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The OFT's new approach to consumer codes of practice **Comments by Mark Boleat, Boleat Consulting**

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Introduction

On 27 February 2001 the Office of Fair Trading published *The OFT's new approach to consumer codes of practice*. The paper explains the existing policy in relation to codes of practice and the reasons for change, sets out a new approach and seeks views on the criteria to be used and a preliminary list of priority sectors for the new approval regime. Comments on the consultation paper are sought by 31 May 2001.

This paper is a personal response by Mark Boleat, who runs the consulting business Boleat Consulting. The author is qualified to comment on this issue as the former Director General of the Association of British Insurers, which managed a number of codes of practice, as a member of the National Consumer Council and the DTI Task Force on Car Servicing and Repairs, and as the author of a number of publications on consumer policy including one specifically on codes of practice.

Summary of key points

- The general approach in the consultation paper is right and is a welcome move away from the unsuccessful policy of the past.
- The two-stage approach is necessary from the OFT's point of view, but associations should handle the issue as a single stage exercise. It is not altogether clear why some matters have to wait for stage two. The OFT resource problem can be addressed partially by charging associations for the work involved in recognising their codes.
- There has been little evidence of joined-up government over the last few years in respect of "soft law". All government departments should embrace the new approach, and the initiative needs to be tied in with other initiatives such as those on car servicing and repairs, the banking code of practice and the Quality Mark in the building industry.

- Associations will need more guidance that the OFT appears willing to give, otherwise there is the danger that work could be done in developing new codes which will then prove unacceptable.
- The major problem areas for associations are consultation with consumers, performance indicators, disciplinary arrangements, persuading members to sign up to much more stringent codes and the cost of putting into place and maintaining such codes.
- There may be a need for special arrangements for codes in sectors where transactions are of a low value.
- The priority sectors are broadly right except that building work must be included.
- The proposed criteria are broadly correct.

General approach

The general approach in the consultation paper is strongly supported. It addresses major problems that have been inherent in consumer codes of practice for many years. Currently, there are hundreds of codes of practice. They vary massive in their impact. Some are probably more effective than formal regulation and have significantly changed the behaviour of companies to the benefit of consumers. Built within such schemes are extensive compliance and redress arrangements. The banking code of practice, the code of practice for the selling of general insurance and the advertising code of practice are good examples.

At the other extreme there are codes of practice which require companies to do no more than observe the law, behave with the utmost integrity and generally “be good chaps”. Such codes invariably have no monitoring or compliance arrangements and are mainly used as a means of an association attracting more members or of its members seeking to attract more business. Between these two extremes are the majority of codes which are of varying usefulness to consumers in respect of their content and, more importantly, compliance arrangements. A code which seems to offer all sorts of protections to consumers is no use if there are no compliance arrangements, and conversely strict compliance arrangements are of no use if it is impossible for a company to act in breach of the code.

The result of the present situation is that the consumer cannot rely on something called a code of practice. Indeed, there can be a perverse situation when the biggest crooks are the quickest to pronounce that they comply with any number of codes of practice and are members of a number of trade associations, the local chamber of commerce and various guilds.

The OFT currently recognises over 20 codes owned by 40 trade associations. One would be entitled to think that these codes are somewhat better than the average. They are not. They are a ragbag of codes for an arbitrary collection of industries and are no better or worse than codes generally. The OFT does not have the resources to ensure that the codes are meaningful or that they are properly enforced.

The proposals in the consultation paper properly address these problems. They constitute a logical regime which, if effectively introduced, will mean that a code with formal OFT approval will be meaningful to consumers. Equally, there should be a

presumption that codes without OFT approval should be regarded as no more than advertising devices.

The OFT, wisely, is not seeking to be too prescriptive about the content of codes or about compliance arrangements. What is appropriate in some sectors where, for example, large sums of money are at stake is very different from what is appropriate in sectors where only small amounts of money are involved. For example, an ombudsman scheme is perfectly proper in the case of mortgages but would be over the top in the case of shoe repairs.

