CP 21/13: a new consumer duty

Response from Shoosmiths

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CP 21/13: a new consumer duty

We welcome the opportunity to respond to the Financial Conduct Authority's consultation paper CP21/13: A new Consumer Duty. This paper sets out our responses, drawing on insights from clients and analysis from our group of specialists.

Shoosmiths LLP is a major UK law firm, comprising 210 partners and over 1,600 lawyers and employees. The financial services sector is one of our key areas of focus: we support financial services firms ranging from new starts and FinTechs to major banks, building societies, lenders, investment companies and insurers. With offices in 13 locations across the UK, we provide advice on English, Scots and Northern Irish law and act for financial services firms in each jurisdiction.

Shoosmiths LLP is an FCA authorised firm, but our responses in this paper represent our thoughts, as legal and regulatory advisors, on how the proposals would affect our clients and the broader financial services market. We are not responding in terms of how the proposals might affect Shoosmiths LLP as an FCA authorised firm.

In certain responses we include examples based on particular sectors, products or services to provide context for our comments. These are intended to be illustrative and not exhaustive.

Q1: What are your views on the consumer harms that the Consumer Duty would seek to address, and/or the wider context in which it is proposed?

It is not unreasonable to address the "consumer harms" set out in paragraph 2.8 of CP21/13. The intention to better protect against consumer harm is clearly appropriate. However, what is important to note is the shift from "process-focused" rules to "outcomes-focused" rules: that is a current theme in FCA proposals and policy, and it makes it significantly more challenging for firms. We have some specific concerns about how the introduction of the Consumer Duty and a shift to "outcomes-focused" regulation will be implemented. Firms need certainty in order to remain compliant.

Review of existing legislative and regulatory framework

Given the breadth of the financial services markets which the FCA regulates and the number of changes currently being proposed within those sectors, we encourage the FCA to look at the Consumer Duty, its Transformation programme and other proposed reforms holistically. When undertaking reform in one area, there is a risk that the consequences of reform may not be appreciated in the context of the wider existing framework. We encourage the FCA to carefully interrogate how the Consumer Duty will sit alongside the existing legislative and regulatory framework for each of the markets it regulates.

We have set out some examples of where additional clarity is needed regarding how the Consumer Duty will operate alongside existing legislation and regulation.

Disclosure of information - Firms have been pointing out for years that there is a risk of "information overload" from the amount of information that firms are obliged to provide to consumers, whether this is under statute, retained EU legislation, or FCA rules and guidance. Meeting the information needs of the consumer, at the appropriate time, is of vital importance to the consumer's ability to make the right decisions. However, in order to achieve that, existing legislation and regulatory requirements must be reviewed.

Examples of this are:

- Consumer credit notices which are in a prescribed form, where the language could be improved.
- Pre-contract credit information, which is in a prescribed form and in reality, is not a helpful document for consumers to understand.
- Statements of fees under the Payment Accounts Directive, which include prescribed elements that do not align neatly with UK banking practice.

  In the first two examples above, failing to present consumer credit notices and statements or the pre-contract credit information in the exact form or with precise content leads to draconian sanctions for the lender, meaning that lenders must focus on tick box compliance rather than assessing the outcome a customer consumer is receiving.

Our concern is that, in some markets, the Consumer Duty will require firms to serve two masters (i) to comply with tick box regulations (examples of which are set out above); and (ii) to consider whether the legally prescribed disclosures allow a firm to satisfy the Consumer Duty, the Cross-cutting rules and outcomes. In the likely event that a firm considers that legally prescribed disclosures do not satisfy its obligations under the Consumer Duty, this will lead to duplication of disclosures and information overload which will be confusing to consumers. The greater the quantity of information provided to a customer, the less likely they might be to read it or to distinguish between what they need to know as consumer and what they are legally required to be told.

We consider that the current consumer credit regime is incompatible with outcomes-based regulation without the much-needed reform of consumer credit legislation.

1. **Unfair credit relationships** - The unfair relationship regime under the Consumer Credit Act 1974: is the Consumer Duty additive to this, or is it intended to help interpret what an unfair relationship may be? What does a proposed PROA add to the unfair credit relationship regime?
2. **Best execution** - Will the duty of best execution under COBS require re-interpretation in light of the proposed Consumer Duty? At the very least, guidance is required on which how firms should interpret their obligations under COBS and SYSC pursuant to any Consumer Duty.

Supervision and Enforcement

We recognise that supervision and enforcement was raised in DP18/05 and that the FCA is revising its approach to regulation by way of its Transformation programme. The FCA refers to more information being made available on this as the Transformation work evolves. We would encourage the FCA to make information available on this in a timely manner so that firms can properly assess how the FCA will supervise in the future together with assessing the Consumer Duty.

