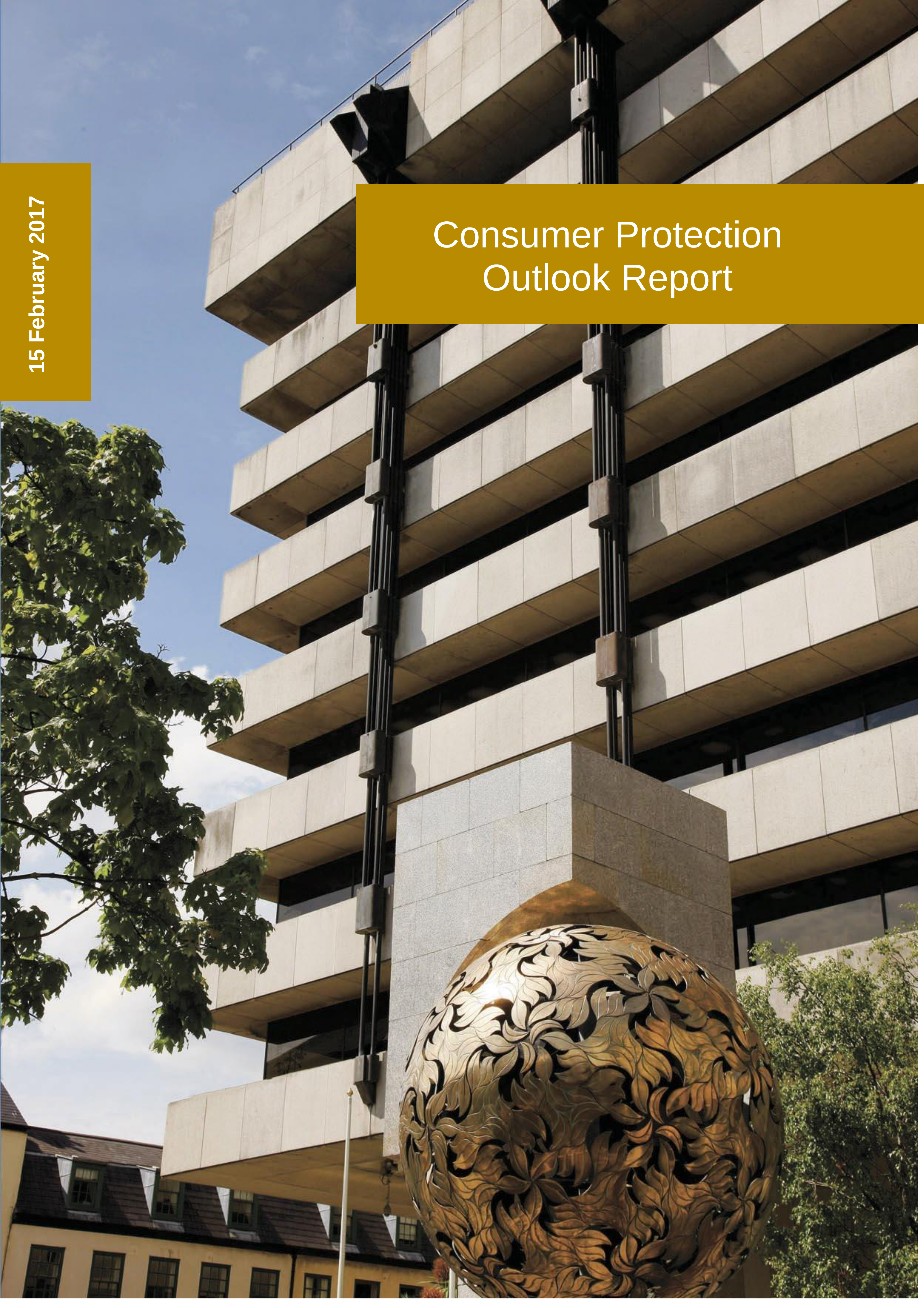

15 February 2017

Consumer Protection Outlook Report

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Foreword

Ensuring that the interests of consumers of financial services are protected continues to be a key priority for the Central Bank as reflected in our mission statement of "Safeguarding Stability – Protecting Consumers" and in the objectives of our Strategic Plan, 2016 – 2018. We aim to deliver on this not only through our consumer protection mandate but also by working to ensure that the financial system is stable and the firms that operate within it, and which are authorised by the Central Bank, are financially sound and safe.

