Response to the the FCA's Consultation on A New Consumer Duty 21/13

Submission by the Transparency Task Force, July 31st 2021

About the Transparency Task Force

The Transparency Task Force is a Certified Social Enterprise, meaning that we exist to make an impact, not profit.

The mission of the Transparency Task Force is to promote ongoing reform of the financial sector, so that it serves society better. Our vision is to build a large, influential and highly respected international institution that helps to ensure consumers are treated fairly by the financial sector.

The primary beneficiaries of our work will be consumers; but the sector itself will also benefit through improved market conduct and increased trust in the services it provides.

Our objective is to carry out a broad range of activities that help to drive positive, progressive and purposeful finance reform, such as:

- Building a collaborative, campaigning community; the larger it is the more influence it can have in driving the change that is needed
- Raising awareness of issues; so that society better understands the problems that exist in the financial sector and how they can be dealt with
- Engaging with people who can make change happen; because through such dialogue we can influence thinking, policy making and market conduct

Much of our focus is on rebuilding trustworthiness and confidence in financial services. To make this possible we are busy developing a framework for finance reform which we describe as a "whole system solution for a whole-system problem" as described in our recently published book

Our response to you has been produced by a highly collaborative group of TTF volunteers, our "Response Squad," working together to build consensus, whilst always remaining true to our "North Star" question: "What is best for the consumer?"

Together, we believe that there is an urgent need to reform the regulation of the financial services sector because far too many people are exposed to the risk of economic crime, especially as only about 1% of the police budget is earmarked towards fighting fraud, even though it is now the most common of all types of crime.

Most people lack the knowledge, experience and expertise to make well-informed, balanced decisions about their finances and as such they are vulnerable to being manipulated by unethical "professionals" and outright criminals. We believe they ought to be properly protected by a robust regulatory framework.

However, there is a mountain of evidence that we do not yet have a robust regulatory framework - the reports by Dame Gloster on the FCA's handling of LC&F and Raj Parker on the FCA's handling of Connaught alone substantiate our point that there is ample scope for the FCA to up its game.

We endorse the recent Petition to Parliament by Martyn Day MP questioning the FCA's fitness for purpose and are providing administrative support to the Call for Evidence about the FCA by the All Party Parliamentary Group for Personal Banking and Fairer Financial Services, in our capacity as Secretariat to that APPG.

Given the breadth of concerns about the FCA's performance, transparency and accountability, we believe it is vital that the entire regulatory framework is strengthened and that includes through the introduction of a legally-enforceable Duty of Care, as opposed to just a Consumer Duty.

For further information about the Transparency Task Force see: http://www.transparencytaskforce.org

How Legitimate and Legal is this Consultation?

We challenge the legitimacy and legality of this consultation.

Please see these two Open Letters to the Chair of the FCA, which are included as part of this response:

- https://www.transparencytaskforce.org/wp-content/uploads/2021/06/Open-Letter-to-Charles-Randell-regarding-Re_-CP21_13_-A-new-Consumer-Duty.pdf
- https://www.transparencytaskforce.org/wp-content/uploads/2021/07/Open-Letter-to-Charles-Randell-regarding-Re_-CP21_13_-A-new-Consumer-Duty-in-response-to-his-reply-to-TTFs-Open-Letter-dated-Wednesday-June-9th-2021.pdf

Similarly, we wish the views expressed from all participants at a recent symposium we ran on this matter to also be included as part of our submission.

A video recording of the event, entitled:

"The FCA's Consultation on Consumer Duty; and why it should be a Duty of Care"

..is available to be viewed here: https://www.youtube.com/watch?v=LcO-OfJE6LY&t=3784s

Introduction

Our response to the Financial Conduct Authority's consultation paper 21/13 is different in tone and content to any other we have submitted before - and, we hope, unlike any we may feel compelled to submit in the future.

We believe that the FCA may be placing itself in breach of the law as a result of this consultation exercise, and that certain statements contained within its paper may have the effect of misleading respondents in a way that could jeopardise the integrity of their responses to such an extent that they should not be relied upon in setting policy.

These are bold claims, so it is right that we should set out the basis on which we make them.

CP21/13 exists because of an obligation placed upon the FCA in terms of section 29 of the Financial Services Act 2021 to consult on the question of whether there should be established a general rule that authorised persons should owe a duty of care to consumers. We are concerned that the consultation exercise currently being conducted by the FCA fails to address that issue and that, in consequence, the FCA is in breach of its statutory obligation.

The legal obligation

Section 29 of the 2021 Act states (*inter alia*):

> "29. FCA rules about level of care provided to consumers by authorised persons
>
> (1) The Financial Conduct Authority must carry out a public consultation about whether it should make general rules providing that authorised persons owe a duty of care to consumers.
>
> (2) The consultation must include consultation about—
>
> (a) whether the Financial Conduct Authority should make other provision in general rules about the level of care that must be provided to consumers by authorised persons, either instead of or in addition to a duty of care,
>
> (b) whether a duty of care should be owed, or other provision should apply, to all consumers or to particular classes of consumer, and

> (c) the extent to which a duty of care, or other provision, would advance the Financial Conduct Authority's consumer protection objective (see section 1C of the Financial Services and Markets Act 2000)."

It should be noted that section 29(2)(b) specifically requires there to be conducted a consultation on whether a duty of care should be owed by authorised persons to consumers.

The Consultation

The manner in which the Consultation seeks to focus the question of a general duty of care is found in Question 12, which states:

> "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?"

This question proceeds upon the narrative given at paragraphs 2.31 and 2.32. In particular, paragraph 2.31 states:

> "What constitutes a 'duty of care' may have different meanings, and our existing rules already create different duties of care for firms. 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 and this is, for example, reflected in Principle 2's requirement that a firm must conduct its business with due skill, care and diligence. In addition, section 49 of the Consumer Rights Act 2015 (CRA) implies into every contract for a trader supplying a service to a consumer a term saying that the trader must perform the service with reasonable care and skill."

Both the question and the explanation are (literally) legally incoherent and inaccurate or, at any rate, severely misleading.

The term "duty of care" has a very specific meaning in law. It is of the essence of a duty that it creates an obligation on a party (A) which is owed to another party (B), breach of which creates a legal liability on the part of A to pay damages to B, in the event that B has suffered loss as a result of the breach of duty. It is clear that what section 29(2)(b) requires the FCA to do is to consult on whether such a duty ought to be imposed. To say (as paragraph 2.1 says) that "'duty of care' may have different meanings" is, simply, wrong. It has only one meaning in law.