Careful consideration will need to be given to the timeframe for implementation of the new Consumer Duty and there will need to be proper consultation of the detail of any new rules. There is otherwise a risk that previously accepted conduct will be assessed by reference to new standards (with a new and enhanced Consumer Duty being applied to judge past conduct). We consider that the proposed time frame which would see the new rules introduced in July 2022 following the proposed publication of the second Consultation Paper at the end of 2021 is unrealistic, not least where the detail of the proposed rules remains unclear.

Existing Principles

Many of the consumer harms listed by the FCA in the Consultation Paper are already covered by Principle 6, Principle 7 or existing rules. Those rules are tailored to address specific risks in relevant markets. It may be more appropriate for the FCA to build upon existing principles rather than introducing a new Consumer Duty. The FCA could introduce the Outcomes to aid the interpretation of Principle 6 and Principle 7 in specific markets.

Q2: What are your views on the proposed structure of the Consumer Duty, with its high-level Principle, Cross-cutting Rules and the Four Outcomes?

We consider that the proposed structure is not unreasonable in principle, provided that the new Principle informs the interpretation of the Cross-cutting Rules which in turn inform interpretation of the Four Outcomes. The structure makes sense but questions arise relating to how the Principle, the Cross-cutting Rules and the Four Outcomes are to be applied and interpreted. Some of our specific concerns are set out below.

Certainty

Regulators should improve confidence in compliance for those they regulate, by providing greater certainty . Without detailed rules and guidance and a willingness to engage with firms, the package of measures proposed will not give firms sufficient certainty to revise their communications, policies and processes to ensure compliance.

A lack of certainty of application on a sector-by-sector and case-by-case basis is also likely to have various adverse effects, including the following:

- Senior manager functions will not have confidence that the policies, procedures, documentation and training meet the expected standards.
- Firms may be more conservative in their approach than they need to be, due to fear of non-compliance. This may limit their actions and ultimately consumer choice.
- Firms will seek certainty by obtaining external advice, and the outcome will be the creation of rules and procedures which reflect “tick box” compliance, simply because firms need metrics for compliance. This has been demonstrated by practice arising after previous attempts by the FCA to move away from “tick box” compliance. For example, senior managers and board members will want the confidence that a new product proposal is compliant before proceeding; compliance monitoring functions will need metrics in order to report whether the firm is compliant with requirements; and law firms providing sign-off or advice will need to have confidence in the advice they give.
- Ambiguity in how the package of measures is applied in various cases will result in more referrals to FOS (which will likely lead to resource issues and longer case handling times); a proliferation in claims raised by claims management companies, resulting in additional cost to firms in responding to what could be very thin claims; and more recourse to the courts, who (as the FCA recognises) will seek to set precedents in order to reduce the volume of future claims.

- Ambiguity is also likely to lead to firms taking different interpretations on what compliance means. This could result in uneven communications and services across the market, which could unravel the FCA's work in aiming to ensure that like-for-like products are explained and operated in a consistent manner, so that consumers can more easily compare products and services when deciding whether to switch products and/or providers. While existing FCA rules should maintain that ability to compare products and services, the information outcome could lead to firms adding more information in a way which then leads to inconsistency.

Q3: Do you agree or have any comments about our intention to apply the Consumer Duty to firms' dealing with retail clients as defined in the FCA Handbook? In the context of regulated activities, are there any other consumers to whom the Duty should relate?

The application to retail clients is acceptable and makes sense in principle. In the longer term, the definition of "retail client" will most likely be expanded due to other proposals, for example, changes to the definition of "sophisticated investor" in the financial promotion rules.

What is not clear is how firms should deal with more experienced or knowledgeable retail clients. Under COBS 3.5.3R, for example, retail clients can become "elective professional clients" if certain conditions are met and those retail clients agree to that treatment. The aim of this is to allow such clients to have access to products and services that otherwise would not be available to them. Will similar considerations apply under the Consumer Duty? If the answer is no, is there a risk that more sophisticated retail clients are disenfranchised from making certain product or service choices? This could be of particular concern to investment managers and private banks. For example, it may restrict the ability of private banks to make available a suite of products and services available to such clients.

Another area of concern is the proposal around the "distribution chain" for retail clients which will lead to wholesale market participants finding themselves subject to the rules. This also applies to "execution-only" services, which will no longer be "execution-only".

An interesting question arises in relation to deposit brokers. Deposit broking is not a regulated activity, so deposit brokers do not have to be regulated – although some are, because they provide investment services also.

In the case of a deposit platform which is not regulated, you would end up with a deposit broker having no Consumer Duty, contracting with a bank or building society who has a Consumer Duty but does not actually owe this to the consumers because the deposit broker is the bank or building society's customer.

