



Financial Conduct Authority (FCA) Consultation Paper CP21/13 A new Consumer Duty

Submission by The Financial Inclusion Centre

About The Financial Inclusion Centre

The Financial Inclusion Centre (FIC) is an independent, not-for-profit policy and research group (www.inclusioncentre.org.uk). The Centre's mission is to promote a financial system and financial markets that work for society. The Centre works at two main levels:

Promoting system level change

Research and policy development to promote sustainable, resilient, economically and socially useful financial markets that: benefit the environment; encourage responsible corporate behaviours and create a positive social impact; and efficiently allocate long term financial resources to the real economy.

Ensuring households' core financial services needs are met

Promoting fair and inclusive, efficient and competitive, well-governed and accountable, properly regulated financial markets and services that meet households' core financial needs. We do this by undertaking research into the causes of market failure in the sector, formulating policies to address that market failure, developing alternative solutions where the market cannot deliver, and campaigning for market reform. We focus on households who are excluded from, face discrimination in, or are underserved by financial markets and services.

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INTRODUCTION AND SUMMARY

- The Financial Inclusion Centre is pleased to submit a response to such an important consultation. We very much support the principle of, and the intent behind, a new Consumer Duty. In theory, a powerful Consumer Duty could help enhance consumer protection and *real* competition, and could advance the FCA's consumer protection and competition objectives.
- A properly implemented Consumer Duty would also help improve confidence and trust in the financial services industry. It could also promote *real* competition by helping those firms who want to treat customers fairly, and allow the FCA to penalise those firms which do not.
- We do not foresee any negative unintended consequences if the Consumer Duty is implemented properly. No doubt, some in the industry will claim that a Consumer Duty would stifle innovation, creativity, choice, and willingness of firms to market and sell to consumers with consequences for inclusion. This would be disingenuous.
- So much innovation in financial services is not actually socially useful and is designed for the benefit of firms' business models, to meet sales targets, and to exploit complexity. A robust Consumer Duty may well reduce the proliferation of products on the market that just add to search and distribution costs, and destroy value. It may reduce the *degree* of choice in the market but improve the *quality* of choice by forcing firms to become genuinely creative and develop socially useful products that represent fair value. That would be a good outcome.
- Competition cannot be relied on to drive out bad providers and products in financial services. A properly structured and enforced Consumer Duty could introduce real competition by allowing more efficient, consumer focused firms the space to thrive thereby supporting inclusion.
- Moreover, a new Consumer Duty (if properly implemented) represents to us a set of standards that society has the right to expect of well-run businesses. If some firms cannot trust themselves to engage with consumers on those terms and withdraw from the market, then that would be a good outcome.
- The new Consumer Duty should ensure that firms act in the best interests of consumers. We have no particular views on how this requirement to act in their interests should be labelled. What matters are the steps the FCA requires firms to take to ensure they are acting in the best interests of consumers. These requirements should ensure firms and others treat consumers fairly and act in their interests throughout the *whole* of the firm/ customer relationship not just at the interaction point where firms are competing for custom.
- We are concerned about calls from some quarters that the FCA should introduce a *duty of care*. This could undermine the intention of the Consumer Duty if the legal definition of duty of care becomes the standard for assessing whether firms are acting in consumers' best interests. The generally accepted legal meaning of a duty of care is an obligation to exercise **reasonable** care and skill when providing a product or service. Obliging firms to exercise *reasonable* care and skill in our view would not have the same direct beneficial effect on firm behaviours as the defensive/ precautionary and positive measures we advocate to make a new Consumer Duty work.
- To make financial markets work for consumers and wider society, a Consumer Duty should be supported by robust rules and meaningful outcomes. The FCA should have greater ambitions for the Consumer Duty. The FCA's definition of what an effective market looks like appears to be quite limited. A recurring theme throughout our submission is that the FCA has to **make** markets work. The Consumer Duty should not be seen as another mechanism designed to create the conditions for competition to drive up standards. We are concerned about the continued reluctance of the FCA to use proven, necessary interventions such as price caps.

