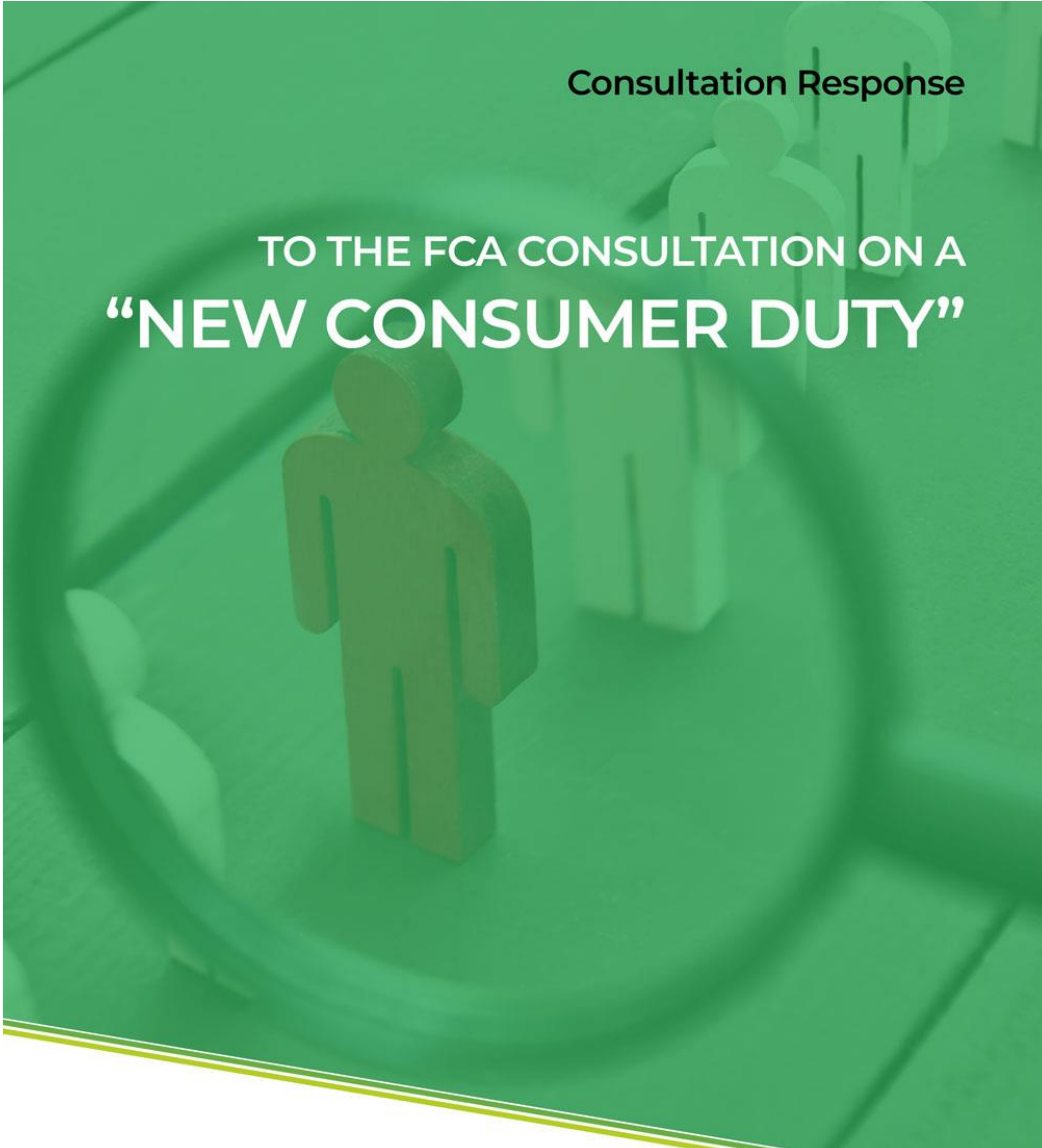

Consultation Response

TO THE FCA CONSULTATION ON A "NEW CONSUMER DUTY"

National Consumer Federation

NCF

@NCFvoice
nationalconsumer.org.uk

Overview

We welcome the opportunity to contribute to the FCA's consultation on a New Consumer Duty and welcome the concept behind the proposals. The National Consumer Federation has long been concerned with the need for a significant shift in financial services firms' culture and behaviour and for the need to see a much higher level of consumer protection in retail financial markets.