As a result, the deposit broking market may split into two: (1) brokers who are regulated and comply with the Consumer Duty, and incur costs in doing so which are passed down in part to consumers through their pricing; and (2) brokers who are not regulated and who do not incur such costs, so may be able to offer better rates. The result could be to move the market into the non-regulated deposit broker market, with fewer protections for consumers.

Banks and building societies may also be nervous dealing with non-regulated deposit brokers because even although they may owe no Consumer Duty, they may feel this is not what the FCA expected as an outcome – so they may be concerned about non-compliance with the Consumer Duty even although it does not strictly speaking apply.

Q4: Do you agree or have any comments about our intention to apply the Consumer Duty to all firms engaging in regulated activities across the retail distribution chain, including where they do not have a direct customer relationship with the 'end-user' of their product or service?

We are broadly in agreement with this principle, but have two concerns:

1. It is impractical for a firm in the "distribution chain" to determine, prior to the fact, what "ability [it has] to influence outcomes for consumers" when dealing with other wholesale participants; and
2. There is a risk of creating an uneven playing field. Firms which have a distribution or supply chain where other firms are regulated will have more success in delivering good outcomes compared to those firms whose suppliers are not regulated.

For example:

- technical service providers, such as cloud outsourcing suppliers, IT providers or data analytics firms.
- overseas regulated firms, e.g. EU regulated firms who (with some vindication) will argue that they are meeting their required standards by complying with their local laws.

  In these situations, we can see that there will be difficulties in persuading those firms to agree terms and change their services so that the regulated firm can deliver good outcomes.

This may then put pressure on firms to terminate relationships which are otherwise effective in order to find regulated UK suppliers who will be subject to the Consumer Duty. This would result in increased costs and a narrowing of choice in the market and in some cases could create insuperable difficulties for UK firms who have no choice but to use overseas service providers for certain elements of delivery (e.g. for local execution, custody or bank clearing).

It is important the FCA addresses these concerns in terms of setting out its expectations for firms.

Q5: What are your views on the options proposed for the drafting of the Consumer Principle? Do you consider there are alternative formulations that would better reflect the strong proactive focus on consumer interests and consumer outcomes we want to achieve?

We do not believe the two proposed alternative Principles are the same.

We also note that neither formulation in terms embeds the proposed concept of "reasonableness" which the FCA has indicated would qualify the obligation.

Option 1: A firm must act to deliver good outcomes for retail clients

Unless there is clear guidance, there is a risk that Option 1 will be interpreted as an obligation to achieve "good outcomes" (rather than act with the objective of so doing). In areas such as investment advice this could create a risk of advice becoming inappropriately conservative, not least given the lack of clarity as to what would represent a "good outcome".

The wording presents the risk of a firm being responsible for all circumstances applying to a consumer including those over which they have no control. How far does a firm have to go to deliver good outcomes for clients? If a consumer receives all information and makes a poor decision for their personal circumstances, how far must a firm go to prevent this?

The FCA has also noted that the Four Outcomes are the "key" good outcomes they are not exhaustive. Lack of clarity in this area creates uncertainty as to what will actually be the FCA's expectations.

Option 2: A firm must act in the best interests of retail clients

We note that the FCA does not intend this to be a fiduciary duty but using the words "best interests" does give that implication. Certain markets already have rules requiring firms to act "honestly, fairly and professionally in accordance with the best interests" of its customers or clients (e.g. ICOBS 2.5.-1 and COBS 2.1). It is unclear whether these rules would remain or whether they would be changed to impose a more exacting standard for retail clients.

A focus on "best interests" is harder to reconcile across all types of financial products or services, and will inevitably make firms and consumers think that this involves some general form of advisory or suitability assessment even though the FCA has said this is not what is intended.

The FCA should ensure that this does not have any adverse effects in other markets prior to adopting this wording. For example:

- where products are not sold on an advised basis, does this require a firm to find out detailed information about each consumer so that it can ensure it is acting in the best interests of that consumer.
- If a firm is offering lower risk products such as interest free retail finance at point of sale, will their duty to act in the best interests be interpreted proportionately?

The FCA will also need to carefully consider consistency with other existing provisions of the Handbook: for example COBS9.5A (insistent clients). On balance, our preference would be Option 2, although this does beg the question what a new principle provides in terms of consumer protection.

If it adopts either of these forms of wording, the FCA needs to ensure:

1. that the Principle remains consistent with and paired to the Cross-Cutting Rules and Outcomes as these will inform the interpretation of the Principle;
2. that the FCA issues guidance to assist firms in understanding what "good outcomes" or "best interests" means and how this will be interpreted in the different markets the FCA regulates. We consider that a "one size fits all" approach across all markets will create difficulties; and
3. The extent to which either formulation will increase the pressure on firms to seek more information than is necessary or which is intrusive.