Of course, there may be issues as to the *standard* of the duty owed, and one can envisage several different standards which might be articulated in the creation of a new statutory duty, for example, the standard of the reasonable financial advisor, or some higher or some lower standard. In that context, it may well be an unremarkable observation that the legal standard to which a duty of care falls to be exercised is the standard of reasonable care, and that, therefore, where there exists a duty of care, the generally accepted content of that duty is "to exercise reasonable care and skill when providing a

product or service." However, where the paper is at least severely misleading is in conflating the *a priori* question of whether a legal duty should exist at all with the question of what should be the standard to which that duty should be exercised.

We are aware that not all of the rules set out in the COBS rules are actionable at the instance of persons adversely affected by a breach of those rules. Breach of some of these rules lead only to regulatory sanction at the hands of the FCA. That Parliament envisaged that there may be questions to be addressed about the setting of regulatory standards and the difference between that and the imposition of a duty of care, is focussed in section 29(2)(a) of the 2021 Act:

> "whether the Financial Conduct Authority should make other provision in general *rules* about the *level* of care that must be provided to consumers by authorised persons, *either instead of or in addition to a duty of care*," [Emphasis supplied]

It is clear that there are 2 options in 29(2)(a) and (b) – first, Rules about levels of care (breach of which might or might not be actionable) and, second, the imposition of a duty of care, which, by definition, would be actionable at the instance of a person harmed by a breach of that duty. Section 29(2)(a) and (b) read together focus the following 3 issues:

1. Should there be imposed a *duty* of care?
2. Should the FCA make general rules as to the standard of care?
3. If the answer to 2 is in the affirmative, should the rules be instead of, or in addition to, the imposition of a duty of care?

This does cover the options as to the means of creating a consumer duty.

Against that background, it might appear that question 12 could have been set only by a person having profound ignorance of both basic legal concepts and the precise statutory obligations imposed upon the FCA.

Let us analyse question 12:

1. *Do you agree that what we have proposed amounts to a duty of care?* First, the FCA is, or ought to be aware of what a duty of care is. It is not for the respondents to inform the FCA as to whether or not what it proposes is a duty of care; second, if it is not a duty of care, that the majority of respondents believe it to be does not make it so; third, if it is a duty of care, that the majority of respondents believe it not to be, does not mean that it is not; fourth if it is a duty of care, then the FCA has proposed such a duty *without asking the question specifically mandated by section 29(2)(b)* as to whether there should be such a duty; fifth, if it is not a duty of care, then the FCA has proposed that there should not be a duty of care *without asking the question specifically mandated by section 29(2)(b)* as to whether there should be such a duty.

2. *If not, what further measures would be needed?* This fails to address the issue of needed for what purpose? If needed to create a legally enforceable duty of care, then there may be repeated the same observations made at 1 above. If needed to create a

satisfactory consumer duty, then it may be that the question is an inept and incoherent attempt to ask the "instead of or in addition to a duty of care" question.

4. *Do you think it should be labelled as a duty of care?* This question betrays profound ignorance. What something is labelled is not determinative of what it is. Changing the label does not change the reality. Whether or not the proposal amounts to a proposal to impose a duty of care is a matter of substance, not labelling.

5. *Might there be upsides or downsides in doing so?* There are, indeed, possible upsides and possible downsides in imposing a duty of care – that is an issue which falls within the scope of section 29(2)(b). However, the question does not seek opinions on the upsides and downsides of creating a duty of care, only opinions on the upsides and the downsides of *labelling* the FCA proposal as a duty of care.

The proposed Consumer Duty

What the FCA has, in fact, proposed is a regulatory solution. To quote paragraph 3.1:

> "To achieve the outcomes we are seeking, we are proposing that the Consumer Duty will be comprised of a Consumer Principle, along with a set of rules and guidance that amplify the Principle and set out the detail of our expectations. This aims to ensure that the Duty is understandable, flexible and adaptable."

This proposal is, however, not a proposal to create a duty of care as that phrase is correctly understood. In effect, what the FCA has done is to propose "general rules about the level of care that must be provided to consumers by authorised persons... instead of a duty of care".

It is entitled to make such a proposal, but it is also statutorily obliged to consult on whether there should be imposed a duty of care. Therefore, it would have been consistent with the statutory obligation for the FCA to set out what it sees as the merits and demerits of a duty of care, the merits and demerits of a regulatory solution, then to set out its proposed solution and seek comment. Such a process would include a question "do you agree that there should not be imposed a duty of care?". That question is simply not asked, nor is the issue adequately explained. Instead, the FCA asks only "should our solution be *labelled* a duty of care?"

The reality is that it is not a duty of care:

- Principle 2 does not create a duty of care because breach of the FCA's Principles for Business does not give rise to a right of private action by parties injured by a breach thereof;

- Section 49 of the Consumer Rights Act 2015 does not create a general duty of care such as envisaged in section 29, because , while it does give rise to a right of private action where a consumer is a party to a contract, that right does not extend to a consumer who is not a party to a contract but where the service provider could reasonably have foreseen that a consumer

would be harmed by its actions. To give just one example, should a firm authorised by the FCA approve a promotion for an unauthorised firm which then uses it to attract customers, if those consumers subsequently discover that the promotion was misleading, the CRA does not give them a right of action against the firm that approved it (because there is no contractual relationship between the consumers and the authorised firm), whereas a duty of care founded in tort (or, in Scotland, delict) would give such a right of action. This is the very issue which was addressed and solved by the articulation in the law of tort and of delict of the neighbourhood principle – that liability is not restricted to an injured party with whom there is a contractual relationship, but extends to all those who might reasonably be foreseen as likely to be injured by one's actions - as long ago as 1932 in Donoghue v Stevenson [1932] AC 562 (as it happens, in a case which involved a consumer, though the principle is of universal application);

- The major advantage which consumers would derive from the imposition of a duty of care is that it would give to consumers who have suffered reasonably foreseeable loss as a result of the actions or inactions of authorised persons the right to sue them for damages, whereas under the FCA's proposed Consumer Duty consumers would have no right to sue and any hopes they may have of receiving compensation would continue to be dependent on the FCA either imposing a restitution order under the powers conferred upon it by the Financial Services and Markets Act 2000 or in negotiating a voluntary redress, both of which are vanishingly rare occurrences

Given the number of lawyers employed in senior positions at the FCA, it should be readily apparent to the organisation that it has failed clearly and explicitly to ask the questions which it has a statutory duty to ask, that it has fundamentally misunderstood or misrepresented what a duty of care is, that it has stated *ex cathedra* an erroneous and misleading statement as to what a duty of care is (which most, if not all respondents will take on trust) and, in consequence, consumer respondents, few if any of whom are likely to be legally qualified, will fail to appreciate that one of the options upon which Parliament mandated consultation – namely whether, in principle, there should be imposed a duty of care – has simply been left off the table, potentially leading respondents into acceptance (with or without suggested fine tuning) of the FCA proposals which, from the perspective of consumers is materially less beneficial than the imposition of a duty of care. It may be that even sophisticated respondents, (unless they engage in their own forensic dissection of the consultation paper in light of the legislation) will fall into the like error.

