A new Consumer Duty

Feedback to CP21/13 and further consultation

https://www.fca.org.uk/publications/consultation-papers/cp21-36-new-consumer-duty-feedback-cp21-13-further-consultation

Response by the Transparency Task Force, February 15th 2022

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

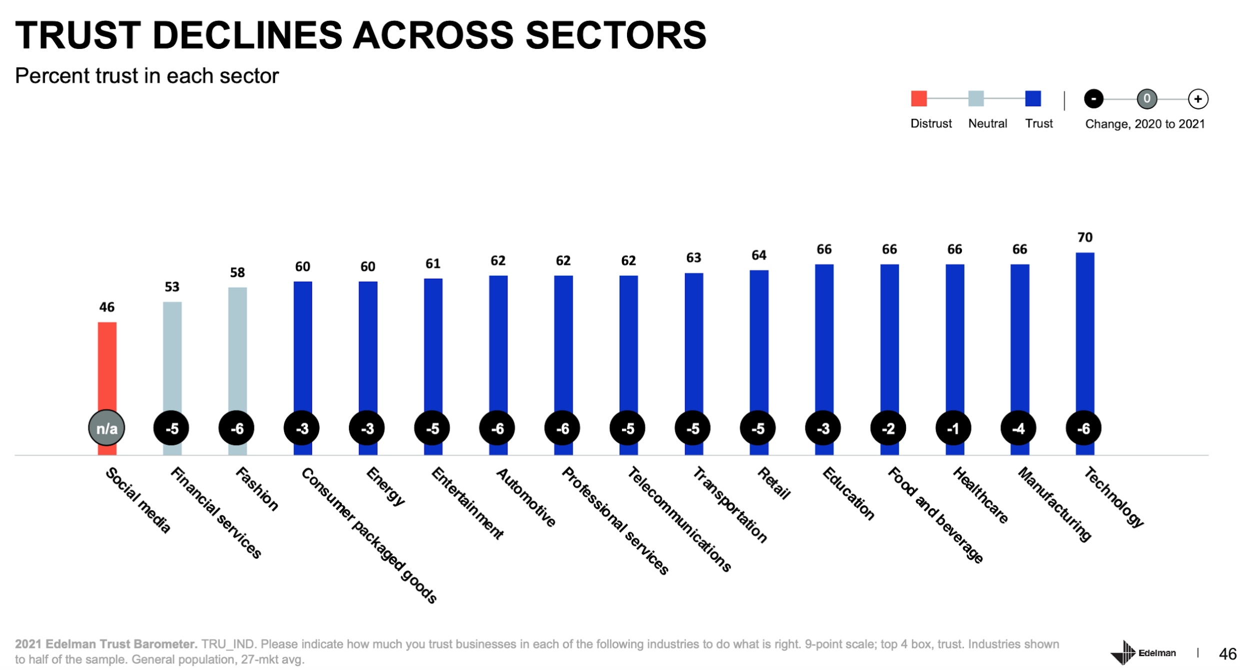
Our response to you has been produced by a highly collaborative group of TTF volunteers, our "Response Squad," working together to build consensus, whilst always remaining true to our "North Star" question: "What is best for the consumer?" For further information about the Transparency Task Force see: http://www.transparencytaskforce.org

This response is all non-confidential. Please note that all comments in this response are part of the response, and should be considered.

Some of this response is contained in answers to FCA's specific questions below, but the parts of the response not shown as direct answers to questions are equally part of this response, and for consideration by HM Treasury.

As always, context is key

We believe that there is cause for concern about the reputational integrity of the financial services sector, in most parts of the world. There is ample evidence to suggest that society is distrusting of financial services. The highly credible 2021 Edelman Trust Barometer in Financial Services shows it to be the second most distrusted industry; second only to social media.



Given the fundamental need for the financial sector to be trusted for it to function successfully, it should be a great concern for the sector's market participants, trade bodies, professional associations and regulators that it is a sector that society does not trust.