The main difficulty with the proposals is that they are seeking to move codes of practice a long way from the current position. Other than in the regulated sectors most sponsors of existing codes will have to make major enhancements. This is desirable but it may well be the case that the move can be achieved only if there is pressure on companies in problem areas to adopt codes of practice that meet the OFT guidelines. If there is no such pressure then there is a danger that there will be a wonderful regime for codes of practice but the only codes which will meet the OFT requirements will be those that exist in the heavily regulated sectors, developed under pressure from the regulators, for example in financial services and the utilities.

The two stage approach

The consultation paper envisages a two stage approach. In the first stage the OFT will confirm to the sponsors of codes that meet the OFT criteria that those codes are likely to be of practical benefit to consumers and good traders. However, there would be no OFT logo or mark because there would be no independent checking of how the codes actually worked. The OFT has made it clear that it will not get greatly involved in assisting trade associations and other sponsors in drafting the detail of codes.

At the second stage the OFT will endorse publicly, including with a well-marketed logo, those codes for which there is evidence of practical success. For stage two, trade associations will therefore have to demonstrate that in practice a code is effective. This must embrace audit arrangements, mystery shopping and customer satisfaction surveys.

The two-stage approach is sensible and is fully supported. However, there is a danger. Trade associations should regard this as a single exercise not a two-stage approach. They will need to build into the arrangements for their codes the compliance and monitoring systems. They will not want the OFT to refuse support at stage two on the grounds that the compliance procedures themselves are inadequate to show that the code is being properly observed. It also needs to be remembered that initially monitoring of code compliance tends to show a fairly low level of compliance. This is true even in heavily regulated sectors such as financial services and the public sector, for example the recent National Consumer Council mystery shopping of local authority trading standards advice services. It is also true in respect of requirements imposed by law. The OFT will need to formulate some criteria so that associations will know what sort of evidence will be required to get stage two approval and what sort of systems they will need to put in place at the outset.

In practice, the OFT will find itself approached by trade associations wanting to discuss the content of and compliance arrangements for their codes so as to be certain that they will not be forced into having two goes at drafting a code.

Joined-up government

Joined-up government does not exist. This is not a particular criticism of the present government but rather has always been the case. This presents problems in respect of the OFT proposals.

In some sectors there is no specific regulator nor do government departments take a particular interest. This applies, for example, to most forms of retailing and also most forms of repairs. In these sectors the OFT is the one organisation which takes an interest at national level. Trading standards departments might also have an interest, certainly at local level and perhaps also at national level. In these sectors the sponsors of a code will merely have to satisfy the OFT.

In many other sectors there are specific regulators or departments which take a close interest in what is going on. In many such sectors there are already meaningful codes of practice, most of which meet the proposals in the consultation paper. Examples of such sectors are –

- The utilities, where the regulators have enforced codes of practice covering such matters as service calls, billing arrangements and disconnections.
- Financial services, where, under pressure from regulators and the Treasury, there are codes of practice covering mortgages, banking and general insurance.
- The travel sector.

It would be a nonsense if trade associations found themselves in a position of having a code of practice endorsed by a specific regulator or government department only for the OFT to say that it did not meet its standards. Similarly, it would be a nonsense if in meeting OFT standards a code of practice did something that the government department or regulator disapproved of to such an extent that they might publicly be critical of the code. The government needs to get its act together in this area. All departments which have an interest in consumer matters should embrace the OFT initiative, should ensure that they take the OFT guidelines as their starting point and should encourage trade associations in their sectors to sponsor codes of practice that meet the OFT guidelines. If the government cannot get its act together in this way then trade associations are entitled to ignore the OFT initiative and indeed to criticise government.

The prognosis is not good. At present, the government is involved in three initiatives with respect to codes of practice –

- It has commissioned a high level review of the banking and mortgage codes.
- It has launched the Quality Mark scheme for the building industry.
- It has established a task force to consider problems in the car repair and servicing industries.