Q6: Do you agree that these are the right areas of focus for Cross-cutting Rules which develop and amplify the Consumer Principle's high-level expectations?

We believe the FCA should provide guidance regarding some of the phrasing.

Avoid causing foreseeable harm

"Foreseeability" is a legal concept which is the subject of much case law and academic discussion. The FCA should provide clear guidance regarding what this means here and whether this is a regulatory standard or legal test. Presumably, as firms are specialist in their sector, the harm which a specific firm could regard as foreseeable is one which that firm, by virtue of its knowledge of the market, can foresee? The same consideration would apply to the firm's knowledge of the individual consumer, and their needs and vulnerabilities. Does this then mean that foreseeability is based on subjective knowledge on a case-by-case basis, rather than an objective "reasonable firm" test?

Enable customers to pursue their financial objectives

This is very broad, and again must rely on the firm's role, its sector, and its knowledge of the consumer. For example, a firm providing an execution only or non-advised service would have a duty to ensure that its products and services were fit for use by the types of consumers it reasonably expects to take up such products and services. The firm would not know the individual consumer's financial objective, and would only be able to assume some of these from the nature of the product or service. By contrast, a firm providing advisory or discretionary services would have a duty to understand more about the consumer's specific objectives. Does this relate to the product a consumer is purchasing or using at the time or does the reference to "wider financial objectives" include other financial products or decisions over which a firm may have no control?

Act in good faith

Again, the firm's role, sector and knowledge of the consumer could lead to different interpretations of what acting "in good faith" means.

All reasonable steps

This term is often debated by lawyers and is invariably interpreted by the courts depending on the specific factual circumstances under consideration.. Does it mean to take all steps (regardless of cost or the firm's commercial objectives)? What does reasonable mean in the context?

We encourage the FCA to provide clear guidance to allow firms to understand the requirements of the Cross-cutting Rules. Our expectation is that the guidance and interpretation should be consistent with existing guidance in other areas (for example MiFID 2) to be part of a broader examination of the best execution owed to customers.

Q7: Do you agree with these early-stage indications of what the Cross-cutting Rules should require?

Please see the notes at Q6 above.

In addition:

1. The focus on "behavioural bias" of individual clients is difficult. Requiring firms to identify, take account of and address each individual client's "biases" is impossible.
2. The ability of firms to demonstrate that consumers may "pursue their financial objectives". An individual's financial objectives invariably change over time and a firm might not be made aware that they have done so unless notified by the client itself.

Q8: To what extent would these proposals, in conjunction with our Vulnerability Guidance, enhance firms' focus on appropriate levels of care for vulnerable consumers?

The Vulnerability Guidance set out the FCA's expectations in relation to dealing with vulnerable consumers. This was particularly helpful in setting out the FCA's expectations for firms with online customer journeys. The Consumer Duty now sets out additional standards on consumer outcomes. We would welcome guidance from the FCA on how the Vulnerability Guidance will work alongside the Consumer Duty. We encourage the FCA to make it clear to firms and consumers how all the various parts of the regulatory framework operate together. There is a risk that reform relating to the proposed Consumer Duty may lead to unintended consequences in other areas. Firms may raise concerns again about how to identify and manage vulnerability, and the costs of doing so, which will be exacerbated by the overlay of the Consumer Duty.

Q9: What are your views on whether Principles 6 or 7, and/or the TCF Outcomes should be disapplied where the Consumer Duty applies? Do you foresee any practical difficulties with either retaining these, or with disapplying them?

If the Consumer Principle is to be additive to Principles 6 and/or 7 then effectively the FCA is saying that it sets a higher standard than those Principles. As such, it would make sense – and reduce the risk of confusion – to disapply those Principles where the Consumer Principle applies, or alternatively to rephrase Principles so as to reflect the existence of the new Consumer Principle so that there is absolute clarity as to which principles apply in a given situation. In either instance, it would need to be made clear that to the extent that the Consumer Principle imposes higher standards then have hitherto existed it cannot be used to assess past conduct (where Principles 6 and 7 would still be determinative).

We note that the FCA states at paragraph 3.38: "There is a lot of Handbook and non-Handbook material that reflects the language of these existing Principles, as well as guidance to firms on how to comply with them. A lot of it is relevant to conduct within the scope of the proposed Consumer Duty. We do not propose to revisit all this material immediately if we proceed with the proposals set out in this Consultation Paper. Instead, we would expect firms to continue to take into account material based on Principles 6 and 7, which predates the Consumer Duty."