- Critically, if a Consumer Duty is to have the desired effect, it should enable: more effective, responsive, and agile regulation; more effective supervision of markets and firms; and more effective enforcement and use of sanctions to deter harmful corporate practices. It should enhance the ability of consumers to obtain redress.
- Unfortunately, the emphasis in CP21/13 on consumer responsibility, tackling information asymmetries, and intention to use tests of reasonableness is unlikely to make markets work significantly better than is the case now.
- We are concerned about the phrasing that accompanies the FCA's proposals for a Consumer Duty. It could set expectations with regards to firm behaviour that could undermine the intended effect of the overarching duty. Phrases such as 'reasonable expectations' and 'causing *foreseeable* harm' are likely to be open to abuse by firms and intermediaries. These phrases could be open to interpretation and introduce a degree of uncertainty around the intent. This could make it difficult for the FCA to supervise markets, enforce against breaches and impose sanctions, and for consumers to obtain redress.
- It would be more effective if the FCA adopted a much tougher approach by requiring firms to adopt the *precautionary principle* when determining whether products and practices are likely to cause harm. Firms and intermediaries, with all the huge financial and technology/ data resources at their disposal, are well placed to determine the likelihood of harm resulting.
- It is unclear how the new duty as proposed by the FCA would deal with emerging risks at the intersection between FCA regulated financial services and non-regulated digital and data services and 'Big Tech' platforms. Regulated financial firms increasingly use digital and data services to target consumers and sell products. The FCA should emphasise that regulated firms must apply the Consumer Duty when using non-regulated digital and data services. Similarly, regulated firms should apply the Consumer Duty when associating with products and services outside the regulatory perimeter.
- It is not clear how the FCA's proposals on price and value would work. The FCA talks about '*products and services that do not represent fair value, where the benefits consumers receive are not reasonable relative to the price they pay*'. This is unlikely to result in significant improvements in prices and value for consumers. In many key financial services sectors, value is poor across the board. Product margins may be low because of high distribution costs so the end price for consumers will be high. But, with the FCA's approach, a firm selling a high price, poor value product could still be considered to be offering a fair price and value because the rest of the market is doing so.
- In other sectors, there may be a significant amount of choice available, so it looks as if there is competition in the market. But, industry margins can be high and significant value extracted from consumers. The result is that the market generally offers poor value. Actively managed investment funds are a case in point. It is genuinely difficult to see how actively managed funds (which tend to have higher prices) represent fair value if passive funds with similar investment objectives are available. In this case, would the FCA expect asset management firms to reduce prices or not sell products, or advisers and platforms to not recommend products?
- Consumers, particularly vulnerable consumers, cannot afford another experiment with competition as the primary mechanism for making markets work. So, we would urge the FCA to be more prescriptive on what concepts such as fair price and value mean and make it clear that it is ready to use price caps and other product interventions as a first resort not a last resort.

RESPONSE TO QUESTIONS

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?

The wider context

We deal with the wider context first. The FCA states in para 2.8, that financial services markets operate effectively, and in the interests of consumers, where:

- firms offer products and services that are fit for purpose in meeting the needs of customers in their target market, and offer fair value
- consumers are enabled to effectively access information and assess which products and services best meet their individual needs
- consumers are able to act effectively, taking responsibility for making decisions to meet their need

The definition used seems to neglect well-established conditions for effective markets such as:

- firms behave responsibly and treating customers fairly
- firms are effectively regulated and well-governed with conflicts of interest between shareholders/ owners and consumers managed effectively so that firms do not exploit imbalances of power
- markets are efficient, truly competitive¹
- markets produce *socially useful* innovations²
- markets utilise technological innovations to improve consumer welfare, not exploit consumers
- markets are transparent and accountable
- market failures do not generate externality costs borne by, or generate risks transferred to, consumers and/ or wider society
- consumers have *justified* confidence and trust in markets
- consumers are aware of their rights and the extent of protection available (including when they are not protected by regulation), and are able to enforce rights of redress
- regulatory standards can be easily enforced
- regulation is flexible, agile, and evolves rapidly to protect consumers from harmful innovation and emerging risks

¹ This is different to the usual text book definition of competition which uses conventional, but often misleading, indicators of competition such as: the extent of choice in a market, low margins, nature of barriers to entry and exit, and levels of switching etc. The fact that a market might meet the conventional text book conditions for competition does not mean that competition is actually delivering good and fair value for consumers

² Similarly, it is important to recognise the difference between innovation as generally understood (that is, the design, development, and distribution of 'new' products and services) and socially useful innovation. Financial services are constantly generating new products and services. This does not mean consumer welfare is being enhanced. Indeed, much innovation in financial services has been harmful to consumer welfare. Payday loans are a good example. Similarly, often innovation in financial services occurs to deal with the risks created by a previous set of innovations. More generally, the existence of plenty of choice in a market does not equate to socially useful innovation. There is a proliferation of products in financial services which just adds to search costs and creates unnecessary complexity and confusion.

The phrasing used, and approach implied, in the FCA's definition places too much emphasis on consumers being responsible for effective engagement with financial services. There is a significant imbalance in power between consumers and providers/ intermediaries in financial markets and services (and in digital markets and services which are playing an increasingly important role in financial services). The emphasis placed on consumer responsibility and addressing information asymmetries is at odds with the proposal for placing a new Consumer Duty on firms.

Encouragingly, the FCA states that the proposals extend to firms that are involved in the manufacture or supply of products and services to retail clients, *even if they do not have a direct relationship with the end customer*.