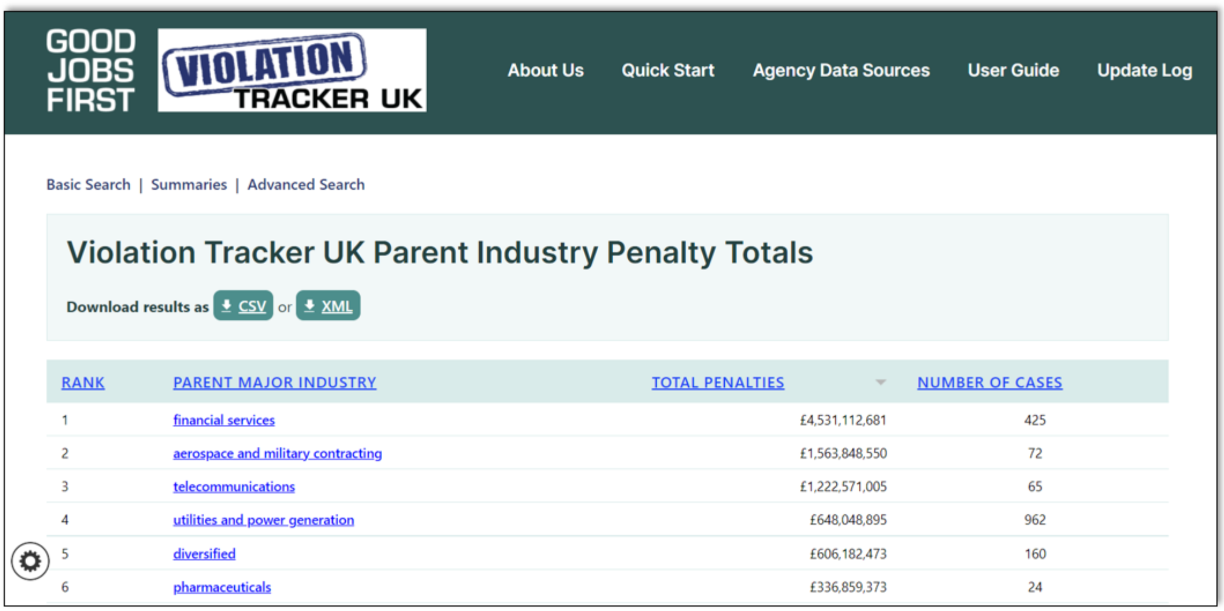
It is easy to understand why the financial sector is distrusted; in fact the evidence suggests that people *should* distrust it. Consider for example the overall conduct of the financial industry in the UK compared to other industries when it comes to the level of violations.

The best source for such data is the recently launched Violation Tracker UK. In the interests of transparency we should point out that Transparency Task is very closely connected with Violation Tracker UK; and proudly so. For example, we Chair its UK Advisory Board.

Violation Tracker UK holds data about corporate infringements in 46 sectors. What does the data in Violation Tracker UK show about the UK's financial services sector? It shows that the conduct of the sector is so bad that if you add up all the infringements by all the other 45 industries it equates to roughly the same as the financial sector on its own.

That is a truly alarming reality; so much so that repairing the reputational integrity of the sector should be Priority #1 for all stakeholders that truly care for the wellbeing of the sector and the society it is meant to serve.

The screenshot below shows the top of a chart that all financial sector stakeholders in the UK should be ashamed that the financial sector is at the top of:



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Violation Tracker UK Parent Industry Penalty Totals

Download results as CSV or XML

RANK	PARENT MAJOR INDUSTRY	TOTAL PENALTIES	NUMBER OF CASES
1	financial services	£4,531,112,681	425
2	aerospace and military contracting	£1,563,848,550	72
3	telecommunications	£1,222,571,005	65
4	utilities and power generation	£648,048,895	962
5	diversified	£606,182,473	160
6	pharmaceuticals	£336,859,373	24

To view the chart in full, click here.

Furthermore, it is impossible to ignore the obvious question: how can it be, that despite the UK's financial sector being such a systemically important part of our economy and our international reputation, that we are tolerating such poor stewardship of it by its conduct regulator?

That question becomes even more poignant when you look deeper into the data held within Violation Tracker UK and consider the obvious pattern of recidivism that exists within the sector. The screenshot below gives a feel for the scale and nature of recidivism within the sector:

Basic Search | Summaries | Advanced Search

Violation Tracker UK Parent Industry Summary Page

Parent Industry: financial services
Penalty Total since 2010: £4,531,112,681
Number of Cases: 425

Note: The totals include only those entries matched to a parent company. The industry designation is the primary one for the parent's operations overall.