In 2011 we recommended a shift of regulation to better address consumer protection achieved by means of regulation applicable to the actual financial products sold to consumers. The report reviewed the history of the FSA's 'Treating Customers Fairly' initiative, its success/failure to that date and gave recommendations for improvement. The report's executive summary and recommendations are given in ANNEX 1 to this paper. If anything, strengthening regulation to address a duty of care across financial product lifecycles is even more important today.

What we continue to see is that the FCA is focussed on the internal processes of companies rather than on a consumer focus. We believe there is a need for more focus on what is delivered to consumers with the ability for the FCA to take action when external deliverables and actions are causing harm. We also refer you to the NCF's Consumer Charter for Regulators that was prepared with support from across the consumer movement. The Charter outlines the key requirements for effective regulation from the consumer perspective.[1]

There is a need to focus on the avoidance and minimisation of harms. The lack of a duty of care limits the harms covered to contractual relationships. Hence beneficiaries of an insurance product (third parties) have no rights if it doesn't deliver to them. Harm associated with insurance products is not limited to those who make claims if a risk arises. Insurance is sold on peace of mind that risks are covered. The FCA refer to a data-led approach. High underwriting margins indicate a lack of competition at the point of sale or a poor appreciation on the part of consumers of the risks actually covered or both. Examples include products like PPI or mechanical breakdown or Gap insurance. Here the product providers are wholesalers who should not be able to avoid responsibility for the actions of retailers.

Private rights of action (or the lack of) are seen by lawyers as critical. This may be necessary but they are very unlikely to be sufficient to protect the majority of consumers. The right to sue is only as good as the means of enforcing it. It risks generating income for lawyers and claims management companies but little by way of redress for consumers. Examples of successful collective action look attractive but cover only a very low proportion of existing harms. Compensation schemes may be set up by the FCA for particular products, otherwise consumers could seek redress through the Financial Ombudsman Scheme. However, we question how the FoS relates to the present proposals?

In answering the consultation questions we call for a formal, enforceable duty of care. ANNEX 2 provides a list of consumer vulnerabilities that need to be addressed by the duty of care.

In the time available to us we have provided answers to the consultation questions most relevant to our interests.

CP21/13 Annex 1 Financial Conduct Authority A New Consumer Duty

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?

[1] http://thencf.org.uk/wp-content/uploads/2021/04/Consumer-Charter-for-Regulators-1-1.pdf

An issue of concern to us is that to date, TCF has focussed too much on internal industry processes, resulting in a box ticking culture and a lack of attention to whether the products and services provided represent fair value and good outcomes for consumers. It is essential for consumers that the FCA holds firms to a much higher standard than has been the case since TCF was introduced. The focus in the Duty on ensuring that products and services are fit for purpose, represent fair value and are clearly communicated and understandable is therefore welcome, as is the recognition that there needs to be a significant culture shift in the financial services industry.

However, Section 29 of the Financial Services Act 2021, requires the FCA to carry out a consultation on the introduction of a Duty of Care. This consultation does not meet this requirement and therefore falls short of the FCA's statutory obligation to consult on this issue (see our response to Q12 below). In a survey conducted by the FCA's Consumer Panel, while no financial services respondents wanted a duty of care to be introduced, 92% of consumers did. While we support the majority of measures comprising the New Consumer Duty, we believe that unless a Duty of Care is implemented, consumers will continue to experience poor outcomes.