Whilst CP21/13 does contain a section (5) on a possible private right of action in relation to the Principles, this is not the same thing as a general duty of care and, indeed, it is positioned as a separate matter to duty of care. It is made clear (paragraph 1.18) that there will be further consultation on any private right of action in a subsequent paper. Given that such a future paper will be published with the feedback to CP21/13, due by 31 December 2021, it is, in any event, unlikely that consultation on this will take place within the legally mandated time frame. Further, given the apparent misdirection of respondents over the distinction between a duty of care as that is properly understood and the proposed Consumer Duty, it may well be that the outcome of CP21/13 will be that there is little or no demand for the former. That may be likely to lead, in turn, to an apparent lack of support for the private right of action in relation to the Principles.

In short: the law requires the FCA to consult on whether a duty of care towards consumers should be imposed upon authorised persons. Quite simply, the FCA fails, in the consultation, to put that option on the table. In consequence, the consultation is fundamentally flawed.

The need for a genuine duty of care

Since the consultation document was published, we have been in correspondence with the FCA's Chair, Charles Randell, an Oxford law graduate and former Partner at Slaughter and May and therefore someone we believe ought to be as alert to the shortcomings identified above as we are. He rejects the commonly accepted legal definition of the term "duty of care" and states that, for the FCA, it means nothing more than "a positive obligation on a person to ensure that their conduct meets a set standard."

Randell claims that while CP21/13 includes questions on "whether or not a private right of action for damages should attach to the duty... there would be alternative ways of enforcing such a duty. These include not only voluntary redress or a restitution order, but also our routine supervision and enforcement activities. And individuals have the ability to seek compensation by referring complaints to the Financial Ombudsman Service, which would have regard to the duty in its decisions."

We have no problem with regulatory remedies being in place *in addition to* a private right of action, we believe they cannot be a substitute for it. We hold this view for two reasons: first, as we have explained above, breach of a duty of care is by definition actionable; and second, the alternatives listed by Randell have consistently been shown to be unsatisfactory.

We are particularly concerned about whether these options represent viable means by which (i) consumers are compensated for the costs incurred as a result of breaches of the FCA's Principles for Business (since it seems that the FCA's proposed new Consumer Duty would amount to a package of revisions to the wording of the same) and (ii) authorised persons can be prevented from causing further consumer detriment and others considering such behaviour can be deterred.

While the Financial Ombudsman Service may provide a route to redress for some consumers, it also has a number of serious shortcomings. These include:

- The upper limits on the sums it can award, which render it unsuited to larger claims;
- The requirement for each affected consumer to submit a separate complaint, which may deter complex claims or vulnerable and unsophisticated complainants;
- The expectation that the complainant should be a 'customer' of the party complained about;
- Time limits on bringing complaints, especially the requirement to do so within six months of receiving a firm's response to a complaint;
- Information asymmetries, in particular the absence of legally enforceable disclosure requirements and penalties for breach, or for misleading the Ombudsman;
- Well-publicised problems with the operational and leadership competence of the Service, including whistleblower evidence of poor training and bias against consumers reported by Dispatches, delays, redundancies (despite a huge case backlog), the CEO's departure, a report finding it unfit for purpose and a dire Trustpilot rating;

- Numerous conflicts of interest arising from its links with the FCA, including concerns that Richard Lloyd, commissioned to write a report into the whistleblower allegations against the Ombudsman publicised by Dispatches had links to the Service, produced a whitewash then was given a job at the FCA and that the FCA's Nausicaa Delfas is to become the Interim Chief Executive Officer and Chief Ombudsman[1]

The FCA's restitution orders provide a theoretical path to redress, especially in cases where a large number of consumers have suffered detriment sufficient to prompt an Enforcement investigation by the FCA. However, in the six calendar years 2015 to 2020 inclusive, the FCA has imposed only two restitution orders on authorised firms, of which only one was ever paid[2], and none on individuals. There have also been two voluntary redress schemes negotiated by the FCA in the same timeframe[3]. Given the number of instances of alleged consumer detriment that took place in the same period, these numbers are clearly very disappointing, and the expectation must therefore be that most consumers cannot expect to be compensated as a result of schemes imposed or negotiated by the regulator.

Finally, we believe there is an unacceptable paucity of Enforcement action by the FCA, resulting in consumers being poorly protected from past wrongdoers and from those who might be tempted by regulatory inaction to do them harm. Our evidence for this assertion includes:

- In the seven years from 2013 to 2019 inclusive, the FCA prosecuted zero firms or individuals for issuing or approving misleading financial promotions; it also removed permissions from zero firms and issued just three sets of fines for such offences during that timeframe;
- Challenged on this by Shaun Bailey MP at a Work and Pensions Committee evidence session in connection with its Pension Scams inquiry, the FCA's Enforcement Director Mark Steward claimed (Q242) that: "There have been a very large number of prosecutions involving scams and unauthorised business where the charge that has been laid is, in fact, a fraud charge rather than a charge under the Financial Services and Markets Act, where the instigation of the scam is, in fact, a misleading financial promotion of some kind or other. Every investment fraud involves a misleading representation being made at the outset." In fact, the FCA obtained only 18 such convictions in the six years from 2015 to 2020, only one of them in the past two years;
- When pressed on the subject by Dame Angela Eagle MP at a recent Treasury Committee evidence session on economic crime, Steward's position changed (Q177): "It is commonly thought that we have a significant role to play in prosecuting fraud. In fact, the Financial Services and Markets Act does not contain any provision that gives us a function in relation to fraud, and the offences that we are authorised to prosecute do not include any offences under the Fraud

[1] Delfas has spent 22 years at the FCA and its predecessor, the Financial Services Authority. She led the Complex Events Team heavily criticised in the Independent Review of the regulator's handling of Connaught and which also played the central role in the Interest Rate Hedging Product redress scheme, John Swift's Independent Review into the FCA's conduct in which is due to be published 'in summer 2021' and has performed a great many other senor roles across Enforcement, Supervision and Policy and twice as Chief Operating Officer, rising the potential that many of the cases that might be brought to the ombudsman are also ones in which there might be grounds for suspecting regulatory failure, whether by Delfas, her direct reports or her close colleagues

[2] £11,876,000 against Vanquis Bank Limited (paid); £203,007 against Blue Gate Capital Limited (in default) (source: FOI8339)

[3] £156,905,000 from Vanquis Bank Limited as part of the same action mentioned above; 'up to £66m' (actual sum paid about £57m) from Capita Financial Managers Limited (source: FOI8339)

Act. For a start, one of the things that create expectations around what we can do is, in fact, something that we are not authorised by the statute to do."