TOP 10 PARENT COMPANIES	TOTAL PENALTY	NUMBER OF CASES
Barclays	£515,651,961	20
Lloyds Banking Group	£467,402,170	35
UBS	£460,563,400	5
NatWest Group PLC	£436,370,276	24
JPMorgan Chase	£396,172,200	4
Deutsche Bank	£395,435,024	4

To see that data in full, click here and when viewing it, scroll down and see the obvious pattern of the same organisations committing the same offences over and over again. Perhaps this suggests that there is a culture within the sector that sees the fines imposed on it as a cost of doing business. Perhaps this hard evidence also calls into question the grotesque lack of effectiveness of the FCA in ensuring the sector behaves properly and that it succeeds in its objective to maintain the integrity of the sector and provide an appropriate level of consumer protection.

That validity of that line of thought becomes even more obvious when you drill down to the next level of infringement data, and look at the violations of particular organisations. For example, examine the infringements by Barclays, Lloyds Banking Group and Nat West; and ask yourself if it would be prudent to do anything that might encourage even more misconduct; or to miss any opportunities to raise the standards of ethics and integrity in the sector.

For the avoidance of any doubt the answer is “No”!

All this makes it perfectly clear that any notion of reforms that might lead to even worse conduct by the sector should be distinguished immediately as a reckless line of thought; and that applies also to failing to introduce reforms that would have a positive impact. The reputation of the financial sector and wealth it generates matter far too much for any reforms to be allowed to gamble with it, or for meaningful reform opportunities to be missed. Rather, we would respectfully suggest that resource and energy would be better spent examining what needs to happen for the FCA, and thus the delivery of financial regulation in the UK, to become fit for purpose. We believe that turning the UK's financial services industry into the world's best-regulated is the best way to restore consumer confidence in it and the UK, and to persuade governments and regulators overseas that the ghosts of the Global Financial Crisis have finally been laid to rest and that the City can be trusted to trade freely across borders.

We are so concerned by the poor performance of the FCA that we are having to spend a huge proportion of our very limited resources on helping to try to fix it, as these slides about our Plans and Priorities for 2022 show - look in particular at the section about the evidence published thus far from the APPG on Personal Banking and Fairer Financial Services' Call for Evidence about the FCA - see here.

Please therefore be mindful of these well-founded concerns when reading the rest of this response as we believe very strongly that this consultation suggests the FCA may once again miss an opportunity to introduce a meaningful reform that would be a major step forward in helping to achieve its objectives to ensure the market operates with integrity and provides consumers with an appropriate degree of protection.

Q1: Do you have any comments on the proposed scope of the Consumer Duty?

In our response to CP21/13 we stated (pp 2-11), based on input from Counsel, that the legal definition of a duty of care is long-established and uncontested, and that the proposed Consumer Duty, unless accompanied by a private right of action (PRoA) could not be considered to amount to a duty of care. We also suggested that the FCA might have misdirected respondents by providing an incorrect definition of a duty of care and falsely claiming that its proposed Consumer Duty could be considered to be one.

Nothing we have seen in CP21/36 leads us to doubt the accuracy of our position. If, as seems currently to be the plan, the FCA proceeds to implement the Consumer Duty without a PRoA attached to it, we anticipate that the decision will be challenged, whether in Parliament - which may reasonably consider the FCA to be in breach of its statutory obligation to consult on a duty of care - the courts, or both.

At a time when the FCA is under intense pressure to raise its game and demonstrate an enhanced capacity to deliver against its statutory and operational objectives, we hope its embattled leadership team will reflect on the reputational harms that would result from being seen to resist a requirement placed on it by elected representatives to provide consumers with a valuable right which the regulator's own consultation has shown they overwhelmingly want and that the industry would prefer it to bury. A decision to do so looks like, and probably is, born of a desire to protect the industry rather than consumers - a classic sign of regulatory capture. If the FCA, under new leadership, wants to signal that it now sides unambiguously with consumers, it should deliver a PRoA, in full, and to the satisfaction of consumer groups and the interests of consumers they speak for.

We recognise that some industry participants are concerned that they might not succeed in implementing the Consumer Duty fully at the outset, and that the simultaneous introduction of a PRoA could leave them exposed to sizable liabilities. We gently remind them, and the FCA, that in the absence of a PRoA, those costs will continue to be borne by consumers. But we offer a pragmatic and implementable way forward; a compromise proposal (in our answer to Q15 and thereafter) that the FCA commits to a timescale for the introduction of a PRoA a material period of time *after* the inception date of the Consumer Duty, to give the industry time to become fully compliant.

