

The Consumer Duty

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The Consumer Duty

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Setting higher standards and putting consumers' needs first is essential to the FCA's strategy. As they express it, the cornerstone of this is the new Consumer Duty that will set higher expectations for the standard of care firms give consumers.

The Consumer Duty does not change the basic principle that consumers are responsible for their own decisions but it does introduce a new duty on firms to comply with the higher expectations of them under the regulatory system when dealing with retail customers, as widely defined for the purpose of the Consumer Duty provisions, and those new expectations over all new manner of activities within a firm – and are far reaching.

In this Briefing Paper, we look at the finalised terms for the new Consumer Duty and focus on the potential impact it may have on firms in the asset management sector. They will present considerable challenges to firms in implementing them, principally in the new aspects introduced in two of the required consumer outcomes but potentially in all aspects of the new provisions. Firms need urgently to plan to ensure that they implement the Duty and thereafter on an ongoing basis meet the FCA's expectations.

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What does the Duty involve?

The Consumer Duty comprises:

- a new Consumer Principle;
- the cross cutting rules – developing the FCA's expectations that apply across all areas of a firm's conduct and informing and helping firms interpret the four outcomes; and
- the four outcomes which are a suite of rules and guidance setting out more detailed expectations for a firm's conduct in four areas that represent key elements of the firm-consumer relationship.

[Policy Statement 22/9](#) of July 2022 sets out the FCA's feedback to CP21/36 and final rules made for this new Duty.

As neatly explained in Chapter 5 of the [Consultation Paper CP21/36](#), the Consumer Duty's structure is as follows:



Source: FCA CP21/36 page 33

The new Principle must be considered in the light of the wider provisions inserted by the FCA in PRIN 2A and the FCA's Guidance on the Consumer Duty which is now set out in [FG22/5 as Final non-Handbook Guidance for firms on the Consumer Duty](#), issued in July 2022.

Usually the FCA indicate what the new Consumer Duty is not:

Whilst recognising the potential benefits of a "private right of action" (PROA) for breaches of the Consumer Duty, at the moment the FCA is proposing not to provide a PROA for breaches of any part of the Consumer Duty at this time. Rather they expect firms to fully embed the Consumer Duty into the firm's culture, policies and processes and the FCA will use its regulatory tools to make sure that this happens. The possibility of a PROA will be kept under review.

They do not agree that the "label" Consumer Duty implies a legally enforceable obligation nor do they agree that the proposals would only amount to a duty of care under the Financial Services Act 2021 if combined with a PROA, and have not therefore branded the Consumer Duty as a duty of care but rather a "package of measures that has been specifically designed to tackle the harms which the FCA see in financial services markets, and their causes, more effectively."

Scope of firms and activities covered

The Consumer Duty applies to firms. It applies where a client is a retail customer or there is a distribution chain which involves a retail customer.

PRIN other than Principle 12 and PRIN 2A applies with respect to the carrying on of:

- regulated activities;
- activities that constitute dealing in investments as principal (disregarding the exclusion of Article 15 of the Regulated Activities Order – absence of holding out etc);
- ancillary activities in relation to designated investment business, home finance activity, credit-related regulated activity, insurance distribution activity and accepting deposits; and
- activities directly arising from insurance risk transformation.

Principle 12 and PRIN 2A apply to a firm's retail market business only, including in respect of existing products and closed products. Where a firm's retail market

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business involves operating in a distribution chain, Principle 12 and PRIN 2A apply only to the extent that the person is responsible in the course of that retail market business for determining or materially influencing retail customer outcomes.

As the Duty applies to firms that can determine or have material influence over retail customer outcomes, firms will need to assess the extent of a firm's responsibilities under Principle 12 which, in any one case, will turn on the substance of the firm's role in the arrangements relating to the product – see PRIN 2A.1.15G.

The underlying concept is that of reasonableness. Principle 12 and the obligations under PRIN 2A are to be interpreted in accordance with the standard that could reasonably be expected of a prudent firm carrying on the same activity in relation to the same product and taking appropriate account of the needs and characteristics of retail customers based on the needs and characteristics of retail customers in the relevant target market or of individual retail customers as the context requires (as set out in PRIN 2A.7.1R).

Retail customers encompassed

Care has been taken to review the meaning of retail customer for the purposes of the Consumer Duty provisions.

Retail customers are now defined in the FCA Glossary as follows:

- "(1) *other than in PRIN, an individual who is acting for purposes which are outside their trade, business or profession but*
- (2) *in PRIN and COCON:*
 - (a) *in relation to activities to which BCOBS applies, a banking customer or prospective banking customer;*
 - (b) *in relation to activities to which ICOBS applies, a policy holder or prospective policy holder;*
 - (c) *in relation to activities to which COBS applies, a customer who is not a professional client;*

- (d) *in relation to managing a UK UCITS, managing an AIF or establishing, operating or winding up a collective investment scheme, a person who is a unitholder, an investor in an AIF or the beneficial owner of units or shares in a fund, excluding a customer who is or would be a professional client;*
- (e) *in relation to any other activities, a customer for the purpose of that activity;*
- (f) *where a firm is involved in a distribution chain, any person who is or would be the end retail customer in that distribution chain but is not a direct client of that firm;*
- (g) *where a firm carries on activities in relation to an occupational pension scheme, any person who is not a client of the firm but who is or would be a beneficiary in relation to investments held in that occupational pension scheme."*

(Note that COCON 2.4.3R modifies this definition for the purposes of COCON. Under COCON 2.4.3R, a retail customer means, in relation to a member of the conduct rules staff of a firm, a retail customer of that firm for the purposes of PRIN.)

