs to firms.

6.2.3 Implementation timeframe

Industry representatives have impressed upon the Financial Regulator that the implementation timeframe for the Code will have a significant impact on the scale of the initial costs to firms. The Financial Regulator accepts the validity of the concerns expressed by the industry and will, without prejudice to the best interests of consumers, schedule the commencement of the Code provisions in a way that is cognisant of these concerns.

6.2.4 Costs to Consumers

Though one of the principle objectives of the Code is to increase the overall welfare of consumers of financial services the Code does impose some costs on consumers. The costs incurred by the Financial Regulator that are funded by the industry, and the incremental costs to regulated firms of compliance with the Code, represent part of the costs structures of those firms and will therefore be likely to be reflected in the prices of financial products and services. Ultimately the consumer will pay these costs.

Similarly, that part of the costs of the Financial Regulator met by the Central Bank will result in a reduced contribution by the Central Bank to the Exchequer and as such is a cost that will be borne by all citizens.
Other costs to consumers include:

- the possibility that a Code will deter potential market participants from entering the market and/or cause current participants to leave the market, with follow-on consequences for the level of competition in the market; and
- the possibility that the Code will engender product harmonization across product providers, leading to a reduction in choice.

6.3 Benefits

When coming to consider the benefits of a consumer protection code, it can be more difficult to quantify these than some of the costs, principally perhaps because costs relate to inputs, which by their nature lend themselves more easily to quantification, while benefits relate to outcomes. Nevertheless, we can approach the issue of benefits in a structured way. Perhaps the best way of doing so is to look separately at the benefits to consumers and the benefits to regulated firms.

6.3.1 Benefits to consumers

In looking at the benefits to consumers, it is important to apply the same principle as was applied to the measurement of indirect costs, that is that the effect to be measured, if possible, is the incremental benefit to consumers of having a Code over and above the benefits that consumers would enjoy absent a Code. Some of the benefits to consumers of a consumer protection code are:

1. by addressing information asymmetries, regulation assists in ensuring that consumers get the precise financial products and services that they want;

2. by raising levels of consumer confidence in financial products and financial service providers the Code can help to ensure that consumers enter the market and get the products that meet need, whether this relates to simple bank accounts in the case of the unbanked, or pensions for employees, or protection products. A greater proportion of successful outcomes from the consumers' perspective will further promote consumer confidence, promoting a virtuous circle;

3. by requiring financial firms to know their clients and to take care that only suitable products are sold to them the risks of mis-selling within the financial services industry should be reduced; and

4. the Code aims to create a level playing field between market participants. This and the enhanced transparency provisions contained in the Code should empower consumers to shop around and promote competition between firms. Greater competition should deliver better services and better value to consumers.

While some of the costs associated with the implementation of the Code may, on the face of it, seem significant they must be placed alongside the value of the potential benefits of regulation. For example, the cost to consumers of mis-selling scandals in the UK relating to:

1. endowments,
2. personal pensions,
3. free-standing additional voluntary contribution pension schemes (FSAVCs),
4. spilt capital investment trusts, and
5. structured capital at risk products (SCARPs)/'precipice bonds'.

is estimated in terms of billions of pounds Sterling.

6.3.2 Benefits to Regulated Firms

Regulated financial firms benefit from operating in a regulated environment, and specifically where conduct of business is regulated, in a number of ways:

1. All forms of regulation, including conduct of business regulation, tend to foster market stability, which is a benefit to all firms insofar as it facilitates long-term planning and the efficient allocation of investment capital over time;

2. The Code, together with the Financial Regulator's prudential supervision, and consumer information and education functions, constitutes a modern regulatory framework, recognised internationally as such. The regulatory standards that operate in Ireland serve to enhance the perception of Irish firms abroad when operating in foreign markets;

3. In the absence of a Code, poor service levels and/or poor outcomes for consumers on the part of some firms may lead to damage to the reputation of the whole sector and to the level of business done by that sector. Responsible firms therefore benefit from operating in an environment where conduct of business rules establish minimum standards for all firms;

4. Similarly, responsible firms that already operate to standards approximate to those set out in the Code incur costs that less responsible firms avoid. The imposition of a statutory Code helps to minimize this unfair competitive advantage;

5. Related to the effect described at 2 above is the fact that regulation, and perhaps particularly consumer protection regulation, tends to enhance consumer confidence in the firms within the regulated industry and their products. To the extent that regulation addresses information asymmetries it should lead to an increased number of transactions; and

6. The existence of a Code, promulgated by a statutory regulator, and accepted as valid by industry, lessens the need for regulated firms to invest in determining appropriate standards of conduct at the level of the individual firm. A Code is therefore an important tool for the management of operational risk within regulated firms.