But, as the FCA will be aware, digital services firms including Big Tech platforms and information intermediaries now play a significant role in:

- manufacturing demand for financial products
- facilitating the selling of non-financial consumer products and services by facilitating access to consumer credit (eg. buy now, pay later)
- providing access to hyper targeted market research focusing on individual consumer profiling rather than group profiling
- allowing firms to target individual consumers and exploit behaviours
- product development and distribution through real time feedback loops and big data

We are concerned that this **intersection** between financial and digital services is poorly regulated. Digital services firms are not regulated to the same standards as financial services firms. Boards and senior managers of regulated primary product providers and intermediaries may be delegating too much responsibility for the above functions to poorly regulated digital services firms.

It would be helpful, therefore, if the FCA emphasised that the proposed Consumer Duty entails boards and senior managers of regulated firms paying much more attention to those functions which are not regulated by the FCA.³

It would also be helpful if the FCA elaborated, with clear examples, on how the proposed Consumer Duty would apply to regulated firms who are involved (consciously or inadvertently) in the marketing and promotion of financial products and activities which fall outside the regulatory perimeter.

We are concerned that the definition used above does not place weight on the need for firms and others in the market to treat consumers fairly throughout the *whole* of the firm/ customer relationship not just at the interaction point where firms are competing for custom, and consumers are making decisions as to which provider to select.

An example of this, relates to the very low level of county court judgments (CCJs) that are marked as 'satisfied' on the judgment register. It is not common knowledge that CCJs are marked as satisfied only if the debt is repaid **and** proof of payment is supplied to the courts in England and Wales (and to Registry Trust for other jurisdictions). This problem could be addressed by the FCA and other regulators⁴ requiring creditor firms within their remit to notify the courts when a debt has been

³ As an aside, FIC argues that we need a Digital Conduct Authority (DCA) to complement the work of the FCA.

⁴ Such as OFGEM, OFWAT, and OFCOM

repaid as part of treating customers fairly obligations (and now as part of the proposed Consumer Duty). Ensuring CCJs are marked as satisfied is a small step that could have a big impact on consumers' financial health and wellbeing. It could help consumers rebuild their finances and bring them back into the mainstream financial system - this will take on even greater significance as the economy recovers from the effects of the Covid. Importantly, this failure to ensure CCJs are marked as satisfied could actually prevent other firms that wish to offer better value products to those consumers who have paid a CCJ. This not just has implications for access to fair and affordable products but can undermine effective competition.

Types of industry practice and consumer harms, and the reality of competition in financial services

The FCA identifies a number of types of practice that can give rise to consumer harms such as:

- Consumers find it harder to make an informed or timely decision
- Consumers buy products and services that are inappropriate for their needs, of inadequate quality, too risky or otherwise harmful
- Consumers incur greater monetary and non-monetary costs
- Consumers receive sub-standard treatment during their relationship with a firm
- Consumers find it harder to switch or get a better deal

It would be helpful if the FCA talked about harm in terms of consumers being ***sold*** inappropriate or inadequate products and services, not consumers ***buying*** those products. This is not semantics. It better reflects the reality of financial services where products are aggressively sold, not actively bought by empowered, autonomous consumers. It would better reflect the nature of the dominant power dynamic a Consumer Duty is meant to address.

The main power dynamic in financial services is not demand from empowered, confident, aware, and autonomous consumers forcing providers and intermediaries to respond - thereby creating fair competition and a mutually satisfying commercial relationship between equal parties.

Rather, there is a clear power imbalance in the supply chain relationship between consumers and intermediaries/ firms/ shareholders. Firms (boards and senior managers) have an imperative to satisfy shareholders' interests.⁵ Firms are under pressure to generate sales and extract revenue from consumers. They compete for the attention of consumers to be able to maximise revenue, or they compete for distribution through intermediaries who also seek to maximise value from transactions and relationships. If anything, competition is characterised not by firms competing with each other to offer fair value but firms competing with consumers to see who can extract the most value from financial transactions and relationships.

A neglected aspect of competition is that which takes place *between* consumers for a limited quantum of value created by market activity. Certain groups of consumers are empowered,

⁵ Non-shareholder owned firms such as mutuals may not be under direct shareholder pressure. But, they do feel the effects of this pressure. If shareholder owned firms acquire market share through aggressive practices, mutuals can be forced to respond in kind.

confident, and aware enough to extract more than their fair share of value from financial transactions and relationships. By definition, that means others will lose out.

We will never get to the equilibrium position envisaged in economics text-books where a sufficiently large group of empowered consumers are actively buying products and services in a market - and therefore exerting control on the behaviours and practices of firms, intermediaries, and distributors.

The main dynamic will remain one where firms, intermediaries, and distributors have to aggressively sell products and services to survive and thrive. This dynamic is the main cause of harm in financial services. This is what a new Consumer Duty must seek to constrain.

When referring to non-monetary costs, it would be helpful if it was made clear that this relates to time costs and emotional costs (such as stress etc).