In order to consistently deliver the right outcomes for their customers, firms must put consumers' interests at the centre of everything they do. This starts with firms understanding the risks faced by their consumers, not only from the products and services they buy, but also from the behaviour of the firms themselves and the wider market and environment.

This Consumer Protection Outlook Report (CPOR) aims to highlight a number of those consumer risks which the boards and senior management of all regulated firms need to consider. The CPOR also outlines those priority areas that the Consumer Protection Directorate within the Central Bank will be focussing on over the next couple of years in the context of our consumer protection mandate.

All firms have a responsibility to help their customers make the right decisions. This responsibility arises not only when selling new products and services but throughout the whole relationship with the customer. This means looking at the relationship through the lens of the customer and not purely from the firms' perspective. We continue to see the problems that arise for consumers when this does not happen. For example, as part of the Tracker Mortgage Examination, the Central Bank has identified issues in relation to the provision of clear and comprehensive information by lenders to borrowers, which may have had an impact on the ultimate decision by the borrower on the interest rate that they chose on their mortgage. This can have serious implications for consumers as well as for the firms. This risk is compounded where firms have a range of products on offer, as it can be very difficult for consumers to figure out what is best for them. One example of this is where we have worked to ensure that health insurance providers are doing more to help their customers decide on the most suitable product when renewing their cover.

The Central Bank, as part of its consumer protection mandate, will continue to challenge firms to demonstrate how they are delivering for their customers. We will also continue, where necessary, to take the appropriate supervisory and enforcement actions to ensure that consumers are being protected.

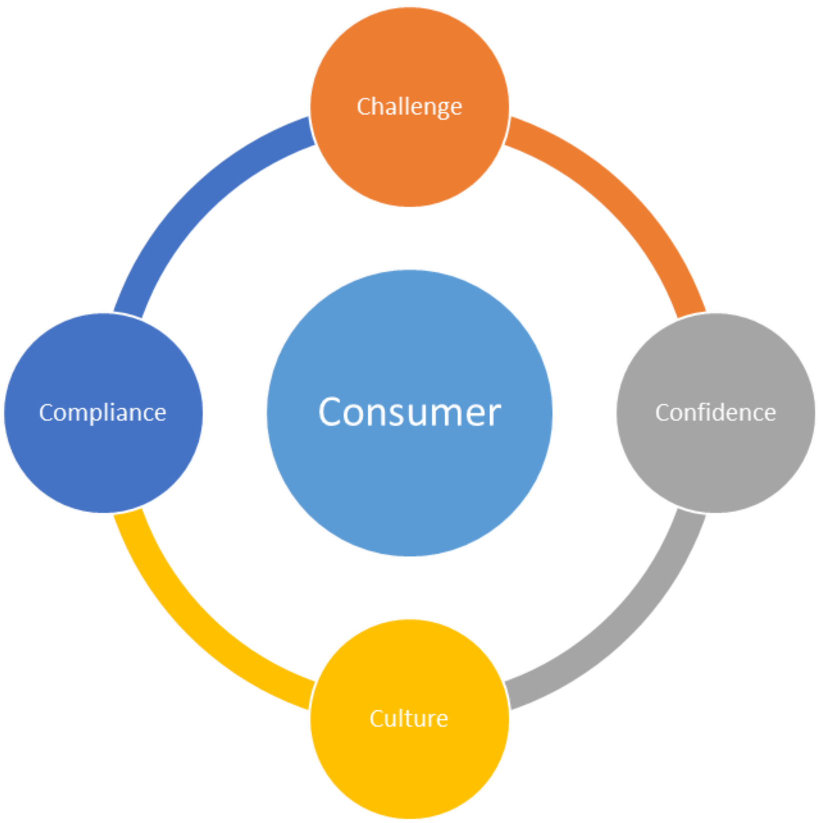
Bernard Sheridan
Director of Consumer Protection
Central Bank of Ireland

Delivering on Our Consumer Protection Objectives

We aim to deliver on our consumer protection mandate in the context of three important desired consumer protection outcomes:

- a positive consumer-focussed culture that is embedded and demonstrated within all firms;
- a consumer protection framework that is fit for purpose and ensures that consumers' best interests are protected; and
- regulated firms that are fully compliant with their obligations and are treating their customers, existing and new, in a fair and transparent way.