- It is our understanding that while the FCA has no *statutory objective* to bring prosecutions under the Fraud Act, it is *permitted* to do so; and it clearly *does* bring such prosecutions, just not very many. Moreover, it also has a statutory duty (1C) to secure "an appropriate degree of protection for consumers." It is difficult to see how this objective is secured when so few wrongdoers are being prosecuted and contradictory excuses being given for the failure to achieve more.

Set against this background of limited and imperfect routes to redress for consumers and a shortfall in regulatory consequences for wrongdoers, we believe that a *genuine* duty of care on the part of the firms and individuals authorised by the FCA to consumers would permanently shift the balance of power in favour of the latter, and away from bad actors in the industry and a regulator that some consumers whether rightly or wrongly feel too often fails to take their side.

For the first time, consumers would have a viable way to bypass the FCA, in the shape of the right to sue those who owe them a duty of care but fail to deliver on it. This right would exist whether or not the consumer was a customer of the firm or individual in question. For instance, if an Independent Financial Adviser approved a promotion for an unauthorised firm, a consumer invested in the product, it turned out not to be as described and the consumer lost money, he or she would be able to sue the IFA.

The introduction of a *genuine* duty of care would create a compelling economic incentive for the more widespread availability of litigation funding in the sector, driving down litigation costs, relieving individual consumers of this burden and raising the cost of misconduct for bad actors (the respondents would pick up not only the greater costs of compensating consumers but also significant legal costs on both sides). This development may be particularly valuable to vulnerable and economically excluded consumers, who are unlikely to be in a position to pursue self-funded legal options (for instance, judicial review) aimed at pursuing a complacent or captured regulator to exercise its statutory powers in their interests.

The parties to a duty of care

Section 29(2)(a) of the Financial Services Act 2021 requires the FCA to consult on whether *authorised persons*[4] should owe a duty of care to *consumers*[5]. Under FSMA, and in UK law generally, 'person' covers individuals, partnerships and incorporated entities. It is therefore clear that Parliament intends this consultation and the resulting rules to apply to approved persons, i.e. individuals authorised by the FCA to perform regulated activities and hold control functions in firms, and not just to authorised businesses. Likewise it is clear that it intends any duty of care to be owed to all *consumers*, and not just *customers* or *clients*, i.e. those bound directly in a contractual relationship to a specific firm.

We have noticed a number of points in the FCA's discussion document in which it uses the terms *firms*, *customers* and *clients* where it should have used *authorised persons* and *consumers*. For the FCA to fulfil

[4] As defined in Section 31 of the Financial Services and Markets Act 2000
[5] As defined in Section 1G of the same Act

its statutory obligations under the 2021 Act, we believe that these errors or misdirections should be corrected in any reissued version of the consultation; and if the FCA is determined to press on regardless, it is essential that the duty of care that emerges is owed as specified in the Act and not as described in many of the formulations in the discussion paper.

Implications

Given our concerns about the scope of this consultation, the misdirections within it and the changes in terminology adopted, we ask three uncomfortable questions:

- What legitimate reason might there conceivably be for the FCA, whose first statutory duty is consumer protection, to seek to deprive consumers of a powerful protection Parliament wants them to have, namely to be owed a duty of care, something that is *intrinsically and by definition actionable by that individual*?
- What motive might it have for misdirecting them about the true meaning of that term in law?
- Why would such a body, as has happened in the consultation paper, seeked to parlay an obligation on *authorised persons* (which includes individuals approved to perform specified functions) into *firms* and *consumers* (which includes people affected by the actions of approved persons but who may not have a contractual relationship) into *clients* or *customers*? Are these changes innocent drafting errors or signs of a captured regulator seeking to protect those it should be policing?

We hope that politicians will see this episode for what it is: a desperate if artfully executed bait-and-switch exercise on the FCA's part, intended to deceive consumers and benefit the industry and even specific individuals within it, and hence a powerful signal that the regulator must be either replaced or subject to extensive reform, under consumer oversight[6]. We are particularly concerned at the impact of this misdirection on vulnerable consumers and excluded and underrepresented groups, who may be less well equipped to spot and challenge the tactic.

We also hope that the FCA will be mindful of concerns expressed by us, other consumer advocates and Parliamentarians about this consultation, and of the risk of losing a very high profile judicial review, and will accordingly accede to our request to reissue the discussion paper, this time wholly compliant with section 29 of the Financial Services Act 2021.

As a result, our response document concentrates on what we see as the defects of this consultation exercise and the discussion paper and sets out what we believe a duty of care is and why it is required, rather than engaging in granular detail with the FCA's proposals for a new Consumer Duty.

Wider pattern of behaviour

[6] See for instance our response to HM Treasury's Future Regulatory Framework review, and especially Appendix III, our proposal to establish an oversight board, the Financial Regulator's Supervisory Council

Sadly, this example of the FCA acting to undermine consumer interests is not an isolated one. In July 2020 the regulator published a consultation into proposed changes to its Complaints Scheme. This happened in long-overdue response to persistent demands from the then Complaints Commissioner, Antony Townsend, to resolve a flaw in the Scheme as drafted, namely that he could not recommend the payment of material sums in compensation in situations in which consumers lost money as a result of regulatory failure. The consultation was open for less than the recommended three months - despite the conjunction of Covid and summer holidays, both of which might have argued for additional time. We also believe no press release was issued, though the FCA claims otherwise. While the FCA claims to have consulted users of the Scheme and consumer groups, we question whether this was done in good faith: the only 'Scheme users' notified were those who had submitted complaints to the FCA but not yet escalated them to the Commissioner, and the only consumer groups notified were approached in the latter half of the consultation period and were members of the FCA's opaque and self-selected 'consumer network'.

Far from resolving the identified shortcomings of the existing Scheme, the FCA's proposals sought to entrench the imbalance between consumers and itself, handing the organisation the right to decide unilaterally to disregard certain complaints and formally establishing upper financial limits for any compensation. The consultation period was extended following intervention from the Treasury Committee, as was the timescale for publication of the resulting policy statement[7]. At the time of writing, the chasm between Parliament's intent, which is that there should not be any constraint on the quantum of compensation payable nor on the circumstances giving rise to such redress, and the Scheme, remains unremedied.