Below, we comment on the practices the FCA has identified which it believes causes those harms.

Types of practice	Comments on practices and harms caused
Firms providing information which is misleadingly presented or difficult for consumers to understand, hindering their ability to properly assess products/ services.	We agree that this is a common practice which can cause harm. But, a degree of realism is needed here. Trying to address information asymmetries does not have a good track record in financial regulation. The harm is often done by aggressive marketing practices and techniques which exploit behavioural biases. Ensuring information is not misleading etc is unlikely to provide a constraint on aggressive market and exploitative behavioural marketing practices. Firms providing better information should not preclude those firms being required to exercise self-restraint when it comes to selling inappropriate products to consumers. Moreover, this practice focuses on the information exchanged between <i>firms and consumers</i> . It does not cover information exchanged between firms and the rest of the market (including information intermediaries) which can determine whether consumers get a good and fair deal. The example, above, on the satisfactions of CCJs is a case in point.
Products and services that are not fit for purpose in delivering the benefits that consumers reasonably expect, or are not appropriate for the consumers they are being targeted at and sold to.	It is not clear what is meant by ‘consumers <i>reasonably</i> expect’. Reasonable expectations are, by definition, influenced by prior experience. If the market, overall, manufactures and sells products and services that are poor standard and value, then consumers will be accustomed to receiving poor value. They will not have had the opportunity to experience better products and services. We saw a historical example of this in the behaviour of insurance companies who were able to deny with-profits policyholders their fair share

	<p>of inherited estates (orphan assets) by exploiting the legal and regulatory interpretation of reasonable expectations. Insurance companies were allowed to determine what constituted a fair share of with profits fund returns. These funds were notoriously opaque and offered poor value for policyholders. Yet, policyholders' historic experience of receiving poor value was exploited by insurance companies to argue that this is what policyholders were used to and therefore met the definition of reasonable expectations.</p> <p>Therefore, the FCA should make it clear to firms that they cannot claim they are delivering what consumers reasonably expect just because they are selling what is standard in the market.</p>
<p>Products and services that do not represent fair value, where the benefits consumers receive are not reasonable relative to the price they pay</p>	<p>Again, it is not clear what is meant by <i>fair value</i> or <i>reasonable</i> relative to the price paid. In some markets, product margins may be low, but the product still offers poor value for consumers – because the market is inefficient overall. In other cases, there may be a significant amount of choice, but industry margins are high and significant value is extracted from consumers meaning that products are comparatively poor value. An example would be actively managed investment funds and certain advice services and platforms. In this case, would the FCA expect asset management firms to reduce prices or not sell products, or advisers and platforms to not recommend products?</p>
<p>Poor customer service that hinders consumers from taking timely action to manage their financial affairs and making use of products and services, or increases their costs in doing so</p>	<p>The definition of customer service should place weight on the need for firms and others in the market to treat consumers fairly throughout the <i>whole</i> of the firm/ customer relationship not just at the interaction point where firms are competing for custom, and consumers are making decisions as to which provider to select.</p>
<p>Other practices which hinder consumers' ability to act, or which exploit information asymmetries, consumer inertia, behavioural biases or vulnerabilities</p>	<p>This should include failure to provide positive information to the rest of the market (through information intermediaries) that may hinder consumers' ability to act or to get a better deal – see example of CCJs and satisfactions, above. We presume this particular example relates to ongoing relationships between firms and consumers. In this case, it is important that the definition of practices refers to the use of technological interventions – not just product or contract features – designed to hinder</p>

	<p>consumers’ ability to act, or exploit behavioural biases.</p> <p>We make a separate point below about presale targeting and point of sale activities.</p>
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Other practices

As mentioned above, we argue that regulated firms, as part of a Consumer Duty, should take greater responsibility for ensuring that when they utilise services provided by non-regulated providers, this does not result in negative consumer outcomes.

This is particularly important when it comes to the use of technology and big data to target vulnerable consumers and exploit behavioural biases *pre* sale.

Another emerging risk we are concerned about relates to the manufacture, marketing, and distribution of ESG products (including the repackaging and rebranding of non-ESG products). Third-party information intermediaries and ratings agencies are expected to play a significant role in the marketing and selling of ESG products to consumers. But, these intermediaries and ratings agencies are largely unregulated. There is a clear risk that product providers will select third party providers with the least onerous rating standards. It is not reasonable to expect consumers to be able to establish the comparative value of these supposedly independent ratings. It is to be hoped that the FCA will soon regulate these intermediaries and agencies. Until then, the FCA could protect consumers by ensuring that providers do not select ratings that are less exacting.