7 IMPACT ON SMALL FIRMS

The purpose of this section is to consider if, when in operation, the provisions of the Code would be unfair to smaller firms, or would disadvantage smaller firms in any other way. The section will seek to consider if there are complexities within the Code that might be prohibitive to smaller firms. Finally, the Section also considers a number of relevant points made by trade bodies representing smaller firms.

It should be noted that in financial services, as in most other industries, scale may confer competitive advantages and disadvantages, and it is neither the purpose of the Code nor the intention of the Financial Regulator to negate the effects on competition of scale.

Notwithstanding the fact that on the one hand a small number of intermediaries are substantial corporations, while on the other hand a small number of product providers are relatively small firms, it nevertheless remains generally true to say that smaller firms are more likely to be intermediaries and larger firms are more likely to be product producers.

Impact on competition between small and large firms

- The single issue within the proposals that attracted the greatest level of comment from bodies representing small firms is the Financial Regulator's approach to the issue of unsolicited contacts. In general there was a view that the proposed rules could favour larger firms. However, even within the group of bodies representing smaller firms there were a number of distinct viewpoints expressed. The Financial Regulator's rational for the rules relating to unsolicited contact is set out in the public response document. The Financial Regulator has noted in particular the concern expressed that the phrase "similar to the proposed purpose of the coldcall" is open to interpretation. While we stress that firms will have to use their own judgement in this regard we will also monitor compliance via our monitoring processes.

- The Professional Insurance Brokers Association (PIBA) cited Rules 73 and 74 of Chapter 2 of the proposed Code as having been drafted with only large firms in mind. These sections, which dealt with the responsibilities of the compliance function within regulated firms, will be redrafted to take account of the fact that small firms will not have a dedicated compliance function.

Complexity

The Financial Regulator recognises that small firms, unlike many larger firms, will be unlikely to have available to them the advice of a dedicated/expert compliance officer or compliance team. Indeed, many small firms are one or two person operations. In order to ensure that the provisions of the final Code are as accessible as possible the Financial Regulator sought and received advice on the best way to express the principles, and will draft the detailed rules in a way that balances the desire to use plain English with the need to ensure that the rules have a precise legal meaning.

The Irish Brokers Association suggested that the Financial Regulator should establish "a support mechanism whereby general or specific queries can be referred on a formal or informal basis for clarification, guidance or ruling". The Financial Regulator considers that formal guidance or rulings would have a status similar to detailed rules, and given the preference of most stakeholders for a principles-based regulatory framework we are not therefore favourably disposed towards providing formal guidance or rulings. Responsibility for compliance with the spirit and, where relevant, the letter of the Code rests with each firm, however the Financial Regulator is always available to discuss regulatory issues with individual firms. In addition, when the final Code is published the Financial Regulator will invest resources in meeting with, and dealing with queries from, as great a number of regulated firms as possible. This may perhaps be achieved by a series of seminars around the country.

Conclusion

The Financial Regulator considers that the Code treats all firms equitably, regardless of size. We will however continue to keep this issue under review during the implementation phase of the Code.

8 COMPETITION ASSESSMENT

The Financial Regulator's Strategic Plan 2004-2006 commits the Financial Regulator to fostering an internationally competitive and successful financial services industry. We hold that consumers benefit from a competitive market through increased choice and lower prices. In framing the Code we have endeavored to ensure that the Code fosters competition by creating a level playing field, and does not discourage new players from entering the various market segments.

The Code itself, in common with all other regulatory provisions, could constitute a barrier to entry to Irish retail financial markets, and indeed to the extent that the Code, together with other related consumer protection measures, is designed to exclude unscrupulous firms it is in fact intended to act as a barrier to entry. The Financial Regulator believes however that the Code constitutes an appropriate balance between the freedom of firms to enter and exit the market, on the one hand, and the need to protect consumers on the other. The Financial Regulator has, in arriving at this view, had particular regard to the comments offered by third parties on the impact of the Code on competition.

8.1 The Competition Authority

The Central Bank and Financial Services Authority of Ireland Act, 2003 requires the Financial Regulator and the Competition Authority to consult with one another for the purpose of ensuring the establishment and pursuit of consistent policies regarding the regulation of financial services in the State.