You have said that you will focus increasingly on the outcomes being experienced by consumers using a data-led approach and that you will challenge firms and intervene robustly where firm practices adversely impact those outcomes. While the Duty might help to ensure that more firms 'get it right in the first place' thus reducing the need for enforcement or remediation, we would also have liked to have seen more detail in the consultation on the FCA's proposed approach to enforcing the Duty. You have also said that you will raise the level of consumer protection by stopping the sale of products that are not fit for purpose and/or do not offer fair value. We look forward to seeing more detail regarding how you will address these issues.

The 'front line' of consumer protection against harm is the financial product itself. Has a financial product been designed to avoid harms or reduce risks of harm if some harms cannot be avoided ? Product liability, market monitoring of products across their lifecycle and enforcement need to be a strong theme in any FCA duty of care regulatory improvements.

Product assessment and approval schemes should be developed that embed a duty of care in meeting consumer expectations and minimising harms from both normal use and misuse of products. Such product assessment to be alongside any distribution, sales and product support duty of care regulation associated with consumer financial products.

Note As an example of a sector with similar problems, that has recently created products with consumer's own risk control and potential harm reduction, the Gambling Commission[2] have caused the main gambling suppliers to create products suitable for their consumer context that provide user product functional controls for the user's risk taking and potential financial loss.

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?

For the Duty to have its intended impact it is indeed essential that firms consider the Duty 'at every stage of [their] processes and at every level of [their] organisational structure'. This setting of overarching expectations across all areas of firm conduct via the cross-cutting rules is very much needed in the industry and may help to reduce 'silo non-compliance' in firms, i.e. where some functions may be focussed on ensuring positive outcomes for customers while others, particularly those at a remove from direct customer contact, while ticking boxes, may pay little real attention to customer outcomes and potentially cause serious harms to consumers. In combination with the high-level principle and the four outcomes, with effective FCA surveillance and enforcement, these cross-cutting rules could help to ensure more joined-up compliance with TCF and a better customer

[2] https://www.gamblingcommission.gov.uk

journey with positive outcomes. However, for the desired culture change to take place, the focus needs to move away from sales to behavioural incentives. Historically, the culture and reward system in financial services has tended towards a top-down approach focused on education and training and incentives for sales performance. This has had considerable impact on knowledge and skill development but poor outcomes as far as attitudes, behaviours and improvement of service delivery are concerned. Making senior executives in financial services firms personally accountable for breaches of the principle could help to shift behaviours and firm culture in the right direction more rapidly.

Q3: Do you agree or have any comments about our intention to apply the Consumer Duty to firms' dealings 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?

We agree that the Consumer Duty should be applied to firms' dealings with retail clients and that this term should apply to all such clients including SMEs which in many cases do not possess the financial acumen and experience to be treated as 'knowledgeable' or 'professional'.

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?

Firms that operate exclusively in wholesale markets as part of a distribution chain for retail products or services should be subject to the Consumer Duty. Therefore, the Duty should apply where a firm can, through its regulated activities, influence material aspects of the design, target market or performance of a product or service that will be used by consumers.

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 prefer Option 1: 'A firm must act to deliver good outcomes for retail clients' with an enhancement (see below*) as Option2 'A firm must act in the best interests of retail clients' seems to be simply restating what is already in the Handbook. 'Best interests' is a vague term which is harder to define than 'good outcomes' which can be more readily clarified and exemplified and its use in the Handbook hereto does not seem to have impacted the industry's ability to deliver good outcomes for customers adequately.

However, *Option 1 should embed explicitly first and foremost as duty of care the avoidance of and minimisation of harms to consumers.

Option 1 will only have currency if the rules and guidance in the wider Consumer Duty provides firms with genuine clarity on what 'good' looks like. As 'good outcome' or 'best interest' in themselves have no legal meaning, the introduction of a general Duty of Care would be helpful in terms of encouraging firms to consider and focus on outcomes that are genuinely good for consumers.

The FCA should consider supporting a duty of care with the wide sharing of industry knowledge of consumer harms and good practices in avoiding or reducing risks of harm.