There appears to be no co-ordination of these initiatives and no consistent approach within government. At first sight it is surprising that the banking and mortgage codes

should have singled out for scrutiny. They are probably among the most effective of all codes in every respect. The Quality Mark scheme is fundamentally misconceived. It is supposed to deal with “cowboy” builders; in practice it will do no so thing but might give a halo to the best companies in the sector. Car servicing and repairs is an area where there is massive consumer detriment and where government has singularly failed to deal with the problem. The government is much softer with the building and car servicing and repair industries where there are real problems, than it is with the banking and mortgage industries where reasonably effective codes are already in place.

The need for guidance and support

The point has already been made that trade associations will want to have a dialogue with the OFT before finalising codes for stage one approval. This section expands on this point.

In any form of regulation there is a constant battle between those who want “certainty” and those who prefer to rely on broad principles. Paradoxically, it is often industry itself that prefers “certainty”. This then leads to a rather perverse situation of government proposing a fairly loose rein regulatory system which trade associations then want turned into a detailed rule book. There is no doubt that the OFT will come under such pressure. It should be resisted as far as possible, but there is a balance to be struck.

The criteria in the consultation paper are logical but they are broad brush and associations will want to know how they are to be interpreted. The consultation paper devoted just ten lines to the content of codes and these are in broad terms, such as “clear precontractual information” and “guarantees and warranties”. It is easy for a code of practice to stipulate that members must provide a guarantee, but if the guarantee is for just one month and applies only in onerous conditions (for example, the practice of some manufacturers of electrical equipment who require an item that is said not to be working to be returned in its original packaging) then is this acceptable? Similarly, the code has to cover “delivery/completion dates”. Does this mean it is acceptable to say that delivery will be made in a one-week slot or rather should the requirement be within a two-hour slot?

The proposals require the sponsors to publish the results of the performance indicators to demonstrate the effectiveness of the code and also to assess regularly consumer satisfaction. What will happen if the mystery shopping shows a 30% level of compliance and consumer satisfaction is under 50%? Will support be withdrawn?

It may be argued that now is not the time to address these issues. However, there is a danger that if they are not addressed then they will come back to bite associations and the OFT at a later stage with the result that the new regime is discredited.

This is an area where perhaps trade associations should seek to get together with the OFT and other interested parties to try to agree some general principles so that these can be taken into account by associations at an early stage of their process of drawing up new codes.

Problem areas for associations

There are five major issues which associations will have to face in meeting the OFT criteria.

The code requires code sponsors “to demonstrate that organisations representing **consumers, enforcement bodies and advisory services have been adequately consulted** throughout the preparation of the code” and for stage two that they have been consulted “throughout the operation and monitoring of the code”. The consultation process can be a long drawn out affair. The following bodies will need to be consulted –

- National regulatory bodies such as the OFT itself and LACOTS (the central body for trading standards departments). However, the OFT has made it clear that it does not intend to become involved in detailed drafting.
- The sponsoring department and any specialist regulatory or other agency. Practice will vary considerably between sectors. Where there is a specialist regulator or a department that is actively involved in a sector then it will want to have a say in a code of practice and will not be content to leave matters to the OFT. Indeed, there may well be a position whereby the sponsoring department or regulatory body has already endorsed a code that does not meet the new OFT requirements. Rather than dream of joined-up government associations will have to work round this problem.
- National consumer bodies such as the National Consumer Council (NCC), the Consumers’ Association (CA) and the National Association of Citizens Advice Bureaux (NACAB).
- Any industry specific consumer bodies. There are a number of organisations that purport to represent consumers, for example associations of bank or insurance customers or the Patients’ Association, but many such organisations are tiny in terms of the number of customers of the sector, are not representative, are secretive about their membership and how they formulate policy, and in some cases are ego trips for the person running them. In many sectors, for example shoe repairs, there will be no organisation representing consumers. How can organisations representing consumers be involved in such sectors? An association can address this issue through extensive market research, most probably using focus groups, or alternatively or perhaps additionally by involving people identifiable as representing the interests of consumers to join the governing body of the code. Such people can be identified with the help of bodies such as the NCC. However, there is likely to be a shortage of good quality people.