We use the 5Cs framework to provide a sound basis for our risk-based approach to deliver on our consumer protection objectives and the outcomes we strive to achieve.



This framework puts the **Consumer** at its centre, where the focus of firms must be on delivering positive consumer outcomes within a regulatory framework that is fit for purpose. This can only be achieved where firms have a consumer-focussed **Culture** which enables consumers to have **Confidence** in both the financial decisions they are making and the firms they are dealing with. The Central Bank will continue to **Challenge** firms, where their focus is not on those consumer outcomes. There is a need and appetite for appropriate regulatory action where **Compliance** standards are not being met.

This framework also comprises our gatekeeper role, where applicant firms can expect us to be rigorous and challenging in our application of the published requirements and standards (including those derived from EU law). Here, we are guided by our mandate to ensure that the best interests of consumers are protected and by our role as a national competent authority within a wider EU framework of regulation.

We adopt a risk and evidence-based approach in prioritising our work, which ensures that we are focussing our resources on those areas where we consider there to be a significant threat to our consumer protection objectives. This includes carrying out a comprehensive annual consumer risk assessment, whereby we examine each of the retail sectors regulated by the Central Bank to identify current and emerging risks. This assessment is informed by intelligence from a number of sources, including:

- our supervisory work and experience, including analysis of consumer data submitted by firms;
- external and internal market research and analysis;
- developments at a European and international level;
- advice from the Consumer Advisory Group[1]; and
- our engagement with stakeholders, including consumer groups and statutory consumer bodies.

[1] The Consumer Advisory Group was established under Central Bank Reform Act 2010 and advises the Central Bank on the performance of its functions and the exercise of its powers in relation to consumers of financial services.

Consumer Protection Risks

The 2016 CPOR highlighted a number of current and emerging consumer risks including culture, product oversight and governance, indebtedness and arrears, IT resilience and data security, the low interest rate environment and the changing nature of how financial products and services are being provided. Many of these risks clearly remain for 2017 with the ongoing uncertainty over the impact of BREXIT adding to the overall environmental risks for consumers.

1. Absence of a consumer-focussed culture

We continue to highlight that the absence of a consumer-focussed culture within firms presents a significant risk to consumers. A positive consumer-focussed culture manifests itself in many ways including how firms communicate with their customers, how they are helped to understand the financial decisions they are making and how firms incentivise their staff. It is important that firms are open to and facilitate feedback from their customers and are willing to learn from past mistakes. This can help firms identify emerging consumer risks as well as building a stronger relationship with their customers.

2. Indebtedness and Arrears

The number of borrowers in long-term mortgage arrears remains high. Also, while the overall level of household indebtedness is falling, many households remain highly indebted and potentially vulnerable to any external shocks including increases in interest rates. While the Central Bank has worked to ensure that there are important protections in place to help these borrowers, it is critically important that lenders continue to work proactively with those borrowers to help them resolve their arrears.

3. Growth in new lending

As the economy has started to recover, the level of new lending in all areas (mortgages, personal loans and credit cards) has started to increase. While this is a positive sign that the economy is improving, it also presents new risks for consumers which need to be managed by lenders to ensure that new debt is affordable and suitable for the borrower. The 2015 Central Bank Mortgage Regulations aim to increase the resilience of the banking and household sectors. However, it is important that industry learns the lessons from the recent past, and works to ensure that individual consumers do not suffer detriment as a result of over-borrowing. The introduction of the macro-prudential policy for residential mortgage lending does not obviate lenders' responsibilities under the existing financial services legislative framework, and in particular, from the obligation to assess affordability and to lend responsibly on a case-by-case basis under the Consumer Protection Code.

4. Risks created by the ongoing low interest rate environment

The continuing low interest rate environment has been of benefit to some consumers in terms of meeting debt repayments, but has also presented challenges for those consumers wishing to earn a return on savings or planning for retirement. This is magnified by the fact that consumers are living longer and so need to generate sufficient savings to sustain them through retirement. There is an increased risk for consumers that firms may sell higher risk products, with a potentially higher return, without ensuring that the increased risks are fully understood by the consumer. Firms need to be vigilant that their consumers are being sold products and services appropriate to their risk appetite.

5. Insurance and protection risks

Over recent years, many consumers have seen significant increases in the cost of insurance, particularly motor and health, which has impacted on household budgets. This may lead to consumers reducing the level of cover they have, resulting in the risk of the consumer not having the level of insurance cover appropriate to their needs.