We note the FCA apparently does intend to revisit existing material, but not "immediately". We consider that this will present difficulties to firms if they are using guidance and material relating to Principle 6 and 7 to inform how to interpret the Consumer Duty, which is setting a higher standard. The Principle 6 and 7 guidance and materials may lead a firm to an incorrect view on how to act. We reiterate our comment that this Consumer Duty must be viewed holistically. Introducing a new Consumer Duty, rules and outcomes, disapplying Principle 6 and 7 where the Consumer Principle is engaged but retaining the Handbook materials relating to Principle 6 and 7 is confusing.

The FCA's desire to implement the Consumer Duty should not be at the expense of clarity.

We encourage the FCA to take time in implementing this (if it chooses to do so) and consider how the Consumer Duty fits in the existing legislative and regulatory framework and to provide updated guidance. If the FCA is imposing new and heightened obligations on firms then it has a duty to provide clarity to firm's to enable them to discharge those obligations.

Q10: Do you have views on how we should treat existing Handbook material that relates to Principles 6 or 7, in the event that we introduce a Consumer Duty?

This is a very important point. As explained in our earlier response, the FCA need to review the existing material in the Handbook in light of the introduction of the package of measures around a Consumer Duty. The FCA needs to provide clarity as to how the Consumer Duty will operate and how compliance will be assessed well before the Consumer Duty is introduced and to ensure that firm's have a proper opportunity to revisit existing policies and practices accordingly.

Q11: What are your views on the extent to which these proposals, as a whole, would advance the FCA's consumer protection and competition objectives?

If implemented appropriately and proportionately, the proposals will promote greater consumer protection from the harms the FCA identifies.

However, the FCA should consider the adverse impact on its competition objective. We have some concerns that a Consumer Duty will lead to fewer firms operating in the sector, fewer products being available, firms withdrawing from certain customer groups (e.g. lenders not offering credit to the sub-prime sector) and more cases being referred to the FOS. Even though the FCA intends to embed the concept of "reasonableness" into the interpretation of the Consumer Duty, if firms are required to act in the "best interests" of consumers or deliver good outcomes, firms could be held responsible every time a consumer is unhappy (or considers that they have not obtained a "good" outcome). This would be in contradiction to the FCA's objective to promote effective competition in the interests of consumers in particular markets.

Q12: Do you agree that what we have proposed amounts to a duty of care? If not, what further measures would be needed? Do you think it should be labelled as a duty of care, and might there be upsides or downsides in doing so?

We consider that in some ways the wording proposed is more onerous than a duty of care. A duty of care is usually defined in law as a requirement to exercise reasonable care and skill. The FCA's proposed form of wording of good outcomes or best interests goes further than this.

We do not consider that this should be labelled as a duty of care. The term "duty of care" carries too much meaning following centuries of case law (ranging from duties in contract and tort and in the context of specific relationships such as agent and principal relationships). As and when cases on the Consumer Duty reach the courts, if the term "duty of care" is used the courts would have to determine whether a Consumer Duty "of care" is different from precedents on duty of care elsewhere. It may as a result interpret that duty more narrowly than the FCA intends.

For example, a regulated firm in the distribution chain which does not have a direct relationship with the end-consumer will nonetheless have a Consumer Duty, but if this were called a "duty of care" then general law would categorise this as a tortious duty in the absence of a contractual relationship with the person to whom that duty is owed. A court would then have to be satisfied that the test for this new duty is different from those of established precedent on tortious duty of care (if that is what is intended). Any level of ambiguity or uncertainty will lead to confusion and criticism from courts. (Few judges are specialists in financial services). Alternatively, courts may take the view that the same tests apply as for other cases of tortious duties – which may then take the Consumer Duty away from what the FCA intends. Put short, the FCA may ultimately "lose control" of the Consumer Duty if it makes it a duty of care.

As the FCA has recognised, the duty may be much lower where the firm's role is limited; in such cases, it is difficult to call this a "duty of care", because the term "care" in itself implies a clear assumption of responsibility to the individual/s who may be the subject of harm.

Q13: What are your views on our proposals for the Communications outcome?

This is likely to be problematic in practice. Firms will be unable to communicate in a way which their potential customers wish them to do. For example:

- in certain areas of financial regulation, legislation directs what must be said – and in some cases (e.g. certain disclosures under consumer credit law) prohibits further information. Is the Communications outcome intended to be additive to what is prescribed, meaning that firms would have to provide information outside of the prescribed text? For example, in the case of a default notice under the Consumer Credit Act, would firms be expected to provide a cover letter explaining the prescribed notice in clearer language? We consider this creates a risk of duplicating disclosures and information overload.
- if the Communications outcome results in additional information being disclosed over and above what is already required by legislation or FCA regulation, this increases the risk of:
    1. information overload (see our response to Q1 above), which in itself could be regarded as a "sludge practice";
    2. consumers not being able to see key disclosures amongst the "information dump"; and
    3. increased consumer disengagement from reading what they should and increased customer journey times (again, reflecting the deterrent effect of "sludge practices").