The effect of paragraphs 2(f) and 2(g) of the definition of retail customer set out above requires careful consideration. Under the guidance in PRIN 2.4.4G, a person may be a retail customer of a firm for the purposes of Rule 6 even though that person is not a direct client of that firm and there is no direct relationship between them. Firms will need to review carefully quite how far they need to look. Are some relationships too minor, indirect or remote? There could well be some interesting borderline cases. Also there are further specific challenges to firms and distribution chains, on which we comment further below.

There was consideration of whether high net worths should be excluded from the scope of Consumer Duty and retain flexibility and the ability to offer those category of customers more complex products suited to their requirements but, as finalised, the Consumer Duty applies to firms dealing with high net worth individuals unless that status takes conduct outside of the FCA's

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regulatory perimeter (for example, if the financial promotion restrictions in FSMA do not apply, if the financial promotion exemption provisions mean that the financial promotion restrictions in FSMA do not apply to certain promotions, communicated to certified high net worth individuals).

After consideration, the position for small and medium enterprises ("SMEs") is to maintain the approach of applying the Duty in line with the approach in the existing Source Books so, where SMEs are already protected by the FCA's Rules under a sector or a Source Book, the Duty will also apply.

Those offering products and services for professional investors only will not be subject to this new Principle but care needs to be taken in this area. It is acknowledged by the FCA that products and services are often held by both retail and non retail customers but those products and services will be included. Obviously rules on product design or assessments of value which apply, for example to UK authorised funds, will apply regardless of the type of customer. The FCA assert in the Policy Statement 22/9 that where these rules apply, complying with these rules will also satisfy these elements of the Consumer Duty – although that does need to be verified for the specific nature of the Consumer Duty obligations. For other requirements, the FCA expect firms to apply the rules in a pragmatic and proportionate manner. For example, firms might develop different communications or support services for retail and non retail customer groups. Equally though they might decide it is appropriate and proportionate to take a consistent approach for all customer groups.

Note that the definition of a retail customer for the purposes of Principle 12 and PRIN 2A includes a prospective customer (PRIN 2A.1.5G refers).

Application to firms in distribution chains

The obligation on firms that can control retail customer outcomes to take responsibility for their actions, regardless of the relationship with the customer does introduce some onerous new obligations on firms further up the manufacturing chain and of course, over recent years, product manufacturers have been increasingly disintermediated from the underlying customers.

Thankfully the challenges of modern day distribution chains are acknowledged.

The rules should be applied proportionately taking into account the firm's role in relation to the product or service, the nature of the product or service and the characteristics of consumers. In general, firms are only responsible for their own activities and would not need to oversee the actions of other firms in a distribution chain. Generally, the Duty will not apply to firms in the wholesale sector. However, the duty will apply to firms which have a material influence over

- the design or operation of retail products or services,
- distribution of retail products or services,
- preparing and approving communication that are to be issued to retail clients or
- direct contact with retail clients on behalf of another firm.

Consequently, firms who generally consider themselves outside of direct responsibilities for dealing with retail customers must still consider the implications of the Consumer Duty.

In PS 22/9, the FCA acknowledge that it would be fair for firms generally to be responsible only for their own acts and omissions. Requiring a firm to take additional responsibility for other firms in the distribution chain would not always be possible and, even where it was, would be expensive and disruptive to the market, requiring firms to attempt to oversee and control each other's work. The FCA's resulting action is to introduce a rule requiring firms to notify the FCA if they become aware that another firm in the distribution chain is not complying with the Consumer Duty – and also introduced a rule requiring a firm to notify other firms in the distribution chain if they think they have caused, or contributed to, harm to retail customers.

Additional guidance has been inserted to explain that where chains include non-UK distributors selling to non-UK customers, it is recognised by the FCA that manufacturers may not be able to gather the same amount of information as when only dealing with UK based firms.

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New Principle 12

The core of the new regulatory initiative looks very simple: a new Principle, Principle 12 called Consumer Duty is introduced which states:

"A firm must act to deliver good outcomes for retail customers."

- **applies to manufacturers and distributors**

The provisions must be considered both by manufacturers and also by distributors where a distributor distributes a product manufactured by a person to whom the rules in PRIN 2A.3 do not apply – and more generally to distribution arrangements by distributors.

Usefully there is now guidance that should support product reviews carried out at manufacturers. Distributors must, upon request, provide manufacturers with relevant sales information including where appropriate, information on the regular reviews of the product distribution arrangements (PRIN 2A.3.18). This should cure a major problem which has been encountered so far by product manufacturers, at least in theory.

- **focus on "fair value"**

Interestingly the value assessments which have already been introduced for UK authorised funds in quite a particular way will now be within a wider FCA focus on retail customer outcomes on price and value set out in PRIN 2A.4. These will require a much more general review of products and whether they provide fair value to retail customers.

The value assessment is to consider the expected total price to be paid by the retail customer or that may become due from the retail customer and any characteristics of vulnerability that retail customers in the target market display and the impact these characteristics have on the likelihood that retail customers may not receive fair value from its product.

- **retail product business**

"Product" in this instance is to be any specified investment or the provision of a service in the course of carry on a regulated activity or an ancillary activity distributed or to be distributed to retail customers and which, unless the context otherwise requires, is

not intended to refer to an individual contract.

Within PS22/9, the FCA refer to additional guidance which sets out that products and all services that are not designed for retail customers are not within the scope of the Duty where they are only marketed and approved for distribution to non-retail customers, and are not provided to another firm under an arrangement between them as part of a distribution chain for a retail product or service. Incorrectly classifying a product or service as non-retail with the aim of avoiding the Duty, and then distributing it to retail customers, would though be in breach of the Duty.

- **disapplication of Principle 6 and 7**

Principles 6 and 7 of course already exist and cover much of this territory but the idea is that Principle 12 should impose *"a higher and more exacting standard of conduct in relation to a firm's retail market business relative to what Principle 6 or 7 would have otherwise required"*.

Principle 12 also has a broader application than Principles 6 and 7 in relation to a firm's retail market business, with a greater focus on consumer protection outcomes for retail customers irrespective of whether they stand in a client relationship with the firm.