Firms have a responsibility to act honestly, fairly and professionally in the best interests of their customers, bringing key information to the attention of the consumer in a manner that seeks to inform them. This includes making sure that any product offered by a firm is suitable for the consumer and that any product recommended is the most suitable product for the consumer. Firms need to be cognisant of these responsibilities where they have a range of similar products and the consumer is renewing the policy or considering making changes. In addition, firms need to ensure that the information they provide to consumers on the level of cover the policy provides is accurate, clear and easy to understand.

6. Risks from poor product design and marketing

Financial products and services can in themselves present risks to consumers. Most financial products can be complex and the terms and conditions can be difficult to fully understand. The matching of the needs of consumers to the most suitable product or service, which consumers understand, is critical for ensuring the right consumer outcomes but can also present significant consumer risks if not done properly. Firms need to be able to demonstrate that their product oversight and governance processes take into account consumers’ ability to understand what it is they are purchasing. Robust product testing and controls before launching new products and ensuring that they are only being sold to consumers for whom they are suitable can help firms mitigate many of the risks for consumers.

7. Fintech and Innovation

Many firms are innovating, through greater use of technology, in how they deliver products and services (Fintech) and this offers the potential for many consumer benefits. The Central Bank encourages innovation, where it is in the best interests of consumers. However, the need for focus on the consumer and delivering fair consumer outcomes through sound product oversight and governance arrangements, as new products and services are being developed and rolled out, is critical in order to prevent consumer detriment. Where firms are moving more to providing financial advice and recommendations through on-line channels they must ensure that the necessary protections are in place to deliver the right consumer outcomes.

As firms move away from traditional delivery models they must also ensure that the needs of existing customers, including those who may be more vulnerable, continue to be met and that particular cohorts of consumers are not financially excluded.

8. Cyber Risks, Data Protection and IT resilience

Firms are exposed to an increasing risk of system failures and cyber-attacks due to their unavoidable dependency on information technology. In addition, there are increased risks to consumers who expect that their financial services provider will continue to offer a reliable service and a safe and secure environment for their personal information. The Central Bank has separately highlighted cyber risk as one of the key threats to regulated firms and sectors.

9. Customer service

With increased pressure on all financial services firms to control costs, firms may be tempted to cut costs in areas such as customer service. Failure by firms to deliver a quality customer service undermines the customer relationship and can also lead to situations where errors and overcharging occur. We are aware that more firms are monitoring key metrics, including complaints and social media activity, to identify emerging issues. This is to be welcomed, but it is also important that boards and senior management focus on the outcomes being delivered for their customers.

Consumer: the consumer protection framework

A key element of our role is ensuring that the consumer protection regulatory framework is fit for purpose and working for consumers and this will continue to remain so. This is particularly important in the face of emerging trends and products, including in the context of the pace and scale of technological innovation in the delivery of products and services to consumers. This assessment of the framework is based on market intelligence; our own supervisory experience; consumer research; and insights into consumer behaviour. Our ongoing assessment of the consumer protection framework also takes account of feedback from a wide range of key stakeholders such as the Competition and Consumer Protection Commission and the Financial Services Ombudsman.

The framework is influenced by domestic issues, European initiatives as well as wider international developments. The influence of European legislation on the shaping of the regulatory framework continues, with the introduction of important European directives in Ireland including legislation relating to mortgage credit, payments, insurance distribution and investments. We continue to influence the development and implementation of this legislation to shape a strong consumer protection framework and to maintain many of the key protections already in place in Ireland. The introduction of European legislation also impacts on the existing domestic consumer protection codes, which must therefore be kept under review to ensure that they are consistent with the new European provisions.

In addition, the three European Supervisory Authorities (EBA[2], ESMA[3] and EIOPA[4]) (the 'ESAs'[5]) continue to play an important role in shaping the consumer protection framework across Europe. The Central Bank is actively participating in the work of the ESAs to influence and contribute to their agendas, particularly in those areas that align with our own priority areas. The Central Bank also continues to play an important role in the wider international development of consumer protection in financial services through

[2] European Banking Authority
[3] European Securities and Markets Authority
[4] European Insurance and Occupational Pensions Authority
[5] European Supervisory Authorities

membership and active participation in FinCoNet, the international organisation of financial consumer protection supervisory authorities.