The FCA needs to consider carefully how this works in digital environments. A major advance in recent years has been the ease of consumers being able to sign up to new products online or by phone. The FCA has encouraged digitisation of products and services where appropriate, and it has clear cost benefits for firms which are reflected in pricing. Firms comply with the disclosure requirements, but there are legitimate questions as to whether many consumers actually read any of the important disclosures in their speed to sign up or simply confirm that they have done so. The FCA must consider the balance between consumer convenience (and the decision not to read disclosures) and firm's disclosure requirements.

There is a risk that unclear application of this outcome to digital journeys will result in a regression in this market, worsened consumer experience, and less favourable pricing.

The communications outcome will encourage firms to think about how they can best deliver communications to consumers to allow a consumer to make an informed decision, but what is the incentive for a firm to do this if it still has to comply with formulaic disclosure requirements (e.g. pre-contract credit information in consumer credit)?

Again, we urge the FCA to consider the Consumer Duty, rules and outcomes alongside the legislative and regulatory framework for all markets it regulates.

Q14: What impact do you think the proposals would have on consumer outcomes in this area?

General Impact

Due to the uncertainty and reach of the new proposed rules, the most likely outcomes in our opinion are:

- fewer participants;
- lower innovation;
- fewer products available; and
- more litigation/pressure on the FOS.

Consumers who are able to acquire products and services may feel better protected, however, there will be a material deleterious effect on competition.

Q15: What are your views on our proposals for the Products and Services outcome?

The monitoring requirement on firms to ensure that products and services remain "fit for purpose" is not objectionable per se. However, it will become onerous and time-consuming and very difficult to demonstrate.

The FCA should consider ranking the four outcomes. For example, if a firm achieves the "Communications" outcome, then it should satisfy the "Customer Service" outcome and the "Products & Services" outcome.

We also have concerns around:

- firms in a distribution chain each taking responsibility for good outcomes. Some firms in a chain may not be regulated, and as noted in our earlier comments, this may create a disadvantage for other regulated firms in the chain. Moreover, if there is no certainty over what compliance looks like, there is a risk that firms in a chain may disagree over what is required to achieve good outcomes.
- outsourcing to non-regulated firms, because some regulated firms may not have the bargaining power to influence the non-regulated outsourcee to agree to provide services to standards which lead to good outcomes. This will especially be the case where there is no certainty over what requirements are needed in order for those good outcomes to be reached.

As a result, there is a concern that where a firm has to outsource, it may have to consider changing its outsourcee – which may not always be possible, or financially as convenient as using the existing outsourcee – or take the risk of not complying with the Products and Services outcome.

Q16: What impact do you think the proposals would have on consumer outcomes in this area?

Please see our comments under General Impact under Q14 above.

Q17: What are your views on our proposals for the Customer Service outcome?

As mentioned above, there are concerns in relation to firms in a chain, and outsourcing of services. There is also a concern surrounding the lack of certainty when it comes to considering service needs. Processes in particular have to be given a metric and be supervised on that basis (especially when it comes to outsourcing – it is a requirement under the EBA Guidelines on Outsourcing Arrangements, for example). As such, firms need to have the confidence of knowing that the correct metrics have been applied.

Without certainty, there is a risk that firms may either overengineer their processes, resulting in additional unnecessary cost, or may decide that they cannot provide processes in a way which they believe is compliant, resulting in a withdrawal of service or delivery lines and a narrowing of consumer choice.

We support the customer service outcome in relation to contracts being terminable on reasonable notice and/or without penalty. However, firms may have spent significant funding costs or built a portfolio for a client from which it is not practical to exit. In the webinar, the FCA stated that a contract should be as easy to get out of as it is to enter. We agree in principle, but the FCA should consider a firm's costs in the initial offering of products to consumers. In practice, allowing a consumer to exit as easily as they entered is going to prove a very difficult task for firms to fulfil.

Q18: What impact do you think the proposals would have on consumer outcomes in this area?

See General Impact section of Q14 above.

Q19: What are your views on our proposals for the Price and Value outcome?

These proposals make sense overall. However, please note the observations in relation to the statement that "firms would not be providing fair value if the price consumers pay for a product/service is not reasonable relative to its expected benefits":

1. This must overlap with the Communications outcome. The FCA recognises that certain products and services carry inherent risks, and it is not the intention of the Consumer Duty to take away from a consumer their responsibility for making a decision where this results in a loss which they accepted. As such, whether a product or service is reasonable value has to take account of what the consumer was told, and what they clearly accepted.
2. Many products have variable pricing while the benefit of the product may be static. Taking the example of a regulated mortgage contract, the consumer receives the benefit on drawdown – the mortgage loan contributes towards the consumer's purchase of the house. However, if the mortgage loan is variable (or becomes variable after expiry of a fixed rate period), then the price paid for that benefit may increase over time, sometimes significantly.
3. In the case of savings, a consumer's expected benefit from a savings product is to receive an interest return. If the interest is variable, the consumer runs the risk of receiving less interest than expected. However, that is the nature of the product. Clearly, the FCA does not intend to say that variable rate products cannot vary to the consumer's detriment. The FCA has to be careful in how it phrases the Price and Value outcome.