The Financial Regulator and the Competition Authority have established a meaningful and ongoing dialogue concerning competition issues in the financial services industry, and the Financial Regulator attaches particular significance to the submission of the Competition Authority in relation to Consultation Paper CP10, especially where concerns about competition issues are expressed.

The Financial Regulator has also welcomed the Competition Authority's recently published reports on competition in the (non-investment) banking sector and in the non-life insurance market. These reports identified significant weaknesses in which competition operates in the relevant markets, and both reports make recommendations, some of which are addressed to the Financial Regulator.

Both of the Competition Authority's reports were published after the Financial Regulator had issued consultation paper CP10[14]. We will implement in the final Code any recommendation that can be taken on board relatively easily. However, we have given a commitment to the industry that we would not incorporate any new provisions into the Code unless we have consulted fully on them. For that reason we will discuss the recommendations in greater detail during the next phase of the Code project, with a view to seeking agreement with the industry on the types of provisions which can be included now and those which will await a further consultation.

[14] CP10 was published in February 2005. The Competition Authority's reports on competition in the non-life insurance market, and in the (non-investment) banking sector, were published in March 2005 and September 2005 respectively.

8.2 Effect of The Code On Competition Between Firms, Sectors And Internationally.

One of the central objectives of the Code is to create a level playing field between financial firms. This is not the same as putting all firms on an equal competitive footing. Factors such as scale, technology, innovation, geography and human capital, to name but a few, will in a competitive market, inevitably confer competitive advantage upon some firms. The Financial Regulator's objective is to ensure that all authorised firms, and all firms entitled to participate in Irish financial markets pursuant to EU passporting provisions, are afforded access to markets on an equal footing. The Financial Regulator is also concerned to ensure that the proposed Code does not, either by act or omission, impact negatively on the operation of competition in relevant financial markets.

As regards competition between firms within the same sector the Financial Regulator is satisfied that as the Code will apply to all such firms in the same way, and at the same time, that the effect of the Code on competition will be neutral. We note that the Conduct of Business rules introduced for retail intermediaries (multi-agency intermediaries and authorised advisors) in late 2001 did not seem to have impacted on the number of firms in the market (see Table 1 below). Many of the principles and detailed rules in that code are reflected in the current Code.

Table 1	**2002**	**2003**	**2004**
Multi Agency Intermediaries	1811	1889	1938
Authorised Advisors	603	525	477
TOTAL	**2414**	**2414**	**2415**

The Financial Regulator's approach in the Code, of structuring the Code under various product types rather than by regulated entity type, is a conscious effort to ensure that firms from different sectors operate under the same terms.

The Code will constitute part of the so-called "common good" apparatus applicable to all financial firms offering relevant financial services in the State, regardless of the domicile of the financial services provider. Accordingly, because the Code will apply to non-Irish firms which are subject to Financial Regulator supervision as well as to Irish firms, the Financial Regulator considers that the effect of the Code on competition between Irish firms and non-Irish firms is neutral.

Although the Financial Regulator is not charged with having regard to competition outside the State it is perhaps worth noting that the Code will not apply to interactions between Irish financial institutions and consumers where that interaction takes place in another jurisdiction. The "common good" apparatus applicable in that jurisdiction will apply. The Code will therefore have a neutral effect on the ability of Irish firms to compete in other jurisdictions.

9 SUMMARY AND CONCLUSIONS

The Financial Regulator's believes that the Code represents a significant step towards:

- improving the welfare of consumers of financial services;
- fostering confidence in financial services firms and the products and services they provide; and
- creating a level playing field for financial firms.

We acknowledge that compliance with the Code will impose costs on firms however we believe that the measures contained in the Code are appropriate, necessary and proportionate and for the most part do not exceed standards that would be widely accepted as best practice. Where measures do go beyond best practice we believe that they will deliver desirable and appropriate benefits to consumers of financial services.

We believe that the Code will be neutral in its effect on competition between firms and on national competitiveness, and that an appropriate balance has been struck between the desirability of creating a level playing field, on the one hand, and concerns about the regulatory burden on smaller firms, on the other.

Select Bibliography

The main purpose of this select bibliography is to lead the reader to further information on significant subjects. The bibliography is not a complete record of the written sources consulted during the preparation of this RIA.

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FINANCIAL REGULATOR
Rialtóir Airgeadais

Consumer Protection Code

REGULATORY IMPACT ANALYSIS

December 2005

This document does not form part, or provide an interpretation, of the Consumer Protection Code or any other code, requirement or provision of law or regulatory practice the subject of the exercise by the Financial Regulator of its functions.