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?

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

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

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?

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? 52 CP21/13 Annex 1 Financial Conduct Authority A New Consumer Duty

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?

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?

What you have proposed does not in itself constitute a 'duty of care' and therefore cannot be labelled as such. A duty of care is a legally enforceable obligation upon, in this instance, regulated persons towards those who are in their reasonable perspective as being likely to be harmed as a result of their acts and omissions. The question does not seek opinions on the upsides and downsides of creating a Duty of Care, only opinions on the upsides and the downsides of labelling the FCA proposal as a Duty of Care which it very evidently is not.

Whilst CP21/13 does contain a section (5) on a possible private right of action (PROA) in relation to the high-level Principle, and while duties of care apply to some of the TCF rules, this is not the same thing as a general duty of care and, indeed, it is positioned as a separate matter to a duty of care. Section 29 of the Financial Services Act 2021 requires the FCA to ask in a consultation if a duty of care should be imposed, whether or not the FCA should make general rules as to the standard of care and if the answer to that question is yes, should the rules be an alternative to, or in addition to, the imposition of a duty of care. This consultation has not explicitly asked any of these questions.

The introduction of a general Duty of Care would enable the FCA to order firms to fully honour their obligations to consumers and use its powers under section 404 of FSMA to impose an industry-wide redress scheme, if necessary, in relation to breaches of any of the principles. It would provide consumers, who have suffered foreseeable harms due to the actions or inactions of authorised firms or persons, with the legal right to conduct a private right of action (PROA) for damages. One would hope that from the consumer perspective this would be a rarely needed last resort. However, under the proposed Consumer Duty, the FCA's enforcement powers will continue to be limited, consumers would have no right to sue and compensation would continue to be dependent on the FCA either imposing a restitution order (an infrequent event) or in negotiating voluntary redress. Evidence suggests that historically this has not resulted in satisfactory outcomes for a large number of affected consumers.

While the prospect of potential PROAs may increase liability insurance costs for firms and create new opportunities for claims companies, with the problems that might accompany this, more importantly, a Duty of Care would encourage financial services firms to comply with the Duty. We do not accept that a Duty of Care would discourage firms from developing innovative products or services, or restrict consumer choice and competition or worsen outcomes for consumers. On the contrary, a Duty of Care would help to protect consumers from the development of supposedly 'innovative' products which produce poor outcomes for consumers. The FCA argument that giving the industry time to deliver this consultation's proposed outcomes, without the prospect of private action being brought, might be important to fully realise the consumer benefits of the cultural and mindset changes the Consumer Duty aims to achieve is illogical. The industry is much more likely to respond rapidly in terms of cultural and mindset change if a Duty of Care is introduced.

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

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

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

See also the NCF responses to Q1 and Q5 re financial products design to reduce the potential for harm and product assessment, combined with the most basic part of a duty of care being to avoid or reduce harm.

You state that you will set out a clear and consistent expectation of how firms should assess whether the prices of products and services offer fair value. There is insufficient detail in the proposed Duty about how firms should go about this. For example, while firms have been obliged to abandon commission payments, disclose charges on investments and to ensure that they have assessed a customers' financial position and risk appetite before recommending an investment solution for quite some time, there continues to be considerable mis-selling in this product sector largely due to misrepresentation, mismatch with investor needs and inadequate risk disclosure. A further issue with investment products is that the provider and/or the intermediary invariably has limited control over performance outcomes. This means that firms need to be realistic and circumspect in terms of the performance expectations they convey to consumers. Exactly how the Duty intends to address provision of investment products and services remains to be seen.

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

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

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

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

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

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

See our response to Q 12 above.

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?

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?

Not applicable to our organisation

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?

Not applicable to our organisation

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?

Providing the Consumer Duty includes a general Duty of Care and is properly enforced, it will be a wake-up call for the industry to change its behaviours and culture and could have the potential to significantly improve outcomes for consumers.