Principle 6 and 7 do not apply where Principle 12 applies but of course failure to act in accordance with the existing guidance on Principles 6 and 7, which would have amounted to a breach of those Principles is likely to breach Principle 12.

Principles 6 and 7 will continue to apply to conduct outside the scope of the Consumer Duty for example, certain SMEs and wholesale business.

In PS22/9, the FCA in their response on feedback to the Consultation acknowledge the overlaps which will result. In particular, they recognise the significant overlap between TCF outcomes and the areas covered by the Consumer Duty, in particular the four outcome rules in the Guidance explained below. Their indication is that firms should focus on complying with the Consumer Duty where it applies, rather than TCF outcomes.

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Cross Cutting Rules

What the FCA call the "cross cutting rules" are set out both for a firm and for its staff.

In PRIN 2A.2, the cross cutting obligations are set out:

- 2A.2.1R: *A firm must act in good faith towards retail customers ...*
- 2A.2.8R: *A firm must avoid causing foreseeable harm to retail customers ...*
- 2A.2.14R: *A firm must enable and support retail customers to pursue their financial objectives.*

Guidance around these rules within PRIN 2A expand upon these requirements.

In addition, there is a new section of the FCA's Code of Conduct Sourcebook ("COCON") at COCON 2.4 entitled "The Consumer Duty". This sets out three new rules:

- COCON 2.4.6R:
(1) You must act in good faith towards retail customers.
(2) Acting in good faith is a standard of conduct characterised by honesty, fair and open dealing and acting consistently with the reasonable expectations of retail customers.
- COCON 2.4.7R: *You must avoid causing foreseeable harm to retail customers.*
- COCON 2.4.8R: *You must enable and support retail customers to pursue their financial objectives.*

There is a new individual conduct rule, COCON 2.1.6: Rule 6 which cross refers to these new COCON 2.4 rules: "*You must act to deliver good outcomes for retail customers. (Note: See COCON 2.4 for what this means.*" "You" means a member of the firm's conduct rules staff.

This new conduct rule is expected to impose a higher and more exacting standard of conduct relative to the existing Rule 4 – the obligation to pay due regard to the interests of customers and treat them fairly. It is also of broader scope for retail customers, given the wider definition of retail customers for Consumer Duty purposes. In PS22/9, the FCA indicated they had considered concerns that the new individual conduct rule would create additional complexity for firms and their staff which undertake a

mix of retail and non-retail activities. However, the FCA emphasise that it is an important change to ensure that individuals at all levels in firms understand how they can act to deliver good outcomes for customers; and training that firms give to their staff should enable them to understand their obligations under the Duty and the individual conduct rules.

For further commentary, reference should be made to the FG22/5 Finalised Guidance at paragraphs 10.16-24 on implications for the Senior Managers and Certification Regime (SM&CR) implications.

Thankfully the FCA have backed off the proposal on requiring firms to "take all reasonable steps". Instead, firms should focus on acting reasonably. The entire Consumer Duty is underpinned by the concept of reasonableness. The FCA indicate the standard reflects the tortious concept of how a reasonable prudent firm would act and is one with which firms should already be familiar due to existing duties under common law. Consequently, the FCA do not think that the standard is unobtainable. (The fact though that in fact firms generally focus much more on contract and FCA regulation than on tort does not seem to be reviewed here by the FCA.)

As recorded in PS22/9, the FCA has updated its Guidance to provide further clarity on good faith. Paragraphs 5.6-5.10 of the Finalised non-Handbook Guidance FG22/5 refer. It is a standard of conduct characterised by honesty, fair and open dealing and acting consistently with the reasonable expectations of retail customers. A firm, for example, would not be acting in good faith where it fails to take into account customers' interests, for example in the way it designs the product or presents information. Seeking to exploit consumers' lack of knowledge and understanding would also be a clear sign a firm is not acting in good faith. A firm is unlikely to be able to act in good faith if it uses staff incentives, performance management or remuneration structures which are likely to cause detriment to their customers.

The non-handbook guidance sets out more detail clarifying the implications of the introduction of the cross cutting rules. Neither the requirement to act in good faith nor the Consumer Duty overall creates a fiduciary relationship (for example a requirement to act only in a client's interest and not to profit from the firm's position as fiduciary) where it does not already otherwise exist

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between the firm and the customer. The requirement for firms to take appropriate action to remedy harm does not require a firm to remedy the effect of risks inherent in a product that the firm reasonably believed that the customer was aware of, understood and accepted. (See paragraphs 5.18 and 5.19 of the Finalised Guidance.)

The four outcomes

The cross-cutting rules are to inform, and are supported by, the four outcomes which set out more detailed rules in key areas of the customer relationship.

A point made at paragraph 7.13 of CP21/36 was that the proposals do not amount to product regulation. They are not setting minimum standards for products to meet in different sectors and, unless otherwise already provided, the FCA will not be approving products before they are launched. Rather, what the FCA is seeking to do is to set high, but they think attainable, standards for what firms decide to offer.

Four outcomes are sought – on the basis set out in the new provisions in PRIN 2A 3-6:

- **the products and services outcome**

PRIN 2A.3 sets out that, for each product, a manufacturer's product approval procedures must include certain detailed elements, with the requirement to review products regularly, taking into account any event that could materially affect the potential risk to the target market.

Where any circumstances relating to the product are identified that may adversely affect retail customers, the manufacturer must take appropriate action to mitigate the situation and to prevent any further harm and, where appropriate, promptly inform other relevant persons in the distribution chain about the circumstances that led to action being taken and the remedial action taken (PRIN 2A.3.8R refers).

A requirement is inserted for testing of products appropriately, including scenario analyses where relevant.

Where there is collaboration on manufacturing a product, there must be a written agreement with respective roles and responsibilities in the product approval process – a matter of good practice in the past but now required under PRIN 2A.3.11.