Finally in December 2020, when the FCA published Raj Parker's Independent Review into regulatory failures in relation to The Connaught Income Fund Series 1, the FCA implied that the victims had recovered all their invested capital and, the following day, falsely stated that they had been placed "as closely as possible back in the position they would have been in if they had never invested in the Fund." It has subsequently used these claims to justify not compensating the victims. Its Chief Executive Officer, Nikhil Rathi, has refused to withdraw or amend the statements; the matter is now subject to a formal complaint, and may go to judicial review.

We see this pattern of behaviour as evidence that the regulator that all too often fails to perform its statutory functions to a satisfactory standard, is attempting to conceal the extent of the problem from politicians and is culturally disinclined to prioritise consumer interests.

We have advanced proposals to remedy these problems in a number of consultation responses, not least our paper responding to Part II of HM Treasury's Future Regulatory Framework Review. We draw readers' attention in particular to the proposal (Appendix III) for the creation of a supervisory board, the Financial Regulator's Supervisory Council. This measure would, we believe, transform the operational competence, culture and transparency of the FCA, by making it fully accountable to a body that genuinely represents the consumer interests that should be at the forefront of everything it does.

[7] Now due 'towards the end of Q2 2021'

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?

Consumer harms

The specific harm that a duty of care is required to address is that consumers cannot sue authorised persons, and the FCA has limited scope to impose collective redress schemes, where the authorised persons have caused reasonably foreseeable harms to consumers but there exists either no contractual relationship between the two or no specific breach of a contract.

We provide five illustrations of this point below:

1. Authorised firm A approves a financial promotion for unauthorised firm B to use in the marketing of a collective investment scheme. Consumer C invests in that scheme. Unfortunately the scheme does not operate as described in the promotion and C loses money as a result. Currently C cannot sue A as C is not a customer of A
2. Authorised firm D is appointed as Asset Manager and authorised firm E is appointed as Authorised Corporate Director to fund F. Consumer G invests in that fund. Unfortunately D departs materially from the promised investment strategy and breaches advertised limits on leverage and the proportion of illiquid assets and E fails to prevent this happening. Currently G cannot sue D or E as G is not a customer of D or E;
3. Authorised firm H operates in the wealth management sector. It uses morally questionable high-pressure sales techniques and adviser incentives to sign up clients, combined with onerous exit penalties to retain them. These behaviours clearly fall short of its obligation to treat customers fairly enshrined in Principle 6. Since the Principles do not amount to a duty of care, consumer I, a customer of H, cannot sue it to recover any fees misleadingly obtained, or imposed as a condition of termination of an arrangement;
4. Authorised firm J, a bank, provides a business account to firm K, which may or may not be authorised. It operates a fraudulent consumer investment scheme. Know Your Client and Anti Money Laundering checks were not performed, or were performed inadequately. A number of red flags about how the account is operated are ignored. Consumer L loses money through investing in the scheme operated by firm K. Currently L cannot sue J to recover his or her losses as he or she is not a customer of J;

5. Authorised firm M, a building society, operates a number of savings accounts offering attractive interest rates for an initial, promotional period and thereafter, derisory rates of interest. It fails to notify customers when the promotional periods end and consequently customer N, who is more vulnerable than others, receives interest that falls far short of market norms. Consumer N cannot claim redress for forfeit interest because there is no breach of the contract between M and N, nor has M misrepresented the rates paid to N

All of these hypothetical scenarios are loosely based on actual cases brought to the attention Transparency Task Force. In none of them did the FCA deal with consumer losses by means of a restitution order, nor did the Ombudsman recommend a payout. And in none of the above scenarios would the introduction of the FCA's proposed 'new Consumer Duty' be of any practical help to those affected unless the FCA chose to go down the restitution order route - something we know it seldom does. But in all of five, a duty of care, which would by definition give rise to a private right of action (PROA), would enable the victims to litigate; and in those where there is a group of similarly-affected consumers, the FCA could also create a Section 404 redress scheme.

Wider context

The wider context surrounding this consultation is that there have been a great many other consultations over the years (14, we believe) into whether there should be a duty of care requirement imposed on authorised parties to consumers. Not one of them has resulted in the outcome desired by and plainly in the interests of the public. As a result, an amendment was inserted into the Financial Services Bill 2021 by a group of peers, which became Section 29 of the Act, requiring the FCA to consult again on the topic, publish its analysis of responses by 1 January 2022 and introduce rules 'having regard to that analysis' by 1 August 2022.

The FCA's and its predecessor the FSA's history of resistance to the introduction of such a duty in our view betrays an institutional bias against the proposed measure, which we fear has resulted in the misdirection about the meaning of a duty of care and the drafting flaws in this consultation set out in our Introduction.

We suspect that the FCA is determined to bring forward rules that reflect its intended perversion of a duty of care - a 'new Consumer Duty' that amounts to nothing more than a re-wording of the Principles of Business, enforceable by it alone and not giving rise to a private right of action. We are setting out these concerns publicly in our consultation response in order to help create an evidence trail that may be helpful in any future judicial review.

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?

They are harmless enough, as detail and colour of how a duty of care might be worded. But they are not in themselves a duty of care.

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

We have concerns relating to the way in which the word 'clients' is being used.

Would this term explicitly include consumers who are not clients of the party causing the harm? We think either that there should be wording explicitly explaining that this is the case or, perhaps better, the term 'consumers' should be used, and defined as in Section 1G of Part 1A Chapter 1 of the Financial Services Act 2012. The FCA discussion paper implies that its use of terms such as customer and client should be held to mean 'consumer' as defined above, but we are concerned that this qualification might be overlooked in any final rules; for this reason, we prefer the use of the term 'consumer' throughout.

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

We are comfortable with these aspects of the document.

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?