The FCA should emphasise that the proposed enhanced Consumer Duty would require boards and senior managers of regulated firms paying much more attention to activities that are not regulated by the FCA, but which are integral to the design, promotion, and distribution of regulated financial products.⁶

Another practice which may give rise to consumer harm is where regulated firms can facilitate access, and provide a ‘halo effect’ to providers, intermediaries, products, and activities which might fall outside the regulatory perimeter.⁷ The FCA should make it clear that the Consumer Duty applies to non-regulated activities where the regulated firm may have an influence over consumer behaviour and decision making.

We are unsure how the Consumer Duty might apply to situations where regulated firms have passed on outstanding consumer debts to FCA authorised third party debt purchasers or collection agencies, to third parties not authorised by the FCA, or to regulated debt purchasers or collection agencies which administer or buy non-regulated debt. We would welcome clarification on these issues.

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?

The FCA proposes that the Consumer Duty would have three elements:

⁶ As an aside, FIC argues that we need a Digital Conduct Authority (DCA) to complement the work of the FCA.

⁷ See, for example, the Gloster Report into the regulation of London Capital & Finance (LCF) [Gloster Report FINAL.pdf](https://publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/614212/Gloster_Report_FINAL.pdf) (publishing.service.gov.uk)

- An overarching Consumer Principle which sets a clear tone regarding the overall standards of behaviour the FCA wants from firms.
- Cross cutting rules. The FCA states that firms must take all reasonable steps to: avoid causing foreseeable harm, and enable customers to pursue their financial objectives. The FCA also states that firms must act in good faith toward customers.
- Four consumer outcomes. The FCA outlines four specific outcomes for the key elements of the firm-consumer relationship: 1. Communications 2. Products and Services 3. Customer Service 4. Price and Value. There will be a suite of rules and guidance which sets out more detailed expectations for firm conduct.

Critically, the real test of the new structure will be whether it forces the market to work for consumers through:

- more effective, responsive, flexible, and agile regulation;
- more effective supervision of markets and firms;
- more effective enforcement and use of sanctions to deter harmful corporate practices; and
- helping consumers obtain redress when firms do not comply with the higher standards envisaged.

We support the overall proposed structure. But, we would reiterate that for a Consumer Duty to have the intended effect, it must be able to deal with the full range of practices and harms described in our answer to the question above.

We also have concerns about the phrasing that accompanies the Cross Cutting Rules. This phrasing could set expectations with regards to firm behaviour that could undermine the intended effect of the overarching duty and principle.

The phrasing could introduce a degree of uncertainty as meanings could be too open to interpretation. This could make it difficult for the FCA to supervise markets, enforce against breaches and impose sanctions, and for consumers to obtain redress.

The phrases 'reasonable expectations' and 'causing foreseeable harm' are likely to be open to abuse by firms and intermediaries, and allow firms and intermediaries to challenge the FCA's efforts to apply the overarching duty and principle.

It would be more effective if the FCA adopted a much tougher approach by requiring firms to adopt the precautionary principle when determining whether products and practices are likely to cause harm. Firms and intermediaries, with all the huge financial and technology/ data resources at their disposal, are well placed to determine the likelihood of harm resulting.

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?

Yes, in general, we support the intention to use the definition of retail client. It is important that SMEs and charities are covered.

But, it would appear that the Consumer Duty would not apply to some customers such as certain pension funds and local authorities because of the definition of retail and institutional client in the

FCA's Handbook. We believe this opportunity should be taken to rectify this. Pension fund trustees and local authority officers are as vulnerable to misselling as SMEs and charity trustees. Indeed, the harm can be greater given that these people may be acting in the interests of a large number of pension scheme members or citizens.

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?

Yes. We agree a Consumer Duty should apply to activities across the retail distribution chain.

But, as mentioned above, non-FCA regulated service providers are playing an increasingly important role in facilitating the creation of demand for financial products, and in the marketing, promotion, and distribution of those products. Big tech platforms, information intermediaries and brokers, and ESG ratings providers are a case in point. It is important that firms apply the Consumer Duty in relation to the use of services provided by non-regulated third party providers where these services are instrumental in influencing how and where products are targeted.

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?

Without further explanation, it is not clear which of the two formulations proposed would best reflect the proactive focus on consumer interests and outcomes. It would have been helpful to have a number of scenarios of potential consumer detriment with an explanation of how the FCA would expect firms to respond under the two different formulations.

Nevertheless, of the two options:

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

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

the second does seem to be the stronger and clearer.

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?

We have grouped these three questions together as the FCA will have to ensure that firms adopt both *defensive* and *positive* actions if markets are to work for vulnerable consumers.

The FCA states that firms must take all reasonable steps to: avoid causing foreseeable harm, and enable customers to pursue their financial objectives. The FCA also states that firms must act in good faith toward customers. The FCA also states that it intends to embed the concept of 'reasonableness' in the Consumer Duty.

We have concerns about this. We think the inclusion of the phrase ‘reasonable steps’ particularly when combined with the phrase ‘foreseeable harm’ could undermine the effect of the requirement to act in the best interests of consumers.