A manufacturer is to select distribution channels that are appropriate for the target market and must provide adequate information to enable each distributor to comply with the rules applicable to it under PRIN 2A, which will include all appropriate information regarding the product and the product approval process from time to time to enable the distributor to comply with PRIN 2A.3.16R.

Distributors then need to maintain, operate and review product distribution arrangements in a way that avoids causing and, where that is not practical, mitigate foreseeable harm to retail customers; support the proper management of conflicts of interest; and ensure the need, characteristics and objectives of the target market are duly taken into account. Distributors must ensure that their procedures include obtaining sufficient, adequate and reliable information from the manufacturer on the relevant issues; they regularly review their distribution arrangements to ensure they are still appropriate and up to date (including verifying that it is only distributing each product to the identified target market); and, where an issue is identified, it must make appropriate amendments to the product distribution arrangements; where harm is identified, take appropriate action to mitigate the situation and prevent further harm; and promptly inform all relevant persons in the distribution chain about any action taken.

The lack of sufficient data flow has been a major issue for manufacturers when trying to comply with the existing product governance provisions. The introduction of new specific requirements aiming to improve the information flow in both directions between manufacturers and distributors is to be welcomed but it remains to be seen how, in practice, this will work through.

It is acknowledged that for investments, insurance and, from July 2022, funeral plans, they are covered by Product Intervention and Product Governance Sourcebook (PROD) provisions. Certainly investment firms currently have comprehensive product governance provisions in place covering all of the above areas.

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The FCA in Section 6 of PS22/9 confirm that the FCA agree that it would be proportionate for firms to comply with the existing rules on product governance to satisfy this outcome, as the FCA consider the existing rules meets their expectations. Consequently, the FCA have introduced new application provisions in PRIN 2A.3 to provide clarity that firms are not subject to both sets of rules.

The new provisions in PRIN 2A.3 provide clarity that firms are not subject to both sets of rules. PRIN 2A.3.2G indicates that a firm which either conducts business in relation to products that would be covered by chapters in PROD if they were manufactured after the date the relevant chapter in PROD came into force, or are subject to PROD 1.3.2R, may choose whether to apply either the processes set out in the relevant chapter of PROD that applies to the product or the processes set out in PRIN 2A.3. Note though that failings to comply with PROD in such circumstances would be taken as failings to comply with the products and services outcome.

The approach documented under the new PRIN provisions is exactly the same as that currently in force under PROD. For the moment, firms can rely on the PROD provisions as set out above. Going forwards though, this is an area to watch as the FCA may, over time, take action to remove distinctions.

- **the price and value outcome**

The FCA's emphasis on fair value is long established now. Despite the rule references to price page 45 of CP21/36 acknowledged that fair value is about more than just a price.

The FCA assert that the Consumer Duty "*aims to tackle factors that can result in unfair or poor value such as unsuitable profit features that can lead to foreseeable harm or frustrate the customer's use of the product, or poor communications and consumer support. The specific focus of the price and value outcome rules is on the relationship between the price the consumer pays to the overall benefits they can reasonably expect to obtain from a product. Value needs to be considered in the round and low prices do not always mean fair value. [The FCA] expects firms to think about price when assessing fair value but not at the expense of other factors.*"

There is though a reference back to the concern about products where there seems to be an absence of effective competition in the market place where they assert that it is less likely that products will offer fair value. High pricing could indicate that some other element is not functioning properly, e.g. transparency, simplicity of terms or ease of exit. The FCA therefore expects firms to think about price when assessing fair value but, as mentioned above, not at the expense of other factors. Notably, it is indicated that the price and value rules do not prevent firms with an innovative product that provides additional benefits to customers charging more for it. It is not the FCA's intention for the price and value outcome or any aspect of the Consumer Duty to hinder innovation.

The details, as now finalised, are set out in PRIN 2A.4.

"2A.4.1R: *For the purposes of this outcome:*

- (1) *value is the relationship between the amount paid by a retail customer for the product and the benefits they can reasonably expect to get from the product; and*
- (2) *a product provides fair value where the amount paid for the product is reasonable relative to the benefits of the product."*

A manufacturer must ensure its products provide such fair value to retail customers in the target markets for those products; and carry out a value assessment of its products and review that assessment on a regular basis appropriate to the nature and duration of the product. PRIN 2A.4.8 sets out the elements which a manufacturer's assessment of value should consider, with the following paragraphs setting out various guidance provisions in this connection.

A manufacturer's value assessment under PRIN 2A.4.8R is to include consideration at least of:

- the nature of the product or service including the benefits that will be provided or that consumers may be reasonably expected and its quality;
- any limitations that are part of the product;
- the expected total price customers will pay. (Note that the expected total price is to include for this purpose:

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- the price paid or agreed to be paid by the retail customer when entering into the contract for the product, including repayments;
- any regular charges or fees payable over the lifetime of the product, for example an annual management charge;
- any contingent fees or charges, for example administrative charges for change of address, charges for falling into arrears on a loan, or charges for transferring investments; and
- any non-financial costs a retail customer is asked or required to provide to the firm. (This reference to non-financial costs is new.)

and

- any characteristics of vulnerability that customers in the target market display and the impact these characteristics have on the likelihood that retail customers may not receive fair value for its products.

A manufacturer must ensure that firms distributing a product have all the necessary information to understand the value the product is intended to provide to a retail customer.

In its turn, the distributor must not distribute a product unless its distribution arrangements are consistent with the product providing fair value to retail customers, which involve the distributor obtaining enough information from the manufacturer (as required by PRIN 2A.4.16R) to identify various features: the benefits the product is intended to provide to a retail customer; the characteristics, objectives and needs of the target market; the interaction between the price paid by the retail customer and the extent and quality of any services provided by the distributor; and whether the impact that the distribution arrangements would result in the product ceasing to provide fair value to retail customers.