The FCA needs to consider (and demonstrate) as to what "fair value" actually entails or open the possibility for increased litigation in relation to this point.

Q20: What impact do you think the proposals would have on consumer outcomes in this area?

See General impact section of Q14 and Q19 above.

Q21: Do you have views on the PROA that are specific to the proposals for a Consumer Duty?

We consider that extending the PROA to the Consumer Duty at a level whereby the right of action would attach to a breach of a Principle, rather than an underlying rule, has a superficial attraction but would not be appropriate for a number of reasons.

There would be no logical justification for extending the PROA to one specific Principle and not to others. However, Principles are of necessity couched in general terms and as the CP notes section 138D FSMA permits a claim to be brought for a breach of a rule but not a Principle. That reflects the fact that framing a cause of action for breach of a Principle creates uncertainty and is capable of being highly subjective.

Given the terms of section 138D we do not accept the statement at paragraph 5.5 that a PROA could be introduced for a breach of the Consumer Principle (as opposed to any underlying rules implementing the Consumer Duty) by way of an amendment to the Handbook. To achieve that an amendment to primary legislation would in our view be required.

The comment in relation to section 404 of FSMA at paragraph 5.9 as to the unavailability of industry-wide redress scheme where there is a breach of a Principle is correct but it only creates an issue in practice where the only apparent basis for a claim is a breach of a Principle (and nothing more). Where a breach of a rule exists provided the other requirements are met then section 404 can be used by the FCA to implement a redress scheme.

The absence of a cause of action for breach of a Principle has not to date caused any obstacle to date to the bringing of claims under section 138D. Claims have been advanced by reference to specific rules (for example, the suitability rules under COBS) as well as established legal duties in contract and tort.

However, it is important to appreciate that the Courts have repeatedly made clear that they are not concerned with failures of process but rather with outcomes. Loss is not assumed but must be proven. Many claims fail on the basis that whilst a claimant can point to a breach of legal duty, they are unable to demonstrate that they have in fact suffered a loss.

We see a significant risk of claims being advanced which may be well-founded in terms of a failure of process but where little or no consideration is given to how that translates into a recoverable loss and which fail as a consequence. Unlike FOS, the Courts do not compensate on the basis of what they consider to be reasonable in the circumstances but on established principles of foreseeability and causation.

Whilst the comment at 5.14 with regard to costs is correct, it does miss the point that the majority of claims which would arises from a breach of the Consumer Duty would be modest (and almost certainly well below the figure of £200,000). Claims below £10,000 are subject to the small claims jurisdiction (where no costs can be recovered save in exceptional circumstances) and the recoverability of costs in claims above that amount will depend on the allocation of the case (Fast Track or Multitrack). Many modest claims can be uneconomic to bring.

The Court system is also under increasing pressure to deal with its existing case load. Legal proceedings can be lengthy, and litigants are subject of specific legal obligations and incur costs risks if they fail to comply with these. Further, there is increasing pressure from the judiciary for parties to legal proceedings to mediate their disputes and it is anticipated that costs penalties for failure to mediate will be introduced.

In the present context, the likely outcome in many cases would be that both parties will be under pressure to settle their claims. From the claimant's perspective this will result in claimants recovering less than the true value of their claim. For firms it will make them vulnerable to speculative low value claims on the basis that the costs that would be incurred in defending the claim (which are likely to be irrecoverable in whole or in part in many instances) make it uneconomic to fight the claim, regardless of the underlying merits. However, firms may consider that they have no alternative but to fight a claim that lacks merit because to do otherwise is likely to make them even more vulnerable to high-volume, low value claims.

There is also a risk that the existence of a PROA would potentially deter the FCA from taking action in appropriate circumstances to secure redress (for example, as part of its enforcement processes) where it is appropriate for it to do so on the basis that affected consumers can pursue claims individually. The FCA could then shy away from more challenging and resource heavy cases and focus on those matters which are more straightforward for it to pursue.

In order to mitigate the risk of CMCs bringing speculative claims it is imperative that a fee cap on CMC charges is introduced as proposed.

Consumer Credit

In consumer credit, it is not clear how a PROA would work alongside the unfair credit relationships regime, which already allows a consumer to bring an action against a lender if they have been treated unfairly. This action is already widely drafted and construed by courts. If the FCA adopts a PROA, which we would strongly encourage the FCA not to, then it should clarify how this will work alongside the unfair credit relationships regime in consumer credit.