While we would like to see the provision of financial services to SMEs that do not meet the definition of retail clients fully within the regulatory perimeter, we accept that this is a separate debate. Given the current Handbook, we accept the proposed scope limitations in respect of such firms. We are pleased to see that prospective customers will be within scope: this opens up the theoretical possibility that the FCA might enforce against, for example, a misleading financial promotion, based on the fact that it is misleading, without having to wait for it to cause identifiable harm to a specific consumer.

Q2: Do you have any comments on the proposed application of the Consumer Duty through the distribution chain, and on the related draft rules and non-Handbook guidance?

We are concerned about how the principle set out in par 3.22 - that each firm is liable only for its own activities - might work in practice. One of the many advantages of a genuine duty of care is that an obligation to avoid causing a reasonably foreseeable harm can bring within scope harms caused by another party brought into play by the first, where that harm could have been or was foreseen. So if firm A introduces a consumer or subcontracts work to firm B, A may be liable for harms suffered by the consumer at the hands of B, if it failed to conduct satisfactory due diligence into B, knew that B was defective or dishonest or failed to provide such support as was necessary for B to perform to the consumer's reasonable expectations.

This is not merely a theoretical risk. To take a recent example, in November 2017 the FCA was able to extract 'up to £66m' (in reality, about £57m) of voluntary redress from Capita Financial Managers Limited (now Link Fund Solutions Limited) for the benefit of investors in The Connaught Income Fund Series 1. The fund contained only around £22m when the firm resigned its role as Operator and handed over to Blue Gate Capital Limited. Capita withheld from Blue Gate concerns it held that led it to believe the Fund had not been described accurately in the Information Memorandum and that it was not operating as it should. Deprived of these insights, Blue Gate agreed to take on the responsibility and continued to market and operate the product much as before. During its tenure as Operator the Fund attracted a further £85m of client monies. Blue Gate was a micro-business with grossly inadequate professional liability insurance, so was unable to remedy the loss. The November 2017 settlement between the FCA and Capita resulted in the latter paying a proportion of the losses, with the balance shouldered by consumers.

There is a risk that if the Consumer Duty operates as described in par 3.22, a firm that finds itself in a similar position to Capita in the future would be able to argue successfully that its responsibility should be limited to the harms caused while it was in place, rather than those that were reasonably foreseeable at the time it terminated its involvement and which later crystallised during the tenure of another firm.

It may be that the proposed Consumer Duty can be worded in a way that clarifies that an authorised person may be held responsible for *all* its actions and inactions, including those which could also be held to be the responsibility of a third party, where it is responsible for that party's involvement and was negligent or dishonest in bringing it on board. But we must reiterate that the introduction of a genuine duty of care would resolve this matter unambiguously in consumers' favour: the reasonably foreseeable harm test, or some variant thereof, clearly captures the acts and omissions of third parties where they ought to have been (or were) foreseen by the first party.

We welcome the 'material influence' test (par 3.26) and the intention that authorised firms that approve promotions for unauthorised firms will be within scope (par 3.33), though wonder how these points will interact with the problematic par 3.22. To take one hypothetical example, if authorised firm A approves a financial promotion to be issued by unauthorised firm B, what happens if, over time, the product ceases to be as described and a consumer suffers loss as a result? Firm A may argue that it believed assurances from B that it would operate the product as described in the promotion and that any failure to do so is B's responsibility; B will simply point to the fact that it is not authorised and thus is outside the regulatory perimeter so not covered by the Consumer Duty.

Under a genuine duty of care, A would be aware that approving a promotion for a third party is an extremely risky activity that could result in it being liable should the product not operate or perform as described, so would be likely to refuse to perform that role unless given such extensive influence and oversight of B's operation of the product that it could be sure that such a liability would not arise. If the FCA is determined to introduce something that falls short of a duty of care, it should at least resolve these ambiguities.

Our view is simple: if part of the value chain is within the regulatory perimeter, the Consumer Duty must apply to the authorised person/s and to them alone, unless the product contains prominent and unambiguous warnings to the contrary. So a full-service bank can operate in wholesale markets without risk of being held to the Consumer Duty in respect of that activity, where the counterparties aren't consumers or where it is clear to clients that the products are not covered. But if an authorised firm places itself in a value chain with an unauthorised one and the end client is a consumer, it must appreciate that it is on the hook if things go wrong.