The phrases ‘reasonable expectations’ and ‘causing foreseeable harm’ are likely to be open to abuse by firms and intermediaries, and allow firms and intermediaries to challenge the FCA’s efforts to apply the overarching duty and principle.

The FCA should emphasise in the rules the need for firms and intermediaries to take **defensive** action to minimise the risk of harm to consumers under particularly risky conditions. It would be more effective if the FCA adopted a much tougher approach by requiring firms to adopt the **precautionary principle** when determining whether products and practices are likely to cause harm. Firms and intermediaries, with all the huge financial and technology/ data resources at their disposal, are well placed to determine the likelihood of harm resulting. This would be all the more important when firms are using the Vulnerability Guidance to actively avoid targeting, and selling products to, vulnerable consumers.

It is important for firms to act *positively* to help consumers meet their financial objectives, as well as act defensively to avoid causing harm. This goal could be supported by firms using inclusive design principles when developing new products and services and targeting 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?

We have no firm view on whether Principles 6 and 7 and/ or the TCF Outcomes should be disapplied. But, as the FCA states, retaining these even where the duty applies would be a simple way to maintain the legal status of this material.

However, it is important that the FCA makes it clear to regulated firms and others involved in the supply chain that the new Consumer Duty introduces a higher expectation, in the round, than the existing Principles/ TCF Outcomes.

For this new Consumer Duty to make a difference to consumers, it has to help the FCA more efficiently supervise markets and enforce against breaches. It would be interesting to see legal analysis of whether retaining those Principles and TCF Outcomes would aid or undermine effective supervision and enforcement (for example, by allowing firms to claim that they had complied with Principles 6 and 7/ TCF Outcomes thereby complying with spirit of the new Consumer Duty).

If retaining the existing material helps firms interpret their responsibilities more easily then it should be kept. But, if it becomes clear that this might lead to inconsistencies and confusion, then it should be rationalised and streamlined.

But, again, it is not really possible to draw firm conclusions on these two questions without scenarios to help readers understand what difference the proposals might make.

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?

In theory, these proposals could advance the FCA’s consumer protection and competition objectives, if supported by robust rules, and meaningful outcomes.

But, as mentioned, the new Consumer Duty would have to allow for more effective regulation, supervision, and enforcement to make markets work. It also depends on how the FCA intends to use the new Consumer Duty and rules to drive out the practices identified above in Q1.

If the description of the practices the FCA includes in CP12/23 signals how the regulator intends to apply the new approach, we doubt that this will result in significant improvements for consumers, especially vulnerable consumers. The emphasis on consumer responsibility, tackling information asymmetries, and intention to use tests of reasonableness rather than more robust regulation is unlikely to make markets work. Moreover, as we set out in Q1, the FCA’s definition of what an effective market looks like appears to be quite limited.

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 matters are the steps the FCA requires firms and others to take to ensure they are acting in the best interests of consumers. These requirements should ensure firms and others treat consumers fairly and act in their interests throughout the *whole* of the firm/ customer relationship not just at the interaction point where firms are competing for custom, and consumers are making decisions as to which provider to select. We have no particular views on how this requirement to act in their interests should be labelled.

There is a potential downside, however, if the legal definition of duty of care becomes the standard for assessing whether firms are acting in consumers’ best interests. As the FCA states, the generally accepted legal meaning of a duty of care is an obligation to exercise *reasonable* care and skill when providing a product or service.

Obliging firms to exercise *reasonable* care and skill in our view would not have the same direct beneficial effect on firm behaviours as the defensive/ precautionary and positive measures we advocate if firms are to comply with the new Consumer Duty – see above. So, there is the potential for the adoption of an approach based on a legal duty of care being weaker than a Consumer Duty implemented through regulatory interventions.

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?

The FCA wants firms’ communications to consistently support consumers by enabling them to make informed decisions about financial products and services, and for consumers to be given the information they need, at the right time, and presented in a way they can understand. We very much support this goal.

It is encouraging that the FCA wants the Communication Outcome to apply at every stage of the product/service lifecycle, from marketing, to sale, and post-sale service. These proposals should improve the ability of *some* consumers to make more effective decisions. But, addressing information asymmetries is not going to be effective at ensuring firms comply with the proposed Consumer Duty. Improved communications standards should not absolve providers and intermediaries of the need to proactively act in the best interests of consumers.

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

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

The FCA states that the outcome it seeks is for products and services to be specifically designed to meet the needs of consumers, and sold to those whose needs they meet.