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

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?

ANNEX 1

Fair enough?[3]

A report to Consumer Focus from the National Consumer Federation on the FSA's Treating Customers Fairly initiative

January 2011

Executive Summary

The FSA's Treating Customers Fairly initiative

This report undertakes a review of the history of the FSA's Treating Customers Fairly (TCF) initiative and its success/failure so far. It provides an assessment of the TCF principles and information supporting them based on the FSA's publicly available information, examining how TCF has been implemented.

The practical implementation is discussed and some recommendations made for improvement. Since the early 2000's the FSA has been developing an approach to address mis-selling and the fair treatment of customers. Their strategy was to bring about cultural change that embraces fair treatment and latterly on achieving the right outcomes for customers. We believe the principles, if applied, can be fully supported by consumers.

However, the implementation phase appears to have achieved little and has had little or no impact on consumers.

Key Draw backs of the current approach:

- The outcomes for TCF set by the FSA were weak and need to be re-expressed in more practical terms from the consumers' perspective;
- The intention to build consumer trust by letting companies work out what to implement and measure for themselves has failed to deliver a consistent or coherent framework;
- We believe the mechanism by which the industry is expected to apply the principles has led to higher costs than necessary and considerable divergence in firms' compliance. This in turn has made effective market surveillance very difficult;
- The TCF framework has failed to deliver substantive culture change;
- Remuneration strategies actively work against fairness;
- The TCF framework has failed to deliver sufficient analysis of the products and services offered to consumers, and has been too focused on process.

Before the announcements about the FSA by the coalition government, the FSA had announced their intention to be far more proactive with intervention to assess business models and product design right through the product chain to the market place using "intensive supervision". It is unclear how this will improve monitoring and assessment of the fair treatment of customers. This is a key issue that needs further work to identify and assess.

Potential for improving TCF

We do not believe that the TCF principles need any significant change and the FSA was right to change their overall approach from reactive to proactive but in our view the new emphasis will

[3] http://thencf.org.uk/wp-content/uploads/2021/07/004-Fair-enough-January-2011.pdf

potentially add to industry's costs and difficulties and still not focus adequately on the needs of the consumer unless considerable work is undertaken to further develop this broad framework.

Our recommendations include future development of the TCF initiative by building on existing good practice standards within the financial services industry and working more directly with stakeholders including consumers and consumer groups.

We also recommend addressing the issues faced by consumers arising from the complexity of many financial services products. We propose that this is achieved by developing common requirements that address the fairness issues raised by these products, hence reducing the need for lengthy and complex consultations with customers. We are not suggesting standardising the products themselves but only the requirements for those aspects pertinent to TCF.

In order for TCF to be fully effective it is also essential that there is a successful cultural change within companies. Senior management focus and responsibilities for TCF need strengthening and company incentive systems need to reward achievement of good TCF practice throughout the product life cycle.

Whilst not ignoring the need to oversee companies' internal processes, the new CPMA must place a greater emphasis on achieving consistent monitoring and assessment of the products and services provided by companies, primarily through market surveillance.

9. RECOMMENDATIONS

1. Maintain and, if necessary, enhance the principles of TCF in collaboration with all stakeholders.

2. Build on existing good practice standards within the financial services industry codes of practice and elsewhere, working directly with all stakeholders including consumer organisations to analyse and report on where these meet, exceed, or fall short of reasonable customer expectations of fair treatment.

3. Produce, in consultation with all stakeholders, an action plan to develop the relevant common assessment agreements needed to provide a level playing field for both consumers and the industry. *Note : it can be expected that there will be core fairness of service/conduct of business benchmarks for use generally by the financial services industry. It can reasonably be expected that some additional fairness criteria will arise from the characteristics of differing product types that are specific to parts of the industry e.g. there may be different detailed fairness requirements for insurance products and services compared with those for bank accounts.*

4. We recommend that standardisation mechanisms are developed through which the complexity of some if not all products can be taken away from the consumer. This would require a degree of standardisation across products and services to address the fairness issues raised by these complex products, whilst allowing firms to innovate within a framework of fairness. We are not suggesting standardising the products themselves but only the requirements for those aspects pertinent to TCF. Hence, if implemented correctly, businesses can be free to compete and innovate in the market place. The role of these product standards would be to address technical issues relevant to TCF on behalf of consumers, thereby removing the need for purchasers to understand all the technical details.