There is a requirement to have a “low cost, speedy, responsive, accessible and user friendly **independent redress** scheme to act as an alternative to seeking court action in the first instance”. The OFT stresses that independence is vital in any redress scheme and that it shall be binding on members who must not be able to prevent a customer taking his complaint to the redress mechanism. For some sectors an ombudsman scheme is the solution but this is costly to put in place. Arbitration is less costly and can deal with sectors where there are comparatively few complaints. The Chartered Institute of Arbitrators runs over 70 consumer dispute resolution schemes, most of which offer arbitration only but some of which include mediation and other forms of alternative dispute resolution.

Code sponsors are required to have **performance indicators**, with mystery shopping exercises and independent compliance audits being given as examples, to measure the effectiveness of the code. In stage two they will be required to publish the results of the performance indicators and also to assess regularly consumer satisfaction. A useful first stage is to require members to certify annually that they have complied with each aspect of the code. Mystery shopping is easy to arrange and there are a number of market research organisations that will do this work. Similarly, a number of independent organisations would be willing to undertake auditing of compliance of the code. The issue is the cost of these arrangements, which can be substantial. In many sectors meeting this requirement is likely to require expenditure well in excess of £50,000 a year if it is to be regarded as meaningful, with perhaps also an additional burden on the companies that subscribe to the code.

Code sponsors will need **disciplinary arrangements** which are likely to culminate in termination of membership of the code and therefore perhaps also the trade association. Associations need to be very careful in this area. It is no longer acceptable to expel members through a loose disciplinary mechanism. It is necessary to build in independence, appeals procedures and correct procedure generally. It is sensible to take legal advice although such advice will probably result in even more complex arrangements “just to be safe”.

For many associations the key issue will be **whether members will want a meaningful code** of practice. Some associations probably realise deficiencies in their existing arrangements but know that they could not push through tougher arrangements with their members. Probably the OFT paper will help those associations wishing to strengthen their codes but still there is the question of how far members will be pushed.

The issue is likely to produce conflict within associations between those members that genuinely want to increase standards and kick out the cowboys and the cowboys themselves who want to be able to state that they are operating according to a code of practice as long as it does not influence their behaviour. The key sticking points for members are likely to be -

- The content of the code itself. This is an area where general guidelines are of little help, as each code will need to be tailored to the particular sector. It is also the area where consumer representatives are likely to take a very different view from industry representatives. This would apply to such matters as delivery times, completion dates, cooling off periods, phased payments and so on.
- Audit arrangements, which at a minimum are likely to include annual self-certification that each point in the code of practice has been complied with throughout the year. This is likely to be a major sticking point in some sectors. Many companies are far more enthusiastic about a tough code than they are about ensuring that it applies in practice.
- Binding redress arrangements.
- The cost of putting the new arrangements in place both through the trade association subscription, through membership of a code of practice if a separate charge is made and also for the cost of arbitration arrangements.

Priority sectors

Properly, the consultation paper says that the OFT's aim is to target those areas where actual or potential consumer detriment is high and consumers need to be able to identify better traders. The OFT lists a sensible set of criteria for selection of priority sectors. These are fully supported with the one exception of the criterion "absence of an alternative self-regulatory regime (eg Trust UK for e-commerce; the DETR's builders' Quality Mark scheme)". It is understood that the major feature of both these schemes is the lack of take up. This applies particularly to the DETR's builders' quality mark scheme where, before the recent relaunch, there were just two builders signed up. The scheme purports to represent an attempt to deal with the cowboy builder problem but actually seeks to give a halo to the best builders. It will do nothing, even in its relaunched form, to address the problem of cowboy builders.