PRIN 2A.4.19R differentiates between a manufacturer considering the fair value assessment at every stage of the product approval process and a distributor considering the fair value assessment when

determining the distribution strategy for the product, and in particular where the product is to be distributed with another product whether as part of a package or not.

PS22/9 emphasises that the focus of the price and value rules is to ensure there is a reasonable relationship between the price a consumer pays for a product or service and the benefits they receive from it. Further examples have been added in the Finalised Guidance of good outcomes and behaviours the FCA expects from firms under the Duty.

Usefully, the FCA confirm that the rules are not intended to prevent cross-subsidies between products or require firms to move on to cost-plus pricing. Also, the Duty does not prevent firms from selling similar products with different prices across various brands, as long as both are fair value.

Again, interaction with existing rules has to be considered. It is confirmed that firms already subject to fair value rules will meet the price and value outcome of the Consumer Duty: notably, firms that meet the value rules in PROD 4 for non-investment insurance or COLL 6, COLL 8.5 or COLL 15.7 for asset management will meet the price and value outcome.

The FCA acknowledge that it would be unhelpful if firms took a different approach to assessing value under the Consumer Duty as IGCs and GAAs do under the COBS 19 rules.

You should not though assume that the fair value assessments are the same. The approaches in the PROD Rules differ from those now set out in PRIN. As indicated above, over time, it might be to be expected that there might be some further alignment – although not immediately.

- **the consumer understanding outcome**

Embedding the newly expressed consumer understanding outcome could cause difficulties.

The FCA's approach is that the proposals build on the existing Principle 7 by requiring firms to focus much more on consumer outcomes and understanding throughout the customer journey. In addition to ensuring communications are fair, clear and not misleading, firms need to consider their overall approach to communicating information to make sure

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they equip consumers to make effective, timely and properly informed decisions. This will also require monitoring and where appropriate testing and adapting communications so that firms can demonstrate they have acted to deliver this outcome and support consumers. It is the support element rather than information to consumers which could be tricky.

The FCA's approach is it should build on the previous "smarter consumer communications" work.

The final text in PRIN 2A.5 is very generally worded and could be applied to be quite onerous.

For example, PRIN 2A.5.7G indicates that in guidance that, in supporting the understanding of retail customers through its communications, a firm should:

- explain or present information in a logical manner;
- use plain and intelligible language and, where use of jargon or technical terms is unavoidable, explain the meaning of any jargon or technical terms as simply as possible;
- make key information prominent and easy to identify;
- avoid unnecessary disclaimers; and
- provide relevant information with an appropriate level of detail, to avoid providing too much information such that it may prevent retail customers from making effective decisions.

All of this might appear to be stating the obvious but it will, for example, preclude the despatch of lengthy standard communications with complicated and unfocused disclaimers, because that would preclude compliance with PRIN 2A.5.5R and PRIN 2A.5.6R. PRIN 2A.5.8R also indicates that in supporting the understanding of retail customers, the firm must tailor communications provided to retail customers, taking into account the characteristics of retail customers, including any characteristics of vulnerability; the complexity of the product; the communication channel(s) used; and the role of the firm, including whether the firm is providing unregulated advice or information only.

Where there is a one-to-one interaction, PRIN 2A.5.9 requires the communication to be tailored to meet the information needs of that retail customer.

Firms will be expected to consider the information needs of likely recipients of communications, informed by their assessment of the make-up of a product's target market. They should consider what they know or could reasonably be expected to know about the sophistication, financial capability and vulnerability of their customers and the nature of the communication itself. It does not involve tailoring communications to meet the needs of each individual consumer but certainly it will involve taking particular care when it comes to communicating with consumers in vulnerable circumstances, taking account of their needs.

This will cover communications whether face to face, in an office/branch, on the telephone, over email or via social media. There is a challenge as to what is expected of ongoing communication.

- Clearly where features change for a product or service, there is an important need to communicate.
- The more difficult aspect is where a consumer's circumstances might change, meaning that products and services may no longer meet needs and the extent to which firms should therefore prompt consumers to consider if the products or services continue to meet needs. This might be more relevant where there are advisory services involved but nonetheless it could be an area of concern.

The FCA acknowledges in paragraph 9.36 of CP21/36 that expectations under this outcome will be informed by the firm's role. So, if the firm is not authorised to provide advice or a customer relationship is on a non-advised basis it would not expect firms to provide advice. Nonetheless, the question will be whether communications should highlight issues which might require consumers to go and seek advice or otherwise review their circumstances. Firms will need to work out ways to monitor, test and adapt communications to support understanding and good outcomes for retail customers.

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The FCA wants firms to focus on the customers they actually serve, not a hypothetical average. The concept previously suggested by the FCA of "average customer" has been a subject of debate. In PS22/9, the FCA explain that they have amended the rules to clarify that it wants firms to ensure their communications are likely to be understood by the customers intended to receive the communication. In particular, it could have led to firms to focus on the needs of an average customer at the expense of customers in vulnerable circumstances or with diverse needs. Consequently, the FCA has amended these references to ask firms more straightforwardly to consider the needs of customers in their target market.

Interestingly, in PS22/9, the FCA acknowledge that, having left the EU and as firms embed the Duty, there may be an opportunity to simplify some of the existing disclosure requirements. If firms have evidence that prescribed disclosures are not effective in supporting consumer understanding, for example through their testing activity, they are asked to share with the FCA, and the FCA will consider if it is appropriate to make changes.

Whilst therefore it might be tempting to view this as an incremental step up from the smarter consumer communications work, it could involve a major - indeed fundamental - change of approach in retail market communications. And, over time, there may be a major reworking of key standard documentation.

- **The consumer support outcome**

Attaining the consumer support outcome is also one which could provide challenges to firms.