We support this intended outcome. But, elsewhere, when talking about the type of practices that give rise to harm, the FCA talks about:

'products and services that are not fit for purpose in delivering the benefits that consumers reasonably expect, or are not appropriate for the consumers they are being targeted at and sold to'

It is not clear what is meant by *'consumers reasonably expect'*. Reasonable expectations are, by definition, influenced by prior experience. If the market, overall, manufactures and sells products and services that are poor standard and value, then consumers will be accustomed to receiving poor value. They will not have had the opportunity to experience better products and services. Therefore, the FCA should make it clear to firms that they cannot claim they are delivering what consumers reasonably expect just because they are selling what is standard in the market.

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?

An element of poor customer service the FCA wants to address is that which hinders consumers from taking timely action to manage their financial affairs and making use of products and services, or increases their costs in doing so.

As mentioned above, it is important that the definition of customer service should place weight on the need for firms and others in the market to treat consumers fairly throughout the *whole* of the firm/ customer relationship not just at the interaction point where firms are competing for custom, and consumers are making decisions as to which provider to select.

The example given above of creditors not informing the courts that CCJs have been paid can hinder consumers from taking timely and effective action, limit access to appropriate products and/ or push up the costs unnecessarily.

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?

The FCA want firms to deliver the following outcome across retail markets - the price of products and services represents fair value for consumers.

In pursuit of this outcome, the FCA does not want to prevent firms from charging different prices to different groups of consumers which could be for a range of reasons, including different risk profiles of different groups. However, the FCA states that the firm should justify the price offered to each group in terms of fair value, with particular consideration given to vulnerable consumers and consumers with protected characteristics.

It is not quite clear how the FCA intends to use this outcome to ensure that vulnerable consumers get a fair price and good value. As the lessons from payday lending and other markets show, there is little reason to expect that competition per se will achieve this. Payday lenders used to argue that costs were so high because of the higher risk associated with the target market. But, the fact was that the poor value was embedded in the business model across the market. Competition and price discovery were inefficient mechanisms for ensuring consumers were protected and received a fair deal.

As explained elsewhere, with the FCA's proposals for the Product, Price, and Value outcomes, we are concerned that firms could justify continuing to sell high price, poor value products if these products are in line with what the market generally is offering. We do not think that, when it comes to vulnerable consumers, it is sensible to allow individual firms and the market generally (through competition and price discovery) to be the arbiter of what constitutes fair value.

So, the question is: how best to determine fair value and ensure the needs of vulnerable consumers are met? There are three complementary interventions which can be applied:

- **Price caps and product regulation:** as mentioned elsewhere, price caps are a proven mechanism. These must be a priority for the FCA. The essence of price caps is that independent agents, not market forces, determine what is the benchmark for fair value and price. This is particularly important when it comes to essential financial services.
- **Transparency:** the FCA wants firms to justify the price offered to vulnerable groups in terms of fair value. We support this intention. But, this begs the question of how will we know whether firms are doing this in a fair way? It would not be sensible to leave this to firms to oversee their own process for doing so. We would urge the FCA to prioritise supervision of these fair value assessments within firms as part of its ongoing general supervisory activity. Critically, we would urge the FCA to require firms to publish these assessments as part of annual Financial Inclusion Reports.
- **FCA reports and recommendations to Parliament and government:** we appreciate that the FCA is primarily a market regulator, not a social policy regulator. Where markets are unable to meet the needs of vulnerable consumers on fair terms, it should be primarily a matter for Parliament and government to address by ensuring availability of alternative products and services. Nevertheless, the FCA could aid this process by making formal reports and recommendations to Parliament and government when it concludes that the market is unable to meet the needs of vulnerable consumers and that social policy interventions are needed.

More generally, we are concerned about the lack of ambition the FCA shows with the Price and Value outcome and the continued reluctance to use tried and tested, necessary product interventions such as price caps.

The FCA rather optimistically states that: *'When markets function well, with competition working effectively in consumers' interests, consumers will be able to choose the product or service that represents the best value for them. Firms will be limited by the value their competitors offer and will only win business if their product or service is good value for consumers.'*

This theoretical approach to competition and market forces is very much at odds with the reality – see above, *The reality of competition*. It is unclear why the FCA continues to believe that market dynamics will ensure a fair price and value equilibrium emerges. Consumers, especially vulnerable consumers, cannot afford yet another experiment with competition as the primary means of delivering fair prices and value. We would urge the FCA to commit to using price caps as a first resort rather than a last resort.

As with the Product outcome discussed above we are unclear as to what the FCA will seek to do with this outcome. The FCA talks about: *'products and services that do not represent fair value, where the benefits consumers receive are not reasonable relative to the price they pay'*.

It is not clear what is meant by *fair value* or *reasonable* relative to the price paid. In some markets, product margins may be low, but the product still offers poor value for consumers – because the market is inefficient overall. For example, fierce competition may mean that firms have to spend significant amounts on acquiring distribution channels. Margins on products may therefore be relatively low but the end price paid by the consumer may still be very high. As we explain above in the section, *The reality of competition*, firms don't necessarily compete for consumers, they compete for distribution. But, with the FCA's approach, a firm selling a high price product may be considered to be offering a fair price and value because the rest of the market is doing so.