The priority sectors should be extended to include all forms of building and house repair work (except new housebuilding) including the installation of double-glazing, conservatories, kitchens and bathrooms as well as general building work. There are three other areas that might usefully be added to the list –

- Computer support services where there is widespread dissatisfaction with the inability to obtain the necessary and promised support.
- Telephone helplines where there is a suspicion, perhaps not well founded, that people are paying to hang on for someone to speak to them.
- Time slots for deliveries and service call. Notwithstanding mobile phones some companies (eg Argos) seem unable to predict when they can deliver something within eight hours.

The issue of joined-up government is relevant here. The overall objective is not to have codes of practice per se. Rather, it is to address real consumer concerns. The various arms of government should aim to secure the implementation of effective codes in problem areas rather than pursue easy targets where codes less needed. The final two items pose a problem for policy makers because they are cross-sectoral. An innovative approach to policy making needs to be used.

The proposed criteria

This section comments in detail on the criteria set out in Annexe B to the consultation paper.

Paragraph B1

Bearing in mind that these criteria will be widely reproduced the introduction to them is unsatisfactory. Under the heading of "Overarching principles" are a couple of paragraphs about timing. The first section would be better headed "Introduction" and then there should be a single overriding principle clearly spelled out along the lines of: "The OFT will seek to endorse only those codes which are effective in protecting consumer interests by offering specific and worthwhile benefits beyond those required by law".

Paragraph B.2 a)

"Significant influence" should not be equated with "a majority of firms in the sector" as a majority of firms could easily have just 5% of the market. This would be true for

building work or car repairs. Rather, the criterion should be over half of activity in the sector.

Paragraph B.2 c)

Rather than specify “independent disciplinary procedures” it would be better to specify “disciplinary procedures with a significant independent element”.

Paragraph B.3 b)

This would be better worded: “Code sponsors shall be able to demonstrate that relevant consumer organisations, enforcement bodies and advisory services have been adequately consulted throughout the preparation of the code. Where there is no appropriate body representing consumers then there shall be meaningful market research among consumers and/or individuals recognised as representing the consumer interest must be consulted”.

Paragraph B.3 c)

As above.

Paragraph B.4 a)

The words “arising within” should be replaced by “in”.

Paragraph B.4 c)

The general point is that these are very vague and will require considerable amplification and guidance if they are to be meaningful. The most important part of the code is what is in it. While it is probably not possible to go into much more detail in the formal criteria, unless they are complemented by extensive guidance they will be of little help. Among other points which could usefully be included are –

- Information about the code itself.
- Contact details for enquires or complaints.
- Refund policy.

Paragraph B.5 a)

This is all reasonable but the implications of the fourth bullet point are huge. To set up such a scheme is very expensive. Is this really necessary for shoe repairs? For some sectors the right option would be to latch on to an existing scheme. Associations would probably value guidance in this area.

Paragraph B.6 a)

It is not clear why some of these provisions are applicable to stage two only. Surely codes must build in the necessary compliance and monitoring arrangements in order to get approval from the OFT in the first place? It is also not clear whether what matters is the publication of the results of monitoring or rather what the results of monitoring show. Is the test a measure of consumer satisfaction or is it that consumer satisfaction must be at a certain level? Similarly, is the test that the performance indicators’ results should be published or that they should be good? It is not at all clear why the requirement to have an annual report should be applicable to stage two only. This must be built into the scheme and the OFT should receive reports from the outset.

Perhaps the OFT is suggesting that it will base stage 2 approval on the results of the various monitoring exercises, which will not be clear for at least a year after a new code has been implemented.

Paragraph B.8

There should be an additional requirement that the code of practice and any published information about the code, such as annual reports, should be on the website of the sponsors.

Arrangements for low value products

The proposals in the consultation paper are most relevant to fairly large sectors with scope for substantial consumer detriment and where a large trade association has the necessary clout and resources. The annual costs of running a code that will qualify for stage 2 approval are likely to be a minimum of £50,000 and well in excess of £1 million for some sectors. These conditions apply mainly in regulated sectors and financial services. They also apply to building work, car repairs and servicing, house removals, funerals, estate agency and travel agency.