It focuses on what the FCA want firms to deliver and makes it clear that this outcome is not limited in relevance to after-sale service or a particular department within firms.

Under this outcome, will be the requirement that firms should ensure that retail customers do not face unreasonable barriers (including unreasonable additional costs) when they want to pursue their financial objectives. The FCA explained in CP21/13 that "unreasonable barriers" are those which frustrate the customer's use of the product or service without reasonable explanation. Thankfully the reference to "undue hindrance" used in the first

Consultation Paper has been changed to refer to "unreasonable barriers" so that it fits more with the Consumer Duty focus on the concept of reasonableness.

In general it should be as easy for a customer to exit a product as it is to enter it. The possibility of a product agreement though including contractual provisions for early termination is acknowledged with a need for those to be drawn clearly to consumer's attention.

As finalised in PRIN 2A.6.2R, a firm "*must deliver support to retail customers such that it:*

- (1) *meets the needs of retail customers, including those with characteristics of vulnerability;*
- (2) *ensures that retail customers can use their product as reasonably anticipated;*
- (3) *ensures that it includes appropriate friction in its customer journeys to mitigate the risk of harm and give retail customers sufficient opportunity to understand and assess their options, including any risks; and*
- (4) *ensures that retail customers do not face unreasonable barriers (including unreasonable additional costs) during the lifecycle of a product, such as when they want to*
 - (a) *make general enquiries or requests to the firm;*
 - (b) *amend or switch the product;*
 - (c) *transfer to a new product provider;*
 - (d) *access a benefit which the product is intended to provide;*
 - (e) *submit a claim;*
 - (f) *make a complaint; or*
 - (g) *cancel a contract, agreement or arrangement or otherwise terminate their relationship with the firm."*

Under PRIN 2A.6.3GZ, for the purposes of PRIN 2A.6.R(4)::

- (1) unreasonable barriers, are those which are likely to cause retail customers to take unreasonable additional steps to

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progress their objectives, including steps which are unreasonably onerous or time consuming; complex for a retail customer to carry out; or difficult for a retail customer to understand; and asking retail customers for unnecessary information or evidence;

- (2) where a firm has included appropriate friction in its customer journey to comply with PRIN 2A.6.2R(3), this would not amount to an unreasonable barrier; and
- (3) unreasonable additional costs includes where retail customers incur unreasonable exit fees or other charges, delays, distress or inconvenience.

The FCA's objectives

To understand the likely implications of the Consumer Duty provisions, it is perhaps helpful to take a step back and seek to understand the FCA's objectives.

It is clear that the FCA see the Consumer Duty as introducing a clear shift in approach. And the FCA indicate that they will back up the new higher standards set out in their new rules with assertive supervisory and enforcement action.

The FCA wishes to address various harms identified in various regulatory initiatives: notably, for asset managers, the Investment Platform Market Study and the MiFID II product governance review and, for funds, the Asset Management Market Study. Specifics highlighted in CP21/36 at Section 2 include:

- asset management firms leaving out certain charges, particularly to portfolio transaction costs, from their cost disclosures (MiFID II product governance);
- complex charging structures for investment platforms so comparing investment platforms was not easy (Investment Platforms Market Study);
- failures in product governance arrangements including problems with distributor firms including platform providers not providing asset managers with data to support their regular review of funds (MiFID II governance review);

- concerns about poor value (Asset Management Market Study);
- concerns on switching, driven in part by difficulties switching between unit classes and exit fees (Investment Platforms Market Study); and
- concerns about fair treatment of vulnerable customers.

The FCA's objectives were set out clearly in CP 21/13: it wants "*to bring about fairer, more consumer focused and level playing field*" in which:

- firms are consistently placing their customers' interests at the centre of their businesses
- competition is effective in driving market wide benefits, with firms competing to attract and retain customers based on high standards and customer satisfaction, and innovate in pursuit of good customer outcomes
- [the] FCA's regulation keeps up with technological changes and market developments so that consumers are protected from new and emerging harms; and firms can innovate to find new ways of serving their customers with certainty of the FCA's regulatory expectations
- firms extend their focus beyond ensuring narrow compliance with specific rules, and also focus on delivering good outcomes for customers
- firms consider the needs of their customers - including those in vulnerable circumstances - and how they behave at every stage of the product service lifecycle
- firms continuously learn from their growing focus on an awareness of what their customers experience
- in line with the FCA's work on diversity and inclusion, firms act to meet the diverse needs of their customers
- consumers get the products and services they need, which are fit for purpose, provide fair value and do not cause them harm
- consumers understand how to use their products and services and receive the support they need to do so
- consumers get prompt and appropriate redress when it is due to them with reduced misconduct ultimately reducing redress costs.

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One could certainly argue that these objectives are not new. Rather the new Consumer Duty will formalise and, as the FCA put it, "build upon" previous interventions in markets by explicitly setting a higher standard of care across all retail markets, extending rules focused on product governance and fair value. This should ensure that firms should consider the needs of their customers and focus on good customer outcomes.

The overall emphasis is on the FCA insisting that firms should need to assess and evidence the extent to which and how they are acting to deliver good outcomes.

Whilst for those in asset management the implementation of remedies pursuant to the Asset Management Market Study will in effect have given asset managers a head start in satisfying the expectations under the Consumer Duty, there is further work to be done. There is a clear real shift in approach from the FCA.

Many of the themes are familiar and the FCA acknowledge that, as mentioned above, where firms already meet existing rules in relation, for example, to product governance, these will usually meet the new requirements on which the FCA is now consulting. However, they point out the Consumer Duty overall is broader than the requirements, so firms will still need to consider if they meet all aspects of the new Consumer Duty. One particular aspect they raise is that a firm's consumer support standards must meet the new requirements.

Whilst this will involve asset managers having considerable work in implementing the Consumer Duty provisions, hopefully further positive consequences should result in due course. Commercially there should prospectively be a benefit for firms and that there should be increased consumer trust in financial services markets.