Priority themes

- The Central Bank will continue to support the Department of Finance on its work to implement into Irish law key EU directives such as the Markets in Financial Instruments Directive II, the Insurance Distribution Directive and the Payment Services Directive 2, as well as working to review and update existing codes to reflect the changes arising from the new European legislation. We will continue to commit our resources to influencing and shaping the international and European agenda, including the work of the ESAs.
- On 21 November 2016, the Central Bank published a consultation paper on the review of the Minimum Competency Code which establishes minimum professional standards for staff dealing with consumers and is a key part of the framework. This review proposes a number of additional measures to raise standards as well as capturing changes required by European legislation and will be completed in 2017.
- Technology-driven innovation (Fintech) is having an impact on how products and services are being delivered to consumers in the digital age. In this context, it is important to consider how the current consumer protection framework addresses emerging risks from these innovations. In 2017, we plan to publish a Discussion Paper on this topic as it relates to our existing Codes.
- As part of our ongoing monitoring of existing Codes, we are planning to review the Consumer Protection Code for Licensed Moneylenders to determine if the existing protections need to be enhanced.
- We will continue our ongoing monitoring of market developments and will conduct consumer research to inform our work, including publishing this research and key trends we observe in the market, in order to inform the wider discussion of consumer protection issues.

Culture: developing a consumer focussed culture

We continue to highlight the importance that **culture** plays in driving the behaviour of firms and the individuals within them. The Central Bank's Strategic Plan 2016 – 2018 highlighted our continuing focus on challenging the industry to develop the right culture. While we are seeing progress being made by some firms, which is to be welcomed, there is clearly some way to go in making the sustainable shift that is needed if consumers are to have full confidence that firms are acting in their best interests.

In order to achieve this sustainable shift, the role of the boards and senior management cannot be overstated. We can see from our own interactions with firms that where the right direction is being given from the top, the firm delivers better consumer outcomes. Firms also need to put in place internal consumer risk frameworks to help support the delivery of their strategies. Recognising the fundamental importance of risk management in achieving the shift in culture mentioned above, the Central Bank has enhanced its Consumer Protection Risk Assessment (CPRA) Model, which provides a strong framework to assist supervisors in carrying out assessments of how consumer protection risk is being identified and managed within firms. This CPRA Model equips us to assess how the firms' consumer risk frameworks are designed and also how effective they are in practice in delivering fair consumer outcomes.

Priority themes

- We will publish details of our CPRA Model by end-March 2017, which will help inform firms in developing or enhancing their own consumer risk frameworks.
- Following the successful pilot testing of the CPRA Model in a number of firms in 2016, we will conduct a series of targeted CPRAs in a range of firms across the different industry sectors throughout 2017, with a particular focus on culture, performance management, sales incentives and product oversight and governance.
- We will continue with our engagement with firms' boards and senior management to ensure that there is a clear focus from the top on embedding and measuring firms' own cultural change programmes.

Confidence: consumer confidence in the firms they deal with

Consumers' **confidence** is directly impacted by the experience they have in their dealings with firms and their staff. Consumers expect firms to act in their best interests and that they will deal with them in an open and fair way. They expect firms to understand their needs and what is important to them. This is relevant not only when a product is being sold but also throughout the ongoing customer relationship. This includes, but is not limited to, when a firm engages with a consumer who has a query or complaint (as shown by our research[6] in this field), where there is a change in the consumer's circumstances or where the firm has made an error or mistake.

We continue to highlight how the right incentives for staff dealing with consumers can help support the relationship, build trust and confidence and avoid conflicts of interest. When consumers are buying products, firms need to ensure that their own interests are aligned with the best interests of the consumer.

Consumers' confidence in firms can also be impacted when they feel they are not being offered the best product from that firm, particularly at renewal time, or if they are not informed that they could make savings by switching products within the range offered by the firm. The Central Bank has focused on this issue over the last year specifically in relation to health insurance and standard variable rate mortgages, to ensure that firms are helping existing customers to understand their options and/or switch to a better product.

Financial products and services can be very complex and firms have an obligation to help consumers fully understand the associated risks and benefits before they make their decisions.