Q Q22: To what extent would a future decision to provide, or not provide, a PROA for breaches of the Consumer Duty have an influence on your answers to the other questions in this consultation?

If a PROA is considered, then rather than the Consumer Duty, the FCA should consider regulating the products and services which can be made available to consumers: quantitative tests per product/service which, if passed, the firm can then move on to qualitative tests.

As the FCA acknowledges, a PROA will lead to claims management companies raising claims – many of which may be spurious but time-consuming and costly for firms to manage.

A PROA may be workable if there is sufficiently certainty over what is or is not compliant, but in reality, this will be the outcome of the FCA's consultation.

Consequently, firms would have legitimate concerns about numerous cases being raised with no real basis for claim, which will drive up firms' costs and ultimately impact what firms charge for their products and services.

The introduction of a PROA for breach of the Consumer Principle would be a significant legal development. It would take time for the jurisprudence around such a PROA to develop which would create legal uncertainty and if a PROA has been introduced before the FCA has issued guidance to assist the Courts in determining how the PROA should be applied then the FCA runs the risk of significant judicial criticism. We have stressed two concepts through our response:

1. the need for greater certainty regarding the proposed Consumer Duty for firms; and
2. the importance of the FCA considering how the proposed Consumer Duty impacts upon each of the markets it regulates and its existing legislation.

If a PROA is introduced then these concepts become even more critical. However, they still need to be addressed even if a PROA is not introduced.

Q23: To what extent would your firm's existing culture, policies and processes enable it to meet the proposed requirements? What changes do you envisage needing to make, and do you have an early indication of the scale of costs involved?

N/A

Q24: [If you have indicated a likely need to make changes] Which elements of the Consumer Duty are most likely to necessitate changes in culture, policies or processes?

N/A

Q25: To what extent would the Consumer Duty bring benefits for consumers, individual firms, markets, or for the retail financial services industry as a whole?

If implemented appropriately and proportionately, there would be benefits for consumers, but at the risk of detriment to firms if the FCA does not provide detailed rules and guidance in order to give firms confidence and certainty in what their expectations are, and what compliance looks like.

Q26: What unintended consequences might arise from the introduction of a Consumer Duty?

Impact upon existing legislation

As referenced throughout our response, our concern is that the Consumer Duty will be added as an additional layer over existing legislation and regulation. In markets, which are already subject to detailed legislation (e.g. consumer credit or payments services), the Consumer Duty coupled with existing legislation will serve to stifle innovation further.

Supply chain

The need for firms to reflect the new rules in their supply chain – for example in back-end services and outsourcing agreements between regulated firms and their suppliers / partners.

To an extent this will likely be treated much the same as any other compliance issue – where firms seek to oblige their suppliers to comply (and ensure that their products and services comply) with the rules (and look for indemnities for failure to comply), whereas their suppliers will look to avoid responsibility / liability for compliance and to put the onus on the firms to ensure that the product / services being purchased meet their needs. Suppliers will also be looking to exclude their liability.

In the absence of very clear / minimum mandatory requirements which firms are consistently required to include in relevant behind the scenes purchase agreements, this could lead (as has been the case with e.g. SYSC, FG16/5 and data protection regulations) to time-consuming debates between firms and their suppliers on allocation of risk and responsibility. One risk is that potentially over-cautious compliance teams in firms, and suppliers looking to avoid additional liability will collide, and firms with less bargaining power will only be able to achieve sub-optimal positions in their contracts.

Wholesale markets

Wholesale markets participants and execution-only brokers could become de facto "financial advisers". The FOB may become over-whelmed and additional legislation and guidance would then be required.

Q27: What are your views on the amount of time that would be needed to implement a Consumer Duty following finalisation of the rules? Are there any aspects that would require a longer lead-time?

The Consumer Duty is (and is intended to be) a material change to the relationship with existing (as well as future) clients. Firms must be given a long lead-time to establish the changes to their existing relationships. It appears that the FCA currently envisages the new framework being operative within six months of the second Consultation Paper being introduced at the end of 2021.

Firms would need to do an end-to-end review of their policies, processes, training and communications. This in itself will take time. Into this we need to factor existing project commitments, where project management, legal, compliance and IT resources will already have been allocated.

Compliance with elements of the Consumer Duty may lead to firms having to amend or upgrade IT systems, which takes considerable time and can lead to considerable cost.

Compliance may also require firms to assess third party supply / distribution chain arrangements and amend these - or even replace them. Again, this will take time and incur considerable cost.

As a result, viewed realistically firms would need more than two years to implement the changes in their final form prior to their formal introduction.

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