Necessary governance arrangements

In addition to understanding the FCA's objectives, it is also important to understand the FCA's expectations of the governance arrangements which they expect firms to put in place.

It is important to note that the governance arrangements, as much as the actual rules themselves, should be carefully reviewed. In Policy Statement 22/9, the FCA indicate that the duty "will require a significant shift in both culture and behaviour by many firms".

A firm's board or equivalent management body is responsible for assessing whether it is delivering good outcomes for its customers consistent with the Consumer Duty. (In the same way as was considered for the value assessments for UK authorised funds, the SM&CR regime establishes requirements.) In this instance, SM&CR will establish clear senior management responsibility for compliance with the requirements and standards of the regulatory system, and the Consumer Duty raises this standard.

The FCA is strengthening its governance and accounting requirements within the final provisions as explained in PS22/9. This is alongside strengthening the redress requirements under the Duty – requiring firms to be proactive and to take action to rectify any situation, including providing redress where appropriate. The FCA will still have the right to require restitution from firms in breach of the Duty under Section 384 of FSMA.

- **Monitoring of consumer outcomes**

The purpose of monitoring is to enable firms to identify whether there are any risks that they are not meeting the requirements of the cross cutting obligations and the retail customer outcomes and so that they are not acting to deliver good outcomes for retail customers.

The details of the monitoring arrangements will depend on the type of firm and its role in the distribution chain and the nature of the product and the target market – and the monitoring obligations should apply proportionately to a firm's role in the distribution chain.

The obligation is to monitor regularly the outcomes retail customers receive from the products the firm manufactures or distributes; the communications the firm has with retail customers; and the customer support the firm provides to retail customers (PRIN 2A.9.8 refers). Under PRIN 2A.9.9, the monitoring must enable the firm to determine at least:

- whether the retail customers are being or have been sold products that have been designed to meet their needs, characteristics and objectives;

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- whether the products that retail customers purchase provide fair value and appropriate action has been taken to address products identified as not providing fair value;
- whether retail customers are equipped with the right information to make effective, timely and properly informed decisions; and
- whether retail customers receive the support they need.

A firm must have in place processes to identify the root causes of a failure to deliver these outcomes for retail customers.

Early consideration of how relevant information regarding these points and how they can be highlighted for the board should be considered.

It is important that this process is not viewed in isolation. Also integrating issues relating to this Consumer Duty review with ongoing product review and assessment is required. The FCA indeed on page 68 of Consultation Paper 21/36 indicated various types of information which firms may wish to collect which could be used – regarding business persistence, distribution of legacy products/pricing and fees and charges; behavioural insights with consumer interactions and drop off rates; training and competence records; file reviews, checking for errors and assessing if customers have received good outcomes; customer feedback generally; the number of complaints and their root causes; compliance result reports generally; testing customer experiences; and reviewing whether processes and policies are effective – and allowing staff to feedback honestly when they think processes could be improved.

Chapter 13 of PS22/9 sets out further comments on monitoring and governance pursuant to the terms set out in CP21/36. In response to feedback, the FCA has amended the Finalised Guidance to give more information about the types of data firms could use to monitor outcomes and other factors which may impact on firms' monitoring – but none of this is exhaustive nor prescriptive. Note that during the implementation period, firms should expect the FCA to ask firms to share their approach to monitoring the duty with the FCA.

● governing body report

In CP21/36, the FCA indicated their expectation that the board or management body would consider a report from the firm assessing whether it is acting to deliver good outcomes consistent with the Consumer Duty at least annually and, before signing off the assessment, the board/governing body should agree action required to address any issues and agree any changes to future business strategy which might be required.

The FCA are not going to prescribe the format of the report to the board or equivalent management body. It is for firms to decide how they best communicate the necessary information to their board or management body – and should apply proportionately, as the FCA recognise that the level and complexity of the report may vary between firms. The FCA do though expect the first report to be considered by the board or equivalent management body within twelve months of the rules coming into force.

Under PRIN 2A.8.3-5R, the Report must set out the results of monitoring under PRIN 2A.9 and actions required as a result of the monitoring, with the governing body at least annually:

- reviewing and approving the firm's report on any outcomes being received by retail customers;
- confirming whether it is satisfied that the firm is complying with its obligations under Principle 12 and PRIN 2A;
- assessing whether the firm's future business strategy is consistent with its obligations under Principle 12 and PRIN 2A;
- agreeing:
 - any action required to address any identified risk that retail customers may not receive good outcomes;
 - any action required to address any identified instance where retail customers have not received good outcomes; and
 - any amendments to the firm's business strategy to ensure that it remains consistent with meeting the firm's obligations under Principle 12 and PRIN 2A.

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As ever, demonstrating that a suitable monitoring and board review process has been followed will be important. So firms should have records demonstrating their monitoring and board review process, and conclusions and actions, on an ongoing basis.

Chapter 13 of the Policy Statement sets out further details of expected monitoring and governance. The FCA indicate that during the implementation period, firms should expect the FCA to ask them to share the approach they are taking to monitoring the Duty with the FCA. The FCA might offer feedback on useful insights to the industry as a whole to enable firms to learn from others, improve their own approach and build best practice.

What is new in the July Policy Statement 22/9 is the introduction of new requirements that the Duty should be reflected in firms' strategies, governance, leadership and people policies, including incentives at all levels:

- firms' boards and senior management should ensure that they are embedding a culture in which good outcomes for customers is central;
- people management policies and practices, including performance management, pay and bonuses will be critical to doing so;
- firms should have appropriate oversight of customer outcomes through their systems and controls;
- risk functions should pay attention to consumer risks and they should also be a key lens for internal audit;
- senior managers will be accountable for delivering good consumer outcomes within their areas of responsibility, in line with the SM&CR Duty of Responsibility and the Conduct Rules.