The FCA proposes two alternative wordings for its Consumer Principle:

- Option 1: 'A firm must act to deliver good outcomes for retail clients'
- Option 2: 'A firm must act in the best interests of retail clients'

Our first concern relates to the use of the term 'firm'. We believe that a duty of care should be owed by all those authorised by the FCA - individuals as well as firms. The case for this is three-fold:

- Section 29 of the Financial Services Act 2021 states that the FCA 'must carry out a public consultation about whether it should make general rules providing that authorised *persons* owe a duty of care to consumers' (our italics); the use of the word persons, as opposed to firms, makes it clear that Parliament's intention is that the resultant duty of care applies also to the individuals approved by the FCA;
- It would, for the first time, create a material alignment of economic interests between individuals approved by the FCA to perform control functions in authorised firms and consumers, by allowing the latter to sue the former should they fail to prevent reasonably foreseeable harms. The benefits of this alignment would extend beyond consumers to shareholders in authorised firms, where these differ from those managing those businesses: for the first time, managers responsible for harming consumers would also be at risk for conduct costs, instead of just the (often wholly innocent) shareholders;
- It would also bypass the FCA's reluctance to use the Senior Managers and Certification Regime to punish managers guilty of misconduct, creating a conduit by which consumers could hold them to account by imposing on them some of the financial costs of their wrongdoing

Our second concern, as explained earlier and it is worth repeating here, relates to the use of the word 'clients.' Would this term explicitly include consumers who are not clients of the party causing the harm? We think either that there should be wording explicitly explaining that this is the case or, perhaps better, the term 'consumers' should be used, and defined as in Section 1G of Part 1A Chapter 1 of the Financial Services Act 2012. The FCA discussion paper implies that its use of terms such as customer and client should be held to mean 'consumer' as defined above, but we are concerned that this qualification might be overlooked in any final rules; for this reason, we prefer the use of the term 'consumer' throughout.

(There may also be a case for a duty of care to be owed to small and medium-sized businesses, as part of a wider move to bring SME banking within the regulatory parameter. We are broadly supportive of such a move, but it would clearly have to take place within a much wider package of regulatory changes, so we are not advocating a standalone measure in respect of duty of care).

Having dealt with these two definitional issues, we are left with the job of comparing the relative merits of 'deliver good outcomes' and 'act in best interests.' Outcomes are more important than intentions, but best is better than good. A formulation that brings together 'best' and 'outcomes' may be preferable to the two options offered.

However, firms may reasonably argue that it is in the nature of financial services that there is usually a gap, sometimes many years long, between the actions of a firm and their outcomes for consumers. A firm may *intend* the best outcome, but circumstances may intervene such that it is not achieved. It may therefore be pragmatic to insert a test of *reasonable foreseeability*: 'a firm must deliver the best reasonably foreseeable outcome for consumers.'

The FCA claims that the generally accepted definition of a duty of care is "to exercise reasonable care and skill when providing a product or service." The concept of a reasonableness test is well established in

common law and allows a court (or the FCA, in the case of any regulatory action) to consider whether or not a reasonable person, aware of the duty of care and consequences of breaching it, would have acted as the firm did, given the information in existence at that time. So we have no objection to the inclusion of such phrasing, but not in isolation. The legal definition includes a focus on *reasonably foreseeable harms*; so while conduct can be considered, outcomes matter too.

A further advantage to a reversion to a traditional phrasing for a duty of care is that it would head off a threatened judicial review from the financial services industry, which is concerned that a 'best interests' test could be unreasonable given that service providers may not always have sufficient information about consumers' interests.

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?

We think the cross-cutting rules are actually quite well drafted. The focus on avoidance of *foreseeable harm*, the presence of *reasonableness* and *good faith* tests and a requirement to consider *different consumers'* [note: not 'customers', since the use of that word could result in there being no duty of care to consumers who are not contractually defined as customers] *needs, expectations and vulnerabilities* all feel like sensible flesh on the bones of what a duty of care should constitute.

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

Regarding vulnerabilities, the harsh reality is of course that all consumers are vulnerable in the face of asymmetries of information and power between firms and consumers. Defining 'vulnerability' runs the risk of focusing firms' attention on box ticking; and perhaps the FCA's too.

Our concern, within the context of the consultation paper as drafted, is that the FCA may be painting a superficially attractive picture of how financial services firms might in future be expected to behave, while at the same time seeking to deprive consumers of a right of private action - a key feature of a duty of care. So these measures should form part of a duty of care; they cannot be a substitute for one.

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?

They should be disapplied where the new duty is demonstrably stronger; but as explained elsewhere a legally enforceable Duty of Care with an integral Private Right of Action is actually a much better solution overall.

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?

As we set out in our introduction, we believe that the legitimate purpose of this consultation, in keeping with Section 29 of the Financial Services Act 2021, would be to seek views on what standard or nature of duty of care should be owed to consumers by authorised parties.

In that context, one wholly viable option would be to use the existing Principles for Business as the start point for any such duty. The word 'firm' would have to be replaced with 'authorised party', and 'customers' and 'clients' replaced with 'consumers' in order to comply with Section 29 of the Financial Services Act 2021. Thereafter, the only change required would be to revoke the rules created by the FCA that use Section 138(3) of the Financial Services and Markets Act 2000 to disapply the provisions of that Section that render breaches of FCA rules actionable by private persons.

Given this point, we should be alert to the risk of falling for the FCA's bait-and-switch: devoting a lot of attention to impressive-sounding but legally insignificant changes to the wording of the Principles is many times less important than the binary question of whether the Principles, and FCA rules underpinning them, are or are not civilly actionable.

Our only observations in this section therefore are that the Principles should define what standard and nature of duty of care should be owed, the rules should reflect the Principles, and breach of the rules in respect of reasonably foreseeable harm to consumers should constitute breach of the duty of care, which should be civilly actionable (additional regulatory remedies would be a bonus, but are no substitute for a private right of action).

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?

Not at all unless they are enforced rigorously. History tells us that the FCA is generally weak when it comes to enforcement. FCA does not generally enforce against principles unless rules have also been broken.

And the FCA knows how rarely the SMCR has been used as intended.

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?

If the FCA's 'new Consumer Duty' amounts to nothing more than a package of largely rhetorical changes to the Principles, backed by some detailed changes to the Handbook, then they would do little to advance the FCA's consumer protection and competition objectives. This is because the FCA so seldom achieves material redress for consumers using its restitution powers and so rarely removes wrongdoers from the Register, or from society, using its enforcement powers.

The only sense in which a non-actionable (by consumers) Consumer Duty would be of any value at all is at the margins: consumers might, in theory, be able to subject decisions by the FCA not to act to judicial review, and could be helped in this by tougher-sounding Principles and rules. However, there is an intrinsic information asymmetry between the FCA and consumers that renders such legal challenges difficult if not impossible: the FCA may claim it *intends* to act, or that there are some *obstacles* to it doing so, but that it is constrained in its ability to do so by Section 348 of the Financial Services and Markets Act, legal and professional privilege or some other legal formulation. This is particularly true of vulnerable consumers and economically and otherwise excluded groups, for whom the prospect of funding and overseeing a judicial review to force the FCA to intervene in their interests is a distant dream.