In other cases, there may be a significant amount of choice (so it looks as if there is competition in the market), but industry margins are high. In this case, significant value is extracted from consumers and the products on the market generally offer comparatively poor value. An example would be actively managed investment funds and certain advice services and platforms. It is genuinely difficult to see how actively managed funds (which tend to have higher prices) represents fair value if there are passive funds with similar investment objectives available. In this case, would the FCA expect asset management firms to reduce prices or not sell products, or advisers and platforms to not recommend products?

There have been examples in the past where this Price and Value outcome might have had an impact. The FCA in its ground-breaking study on the dysfunctional overdraft market⁸ found that vulnerable consumers (including those on very low incomes and with protected characteristics) were paying significantly more for overdrafts than better off counterparts - even though technological developments meant that such a high 'risk premium' was no longer justified. In our view, this was clear discrimination and exploitation. The FCA refused to take action against the banks involved. The Price and Value outcome could have been used to prevent this. But, this still leaves the question: would relying on banks interpreting what fair price and value means be the most effective way of protecting vulnerable consumers? We would argue not. A more efficient method would be for the

⁸ [FCA confirms biggest shake-up to the overdraft market for a generation | FCA](#)

FCA to instruct banks not to behave like this and/ or to use price caps which as we know have been shown to be more effective than markets policing themselves.

So, we would conclude that if this outcome is to have effect and protect consumers, the FCA will have to be more prescriptive on what fair price and value means. As mentioned, price caps are clearly a more effective way of ensuring fair prices and value than leaving it to markets in these cases.

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

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?

We would support a private right of action (PROA) to support the new Consumer Duty. This should allow for collective redress claims and class actions.

We would not expect that many consumers to use a PROA. Most ordinary consumers who need redress will continue to use FOS. But, the fact that the potential for a PROA exists would act as a powerful deterrent against firms breaching the Consumer Duty.

The existence of a PROA would not change any of our responses. The PROA should be seen as complementing the measures in the Consumer Duty, not substituting measures.

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?

See above answers to Q1 and Q11. In theory, a powerful Consumer Duty could help enhance consumer protection and *real* competition, and could advance the FCA's consumer protection and competition objectives. But, to do so, the duty needs to be supported by robust rules, and meaningful outcomes. It would have to allow for more effective regulation, supervision, and enforcement to make markets work.

As already mentioned, if the description of the practices the FCA includes in CP12/23 signals how the regulator intends to apply the new approach, we doubt that this will result in significant improvements for consumers, especially vulnerable consumers. The emphasis on consumer responsibility, tackling information asymmetries, and intention to use tests of reasonableness rather

than more robust regulation is unlikely to make markets work significantly better than is the case now. Moreover, as we set out in Q1, the FCA's definition of what an effective market looks like appears to be quite limited.

A properly supported Consumer Duty would also help improve confidence and trust in the financial services industry. It would also promote *real* competition by helping those firms who want to treat customers fairly, and allow the FCA to penalise those firms which do not. However, a recurring theme throughout our submission is that the FCA has to **make** markets work. The Consumer Duty should not be seen as another mechanism designed to create the conditions for competition to drive up standards.

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

We do not foresee any negative unintended consequences if the Consumer Duty is introduced properly. The duty needs to be supported by robust rules, and meaningful outcomes. It would have to allow for more effective regulation, supervision, and enforcement to make markets work.

No doubt, some in the industry will claim that a Consumer Duty would stifle innovation, creativity, choice, and willingness of firms to market and sell to consumers with consequences for inclusion. This would be disingenuous.

As explained above, so much innovation in financial services is not actually socially useful and is designed for the benefit of firms' business models, to meet sales targets, and to generate returns for shareholders. The Consumer Duty may well reduce the proliferation of products on the market. It may reduce the *degree* of choice in the market but improve the *quality* of choice by forcing firms to become genuinely creative and develop socially useful products that represent fair value. That would be a good outcome.

Competition cannot be relied on to drive out bad providers and products. A properly structured and enforced Consumer Duty could have this effect. This would allow more efficient, consumer focused firms the space to thrive thereby supporting inclusion.

Moreover, the new Consumer Duty (if properly implemented) represents to us a set of standards that society has the right to expect of well-run businesses. What is proposed in our response is not unreasonable. If some firms cannot trust themselves to engage with consumers on those terms and withdraw from the market, then that would be a good outcome.

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?

We are not in a position to say. We appreciate there is a significant amount of work involved. But, we would urge the FCA to start as soon as possible given the degree of detriment still existing in financial services.

However, we would point out that our proposal to require creditors to inform the courts when a CCJ has been paid could be introduced very quickly and without much disruption.

This marks the end of FIC submission