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[6] http://www.centralbank.ie/press-area/press-releases/Pages/CentralBankpublishesresearchonconsumerperceptionsofcomplaintshandlinginregulatedfirms.aspx

Priority themes

- The ongoing Tracker Mortgage Examination continues to be a key priority for the Central Bank to ensure the fair treatment of tracker mortgage borrowers and is the most significant supervisory review that the Central Bank has undertaken in the context of our consumer protection mandate. We have published regular updates on progress during 2016 and we expect all relevant lenders to have identified and commenced engagement with most impacted customers by mid-2017, with the payment of redress and compensation extending beyond this point for some lenders.
- In July 2016, we published a discussion paper on the risks and benefits of the practice of product producers paying commission to intermediaries for selling their products. This work will be progressed in 2017 to determine what measures, if any, need to be put in place to strengthen the protections for consumers.
- Systems failures and errors will continue to be monitored to ensure that firms are delivering on their obligations to ensure that consumers are kept fully informed of any issues and that the impact on the consumer is dealt with in a timely and appropriate manner.
- In 2016, we launched research into mortgage switching to see if there are further measures we could introduce to facilitate consumers who wish to switch their mortgages. We will conclude this research shortly and bring forward any proposals for consultation based on these findings in 2017.

Challenge: of firms and ourselves

One of the key functions we have is to act as gatekeeper in terms of whether applications from firms and individuals seeking authorisation to provide services are approved or not. It is important that the requirements in place help to ensure that only those who meet the minimum standards are approved and also that we are prepared to challenge applicants during the process to demonstrate how they meet those standards.

We will continue to challenge firms at board and senior management level on their culture and practices where we believe there is or may be a threat to our consumer protection objectives, both at authorisation stage and through the ongoing supervision process. We have demonstrated that we are prepared to challenge firms when we see potential consumer detriment by taking supervisory and enforcement actions where necessary.

Priority themes

- The Central Bank is currently reviewing applications from Credit Servicing Firms, i.e. firms which service loans sold by regulated lenders to third parties, under legislation giving the Central Bank responsibility for their regulation. This has included the assessment of those firms against the detailed Authorisation Requirements and Standards introduced by the Central Bank on foot of that legislation. During 2017 these applications will be progressed to decision stage i.e. either authorisation or refusal.
- Applications for authorisation from other retail sectors including payment institutions, electronic money institutions, bureaux de change, retail intermediaries, debt management firms, retail credit firms and moneylenders will continue to be assessed in line with the relevant authorisation requirements and standards. This includes applying the timeframes of our new authorisation models introduced in 2016, against which we have commenced reporting publicly in 2017, and refusing to authorise firms that do not meet our standards.

Compliance: how firms are meeting and demonstrating compliance

Consumers can only really benefit from having a strong consumer protection framework in place if firms are meeting their obligations and complying with the standards prescribed by that framework. Responsibility for compliance is clearly for the boards and senior management of regulated firms, while the Central Bank is responsible for monitoring and enforcing compliance using the various powers and tools available to it. As set out above, we adopt a risk and evidence-based approach in prioritising our work, which is informed by a range of factors. This ensures that we are focussing our resources on those areas where we consider there to be a significant threat to our consumer protection objectives.

A key part of how we monitor compliance is by undertaking thematic reviews, which enables us to examine specific risks across a number of firms in a sector or across sectors. The results of these reviews are published and the findings inform any supervisory or enforcement action that we may take against non-compliant firms. This work will continue in 2017 across the different sectors including examining product/service-specific risks and is in addition to the firm-specific CPRAs referred to above.

One area of focus of our thematic reviews over the last couple of years has been in respect of retail intermediaries, where a significant number of firms were not engaging appropriately with us, including firms which were failing to submit the basic information necessary for us to be able to effectively supervise them. We have made significant progress in dealing with non-compliance and this will continue to be a focus of our ongoing supervision of this sector.

Priority themes

- In addition to the CPRAs which will be undertaken, and the continuing Tracker Mortgage Examination, we plan to conduct or commence a range of themed reviews and inspections, including:

    - Insurance companies selling niche/add-on insurance;
    - Payment institutions' safekeeping of client funds;
    - Retail intermediaries’ compliance with minimum standards; and
    - Retail intermediaries which are acting as managing general agents on behalf of insurance companies.

- We will also continue with our initiatives to facilitate smaller firms in understanding their responsibilities better, including hosting roadshows around the country and the publication of newsletters for a number of industry sectors.