If there is any doubt that there is a need for a genuine (and hence intrinsically actionable by consumers) duty of care, we refer you to the recent announcement by the FCA that it has found evidence of breaches of the Principles by Lloyds Banking Group's general insurance division. The headline announcement claims that measures to avoid price gouging of existing customers on renewal is expected to save consumers £4.2bn over a 10year period. LBG has a 12.29 percent market share, suggesting a consumer loss of around £465m during the nine years covered by the Final Notice. That's just the principal; with interest (the Financial Ombudsman's default rate is eight percent a year) the total consumer detriment could be close to £1bn. The FCA fined LBG £90m and has allowed the firm to provide just £13.7m in compensation to affected consumers.

Under a duty of care (but not under the new Consumer Duty, unless accompanied by a private right of action), consumers would be empowered to sue LBG for their losses. Had such a right already been in place, the bank may well have agreed to compensate them in full, to avoid both sides' litigation costs and the reputational harm and enforcement consequences that would have followed the exposure in open

court of the full details of its misconduct. Even if it had chosen to contest the matter, and even if claims management companies or litigation funders took 35-40 percent of sums awarded, consumers would be many times better off under a duty of care than they would be if still deprived of it.
The ‘new Consumer Duty’ as drafted is not a duty of care. This statement is a fact of law, not a matter of opinion. As we set out in our introduction (‘Let us analyse question 12’), calling a regulatory solution a legal one does not make it so. The ‘new Consumer Duty’ must not be labelled a duty of care, and any attempt to do so is likely to lead to the FCA further damaging its already tarnished reputation among Parliamentarians and consumer advocates.

For the FCA to comply with its obligations under the 2021 Act it should immediately reissue this consultation, having first put on notice potential respondents, with a legally watertight and non-contentious definition of a duty of care at its core, combined with sensible questions about the standard and nature of that duty of care. It would be legitimate to explore at the margins whether a duty of care is needed or desirable and to probe what alternatives might be considered, but the central focus of the consultation should be on the assumption that there will be a duty of care and thus on consideration of the detail of how it might be defined and applied.

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

This matter falls into the 'vulnerability' trap again. Firms should communicate with all consumers (as defined in FSMA) as if they were vulnerable. Vulnerability is often not a fixed characteristic and firms cannot know whether it exists or not in any consumer or group of consumers at any one time.

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

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

Fine words but they need to be backed up with much stronger enforcement. The FCA needs to be prepared to ban a whole raft of products that don't achieve this outcome.

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

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

This section doesn't say anything about complaints. Firms should ensure their complaints processes represent good customer service and not kick complaints to the Financial Ombudsman Service which is an additional hurdle for consumers. Firms should also analyse complaints to identify and remedy root causes.

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

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

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

The FCA should be wary of being too prescriptive in drafting any duty of care. The 'motherhood and apple pie' statements in this section of the discussion document are harmless enough, provided they are not enshrined in the Principles or Handbook as exhaustive and therefore potentially exclusive. It should be for a court to define whether a duty of care has been breached with reference to a reasonableness test; it should not be constrained by detailed expositions by the FCA.

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?

As we have explained in our introduction and referred to at numerous points in this response paper, we see a duty of care and the FCA's proposals for a Consumer Duty as two different things: in short, we're

calling the regulator out on its bait and switch. A duty of care by definition includes a PROA. The proposed Consumer Duty does not; the FCA has included a handful of questions on whether there should additionally be a PROA, but you have done so in bad faith. Its definition of a duty of care is incorrect in law and, given the number of lawyers at the FCA, we must assume this is a wilful misdirection rather than an innocent error.

A PROA is a hugely valuable right for consumers, and it worries us deeply that a statutory body whose first objective is to protect consumers should be seeking to deprive them of this route to financial recourse. Set against a backdrop of institutional inactivity in the application of its restitution and enforcement powers, it is difficult to see this action as anything other than regulatory capture expressed as an intention to protect the industry from consumers, when the opposite is what the FCA should be doing.

We have no objection to a duty of care that *also* provides the FCA with options to utilise its restitution and enforcement powers, or to the FCA calling the latter a 'new Consumer Duty', provided it also disapplies the provisions of Section 138D of FSMA that currently bar consumers from enjoying a PROA in respect of breaches.

We also note that doing so would hand the FCA an additional power, which if utilised would be beneficial to consumers, namely the right to impose industry-wide redress schemes under Section 404 of FSMA. It is the absence of such a power that was used to justify the regulator's decision not to institute a collective redress scheme for the 'mis-selling'[8] of Payment Protection Insurance ('PPI'). While some £50bn was paid by banks to consumers in redress, the majority of such payments were made through claims management firms, which kept typically between 25 and 40 percent of awards, and there was no proactive endeavour to identify and contact the victims; the total amount of unremedied consumer detriment is therefore unknown, but may have been double the sum paid out.

A further advantage to the duty of care is that, since it would give rise to a civil liability to consumers arising through regulatory breach, should a firm go into default that liability would pass to the Financial Services Compensation Scheme. This is important, since it means that awards would be underwritten, at least up to the FSCS limits (there may be a case for raising the upper threshold).

We note the section of the discussion paper listing potential unintended consequences of the introduction of a PROA; we see some as invalid and others as desirable. Taking the key ones in turn:

- Making firms [and approved persons, as previously explained] averse to behaving in ways that avoid them causing consumer detriment that could give rise to litigation is wholly desirable, and should be counted as one of the most compelling arguments for a duty of care (and thus a PROA);
- We do not believe that this would "discourage firms from developing innovative products or services, which could restrict consumer choice and competition." If a product is intrinsically harmful to all consumers, we welcome the creation of an economic deterrent to its creation; if it

[8] We'd argue 'fraud by misrepresentation or material omission'

is suitable to only some consumers, we welcome the creation of an economic deterrent to it being offered to consumers for whom it is unsuitable;