The FCA will also consider evidence of individuals' understanding of and actions taken to comply with the Duty, when considering individuals for approval.

- The Guidance has been amended to make it clear that firms should have a champion at board level or equivalent governing body who, along with the Chair and CEO, ensures that the Duty is discussed regularly and raised in all relevant discussions – See Section 10 of the Final non-Handbook Guidance FG22/5.

Paragraph 10.10 of the Guidance indicates that the champion should be an Independent Non-Executive Director where possible. For larger organisations with

group structures, the FCA expect this champion to be at an appropriate level to ensure that the Duty is discussed in a meaningful way. This expectation applies reasonably, so the FCA would not necessarily expect the same level of formality in smaller firms.

Implementation challenges

There is to be a two-phase implementation period:

- From the end of July 2023, the Duty applies to all new products and services, and all existing products and services that remain on sale or open for renewal. This allows twelve months for firms to implement the new requirements for the majority of retail financial products and services.
- From the end of July 2024, the Duty will be fully in force and apply to all closed products and services.

The FCA's key expectations of firms are summarised in the extract from page 70 of the Policy Statement 22/9 which is appended to this Briefing Paper.

By the end of October 2022, the FCA expect that firms' boards (or equivalent management body) should agree implementation plans and maintain oversight of their delivery, to ensure the implementation work is sufficient to meet Consumer Duty standards. (By the end of October 2022, firms' boards or equivalent management body should have scrutinised and signed off the relevant implementation plans, and they should maintain oversight of the implementation work to ensure it remains on track and meets the standards of the Consumer Duty.)

Manufacturers should share key information with distributors three months ahead of the implementation deadline to enable all firms to comply in time, so by the end of April 2023. Firms should engage with the FCA if they considering withdrawing any products and services due to the Consumer Duty so that the FCA can identify if there is any potentially significant impact on consumers.

It is a little concerning that the FCA indicate that the implementation of the Consumer Duty will be "iterative". Note that they are considering whether and how they can give regular updates on what they are seeing and their views of it so as to provide further clarity to firms on the FCA's expectations. The FCA expect to use a number of

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channels to be used. Chapter 14 of the Policy Statement 22/9 explains the high profile campaign that the FCA plans to continue throughout the implementation period. It will be important that the FCA collect together and make these comments easily accessible so as to ensure that firms can follow the FCA's developing views. Firms are in effect asked to chase a moving target as the FCA learn more from firms' implementation and reviews of products and services which will lead the FCA to give further regular updates on what they are seeing and their views of it.

Whilst follow-up will of course be helpful, the implication of course is that there could be lack of clarity and uncertainty in the early days. The risk of resulting uncertainty is raised as a possible unintended consequence at paragraph 1.39 of Consultation Paper 21/36 and it is good that the FCA take these concerns seriously.

There is therefore a risk that the initial years will show a similar experience to that on introduction of the value assessment requirements for UK authorised funds, where

firms are required to take their own initiative on implementing the rules and then further clarity on the nature of those rules is provided by the FCA after the event.

Nonetheless, it is clear that there is a target which involves firms changing markedly the emphasis of their approach. For some firms which have already put customers at the core of their business it may be an evolution of their existing approach and governance arrangements to meet the new Consumer Duty expectations, but there is still much work to be done to make sure that the Consumer Duty is implemented properly and across the business, and demonstrated to be implemented. For others, it could be more revolutionary.

As acknowledged in PS22/9, embedding the new Consumer Duty is a complex task which expects substantive changes from firms in their approach, and it requires each and every firm's urgent attention.

Appendix: Key expectations of firms during the implementation period

Our key expectations of firms during the implementation period

1. By the end of **October 2022**, firms' boards (or equivalent management body) should have agreed their implementation plans and be able to evidence they have scrutinised and challenged the plans to ensure they are deliverable and robust to meet the new standards. Firms should expect to be asked to share implementation plans, board papers and minutes with supervisors and be challenged on their contents.
2. Manufacturers should aim to complete all the reviews necessary to meet the four outcome rules for their existing open products and services by the end of **April 2023**, so that they can:
 - share with distributors by the end of **April 2023** the information necessary for them to meet their obligations under the Duty (eg in relation to the price and value, and products and service outcomes)
 - identify where changes need to be made to their existing open products and services to meet the Duty and implement these remedies by the end of **July 2023**
3. Where firms identify serious issues causing immediate consumer harm, they should prioritise action to remedy this. This is particularly important where the harm is likely to be a breach of existing requirements (eg TCF). Significant breaches of existing rules (including the Principles for Businesses) should be reported to us, as required by SUP 15.3.11R in our Supervision sourcebook.
4. Where actions to bring products and services up to Consumer Duty standards can be completed more quickly than the implementation deadlines, firms should consider doing so, to improve outcomes for consumers more quickly.
5. In line with Principle 11 (Relations with Regulators), firms should engage with us if, as part of implementation of the Duty, they are considering withdrawing or restricting access to products or services in a way that will have a significant impact on vulnerable consumers or on overall market supply.
6. Boards (or equivalent management bodies) should maintain oversight of firm's implementation plans to ensure they remain on track, and that the work to review and improve the firm's products and services is sufficient to meet the Duty standards.
7. Firms must alert us (as required by SUP 15.3.11R) if they believe that they will not be able to complete all work necessary to be compliant with the Duty before the implementation deadlines. We expect firms to be compliant, but firms should also take a risk-based approach and prioritise the implementation work that is likely to have the biggest impact on consumer outcomes (for instance, by reviewing first the most complex or risky products and the most significant communications).
8. At the end of implementation period, boards (or equivalent management bodies) should assure themselves that their firm is complying with their obligations under the Duty, and ensure the firm has identified any potential gaps or weaknesses in their compliance and any action needed to remedy this.

Source: FCA Policy Statement 22/9 pages 70-71



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