5. The cultural change element of TCF needs to be maintained and strengthened in two key ways. Firstly, the strengthening of senior management focus and responsibilities for TCF, and secondly ensuring that any incentive system rewards individuals and/or teams for the achievement of good TCF practice throughout the product life cycle.
6. Whilst not ignoring the need to oversee companies' internal processes, the new CPMA must place a greater emphasis on monitoring and assessing the products and services provided by companies, primarily through market surveillance.

7. Rebalance the surveillance and enforcement system for the financial services industry towards the consumer experience in the market place, working more closely with consumers and consumer organisations. The system needs to be more transparent, effective and we believe better coordinated.

ANNEX 2

Annex 1 – List of consumer vulnerabilities to be addressed by a Duty of Care

Note: based on previous work by the NCF and current work within ISO re: inclusive services which focuses on good practice in service provision that addresses consumer vulnerabilities. Examples shown in *italics*

Personal characteristics

Age – *Initially personal competences increase with age from baby to adulthood, Youth can be associated with inexperience; with aging the incidence of cognitive impairment may increase*

Gender – *gender identity discrimination, unable to access credit; discriminatory pricing*

Culture - *Differences in influencers, religion, beliefs and behaviour*

Geographical location - *Living in crowded premises or a rural or isolated area*

Personality – *Risk taking beyond ability to deal with risk, High levels of credulity, impulsiveness*

Health and abilities

Physical health - *Injury; chronic, severe or terminal illness*

Physical impairment - *Reduced dexterity, loss of mobility*

Sensory impairment - *Limitations to sight, touch or hearing*

Mental health – *anxiety, fears, depression, anxiety, bipolar, schizophrenia, suicidal thoughts*

Cognitive ability – *Ability to recognise (or not) scams, impairment - dementia, brain injury*

Developmental condition - *Autism; learning difficulty (e.g. dyslexia, ADHD)*

Addiction - *Alcohol, thrills, drugs or gambling*

Access and skills

Language - *Not fluent in official language(s) of country of residence*

Literacy or numeracy - *Low level of literacy or numeracy*

Digital access or technical skills - *No access to mobile phone, internet or computer; lack of knowledge or confidence in using technology.*

Household access – *lack of account access for services, and communications if accounts held in one person's name, as a consequence lack of ability to provide proof of identity*

Life events

Income shock - *Retirement; loss of job (own or partners) ; low or erratic income; poverty; debt*

Homelessness - *Lack of permanent address for communications, service provision and billing*

Abuse - *Victim of online, sexual, financial, domestic or elder abuse, preventing access to products or people*

Caring responsibilities – *children plus aged parents, Increased demands on time, emotional strain*

Bereavement - *Loss of a loved one*

Relationship breakdown - *Separation or divorce (see also abuse)*

Change of living situation - *Moving home; refugee; entering or leaving hospital or care; social isolation*

Parenting - *Pregnancy, new baby, maternity/ paternity responsibilities*

Economic - *Prices, inflation, recession, asset value reduction, scams*

External conditions

Health and environment - *Natural disaster, weather event (flood, drought, lightning), pandemic*

Market conditions - *Imbalance of power between an individual and an organization; inability to switch, complexity of market, services and products*

Organizational behaviour - *Poor communication, access, customer service or complaints management; poorly designed products or services, poor processes; poor practice in advertising, mis-selling; poor data management, such as poor data sharing controls, data breaches, leading to 3rd party exploitation of vulnerabilities*

@NCFvoice
nationalconsumer.org.uk