- There is an intrinsic inequality of arms between most consumers and most authorised firms and individuals, and litigation funders take on only cases in which there is a very high probability of success. For these reasons, we do not believe there is a material risk of authorised persons facing litigation costs in circumstances in which they are innocent; we see it as desirable that they should face such costs where they have done wrong. Moreover, if the duty of care is constructed in such a way that there are also regulatory remedies (such as the right to impose restitution orders) for breach, the FCA can spare approved persons these litigation costs by choosing to deal with the need to remedy consumer losses by means of industry-wide or specific redress schemes;
- Professional indemnity insurers underwrite policies based on a detailed understanding of the risks presented by the firm, individuals and activities. It is reasonable to assume that a PROA would result in PI costs soaring for those authorised persons whose conduct history or specific activities suggest a high risk that claims will successfully be brought and smaller or no rises for those who conduct themselves in a prudent and honest manner. This is a wholly desirable outcome: a PROA is a market-based solution for imposing the negative externalities of misconduct on the perpetrators, and PI premiums are an excellent *ex ante* proxy for those costs. If a few risk-takers are priced out of the industry by prohibitive PI cover, that is a public good;
- Where a duty of care has been breached in respect of just one consumer, it is true that the risk of adverse costs might deter that person from bringing a claim. It may be that if the duty of care is reflected in changes to the Principles and Handbook that the Financial Ombudsman might be able to deal with claims that it currently does not handle (for instance where the consumer is not a client of the firm); also, it is always an option to revise the remit and rules of the Ombudsman to address the shortcomings identified in our introduction. Where a material group of consumers is affected by the same or a similar breach of the duty of care, it is likely that litigation funders will move into the sector and ATE[9] insurance be obtained to protect against counterparty costs. Moreover, in the scenario outlined, we would hope that the reputational desire to protect consumers from either the risk of adverse costs or the need to sacrifice a high proportion of payouts to a litigation funder would place pressure on the FCA to make more use of its restitution and S404 powers, reducing the need for litigation;
- The concerns about claims management companies are legitimate, but overstated. The overriding point is that the FCA can and should deal with cases in which a material number of consumers have lost money through breach of a duty of care by authorised persons using its own powers, obviating the need for consumers to contract with CMCs. The presence of CMCs in the sector is evidence of regulatory failure, and the FCA should be shamed by it into action;
- We agree that the courts would play a significant role in the interpretation of a duty of care; we see this as an intended and desirable outcome. Currently, the FCA is the principal arbiter of whether breaches of the Principles and COBS have taken place, and we are concerned that it is excessively cautious, risk-averse and institutionally included to take a pro-industry perspective in doing so. The introduction of a duty of care, which would by definition include a PROA, would

[9] After The Event

provide consumers with an alternative, independent and transparent environment in which to pursue financial remedies for poor treatment by authorised parties;

- We recognise that a period of time would be needed for the industry to adapt to the introduction of a duty of care, and we also accept that there is a need to consult on the details of its implementation between December 2021 and August 2022, by which time the new rules must be published (though the 2021 Act does not require immediate implementation);
- We also recognise that the discussion paper proposes (2.37f) that any changes would not apply retrospectively. If this is to be the case, there needs to be a fair means of dealing with the many legacy cases in which consumers have lost money through harms caused by authorised persons and the FCA has failed to secure redress through the exercise of its existing powers. In many such cases, regulatory failure predates and thereby enabled the harms, or ran consecutively with them and therefore allowed them to continue for longer and on a larger scale than would otherwise have been the case. There is therefore be a need for a legislative route to be provided for the payment of such redress, whether by amending the Compensation (London Capital & Finance plc and Fraud Compensation Fund) Bill[10], establishing a Royal Commission similar to that held in Australia or by some other means;
- One other means that Government should consider is whether to remove the FCA's general exemption from civil liability[11], perhaps combined with a waiver of the Limitation Act so no legacy cases would be time-barred. It could also go further and explicitly place on the FCA a duty of care to consumers, corresponding to that which we argue is required for authorised persons

A genuine duty of care owed by authorised persons to consumers would bring an additional benefit not mentioned in the consultation paper. One of the key problems identified in Dame Elizabeth Gloster's Independent Review into the FCA's regulation of London Capital & Finance plc is the 'halo effect' whereby a firm authorised by the FCA may benefit from an enhanced degree of trust from consumers even when offering products that are themselves unregulated. Further, this lack of clarity about the regulatory perimeter can also lead to misunderstandings about whether such products are or are not eligible for compensation from the Financial Services Compensation Scheme.

Under the duty of care as specified in Section 29 of the 2021 Act, a duty would be owed by dint of one party being an authorised person and the other being a consumer; it would not be dependent on whether the products being discussed or purchased are regulated or not. Thus in return for the regulatory halo, authorised firms would owe a concomitant duty to consumers, which feels reasonable and proportionate. And since a genuine duty of care brings with it a PROA, which creates a civil liability, the FSCS would stand behind such a firm in default.

Looking at responses to previous consultations on a potential duty of care, we note that consumer advocates tend to favour it, while noting that its value is as a fall-back should regulatory action not result in redress being secured without the need for litigation; in contrast, many industry representatives,

[10] LCF Bill evidence session notes.pdf

[11] Subject to two very narrow carve-outs (bad faith and breach of human rights); we do not believe either has successfully been exploited in court

including some ‘AstroTurf’ organisations and academics funded by the same, tend to oppose it. We believe that this is in itself evidence that a duty of care would be beneficial to consumers, and we hope that the FCA, whose statutory duties include consumer protection and the promotion of competition, will not weigh equally the responses received from these opposing stakeholder groups.

Finally, we also hope that the FCA does not seek to exploit any evidence that consumers and consumer advocates responding to this consultation exercise accept its claims that its proposed ‘new Consumer Duty’ amounts to a duty of care or that a PROA is not required to attempt to impose on the public anything less than the genuine, civilly actionable duty of care envisaged by Parliament. Any such responses will be the result of misdirection, in our opinion wilful, by the FCA, and should not be taken to constitute a shift of opinion on the part of those stakeholder groups.

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?

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?

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?

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

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

Most of these questions relate to firms (23, 24, 27) or have already been covered (26, much of 25). To the last of these we would add just one observation: consumers, the honest majority of authorised persons and the United Kingdom as a whole all benefit from the country's financial services industry producing high-quality products and services that inspire confidence among those who might use them.

When consumers decline to interact with the industry because of fears of being treated badly, a deadweight loss is created: consumers fail to benefit from services that suit their needs; capital is misallocated to unduly risk-averse, unproductive assets (such as cash, or under-occupied family homes); those consumers may become burdens on the state, having declined to make provision for adverse events or old age; the industry is deprived of legitimate profit opportunities and the Treasury from the opportunity to tax both consumers and firms on the upsides of those activities.

In recent years, there have been far too many instances of consumers being treated badly by some in the industry, and of them being expected to shoulder some or all of the resulting losses. Rebuilding confidence in the sector will require the introduction of bold measures designed to make both the industry and its regulator more accountable to consumers, both in governance terms and financially. The creation of a duty of care, which by definition includes a PROA, is a necessary step along this path.

Final thoughts

We remain very concerned about the legitimacy of this consultation exercise for the reasons explained and we also remain very concerned that a golden opportunity to provide the best possible framework for robust consumer protection by way of a legally-enforceable Duty of Care, as required by Parliament, is being missed.