But there are many small sectors comprising largely small businesses where it will be difficult to meet the OFT criteria. Using the list of consultees to the consultation paper as a starting point, the following sectors may come into this category: cheque cashers, footwear, photography, locksmiths, tyre distributors, shoe repairers and ticket agents. With the proposals as they stand the associations may face the choice of continuing their codes without OFT recognition (and therefore being devalued in the marketplace) or abandoning the codes. This may reduce the protection which consumers currently enjoy - a classic example of the best being the enemy of the good.

The major stumbling blocks in these small sectors are consultation with consumers (unless letters to the major consumer bodies are considered adequate), conciliation and redress arrangements (in particular the independent element of redress arrangement) and monitoring arrangements.

One possible approach to this problem is to stick with the proposals more or less as they stand but through guidance to set out how a regime could work for small sectors. This could include –

- Accepting that letters to the NCC, CA, NACAB and LACOTS inviting their views and later inviting them to comment on the draft code are sufficient.
- Relying on self-certification and monitoring complaints for monitoring.
- Tapping into a general redress service rather than creating one specific to the sector.

Alternatively, the OFT could devise a modified regime for small value sectors.

A natural market reaction to the OFT's proposals would be for some codes to be amalgamated or at least for some elements, in particular redress, to be amalgamated.

Areas where this could usefully happen include shoe retailing and repairing, building work and car servicing and repairs.

OFT resources

It is clear from the paper that the OFT has limited resources. This is given as one reason for the two stage process. The work required by the OFT for stage two is clearly greater than for stage one although the OFT may have underestimated the amount of work that will need to be done in stage one. The development of a code of practice to meet the new OFT guidelines will cost associations thousands of pounds each and each code will cost a substantial amount of money to run, perhaps millions of pounds for the major sectors. It is therefore wholly appropriate that the OFT devotes sufficient resources to helping associations develop meaningful codes and to fulfilling its monitoring role. These resources are unlikely to materialise from the government. The other source of funding is trade associations themselves. There is no reason why the OFT should not charge associations for giving the stage one approval and the stage two endorsement to reflect the work it does.

The OFT should also consider the use of accreditation agencies to assist it in its work. It may be more acceptable for a trade association to pay a third party than to pay the OFT directly. However it should be recognised that those same accreditation agencies will be seeking business from trade associations and it is essential to avoid any conflict of interest in this area.

The consultation process

In November 2000 the Cabinet Office published an obligatory Code of Practice for government departments and agencies on consultation exercises. Like the OFT proposals this recognises the importance of compliance. One would expect the OFT to ensure that in a consultation paper on codes of practice, it took care to comply with codes to which it is subject. The consultation paper states that it complies with the Cabinet Office guidelines that are reproduced in Annexe E. In fact the consultation paper does not fully comply with the guidelines. Only the headline criteria have been complied with rather than the detailed points set out in the Cabinet Office paper. The position is not helped by the criteria being reproduced in the wrong format without the seven points being clearly listed (five of them are listed as being a subset of a sixth).

Specifically –

- It does not include an assessment of the impact of the proposals on groups likely to be particularly affected – in this case trade associations. (Criterion 2.2)
- Arguably, as the proposals will create a burden for business, they should have been accompanied by a draft regulatory assessment. (Criterion 2.3)
- Representative groups are not asked, in responding, to give a summary of the people and organisations they represent. (Criterion 2.7)
- No details are given of a contact who can respond to consultees' questions (as opposed to the person to whom responses should be sent). (Criterion 3.9)
- No details are given of someone who will pursue complaints or comments about the consultation process. (Criterion 3.10)
- There is no indication on the OFT's website that the Office has appointed a consultation co-ordinator. (Criterion 7.)

If the OFT is seeking (correctly) to make private sector codes more meaningful then it would seem sensible for it to comply with codes to which it is subject.

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