Q3: Do you have any comments on the proposed application of the Consumer Duty to existing products and services, and on the related draft rules and non-Handbook guidance?

We welcome the obligation on firms to comply with the Consumer Duty on a forward-looking basis for customers with existing contracts (par 4.5). However, we wonder whether this is undermined by the wording of par 4.9, which states that the FCA 'would not expect firms to give up any contractual rights they had a firm expectation of being able to enjoy' and that they might instead 'be able to make changes to the contract that do not alter their vested rights to remuneration'.

Taking, for example, the plight of 'mortgage prisoners', is the FCA saying that the Four Outcomes it expects to see - especially that relating to price and value - and the Overarching, Cross-Cutting Rules (such as avoiding foreseeable harms, including the exploitation of a vulnerability such as an inability to switch lender, and acting in good faith, for instance by not imposing a Standard Variable Rate (SVR) that is out of step with those charged by active lenders) trump the lender's contractual right to continue charging whatever interest rate it chooses, knowing that there are barriers, often insurmountable, to the customer switching? Par 4.8 implies that the Cross-Cutting rules *will* apply even to closed-book products, but there is a lack of clarity about the Four Outcomes and a potential conflict with the remuneration protection clause (par 4.9).

The Mortgage Prisoners' Review has set up an expectation (par 8.3) that the Consumer Duty should result in 'good outcomes for all borrowers' and that the FCA will take 'action as necessary to address harms we find'; however, it is unclear from CP21/36 whether borrowers can expect only the 'motherhood and apple pie' commitments in par 4.9 or genuine action to end and remedy unfair treatment implied by par 4.5 and also in the Mortgage Prisoners' Review.

While we make these observations in the context of mortgage prisoners, they self-evidently apply across the sector. Examples include, but are not limited to:

- Life insurance: new-policy premiums have fallen during the lifetimes of many policies, especially for people with specific protected characteristics (for instance, gay men and haemophiliacs);
- Open-ended investment companies such as unit trusts, especially overt and closet trackers, endowment policies and pension schemes: management fees charged by legacy products may be egregiously high relative to modern products offering similar or superior features and performance;
- Life, health, private medical and pet insurance: deterrent customer pricing of pre-existing conditions when quoting for new business may trap consumers with legacy providers;
- Wealth management: egregious switching penalties contractually imposed by firms such as St. James' Place plc that deter consumers exiting in favour of better-value providers or self-management

We believe the Consumer Duty must specify unambiguously that existing contracts are within scope.

Q4: Are there any obstacles that would prevent firms from following our proposed approach to applying the Consumer Duty to existing products and services?

We can see nothing that would *prevent them doing so*; we can see compelling reasons why they would *prefer not to have to bother*. And we fear that they will present the latter as the former, and that the FCA will yield to their representations.

Clearly, a combination of price-walking, sludge policies, switching costs, information asymmetries and recent market developments (for instance, online price aggregators, low-cost platforms and ETFs) mean that legacy products, closed-book ones especially, tend to be more profitable for providers - and inferior value for consumers - than new ones. The question is whether and if so how far the FCA will go in challenging the industry's extraction of rents from those long-established customers, many of whom will have vulnerabilities.

Furthermore, we are very concerned that under the proposals, in effect, almost all of the previous bad behaviour is going to be allowed to escape prosecution, persecution and redress. The rules as drafted will only impact new sales and not on old, existing products which were sold prior to the date of implementation of the new rules.

Q5: Do you have any comments on the proposed Consumer Principle and the related draft rules and non-Handbook guidance?

We believe that this is another area in which the FCA risks placing itself in breach of the obligations created by Section 29 of the Financial Services Act 2021, in order to protect authorised persons and deprive consumers of rights Parliament wants them to have. As we explained (Q5) in our response to CP21/13:

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 - authorised persons 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 underline); 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.

For these reasons, we believe that the Consumer Principle must be changed from, 'A firm must act to deliver good outcomes for retail clients' to 'An authorised person must act to deliver good outcomes for consumers.'

While we remain concerned that an outcome test can be challenging when the gap between product design/sale and outcomes can be measured in decades in the case of many financial services products, provided the reasonableness and foreseeability tests (par 6.25) are not lobbied away prior to implementation, we hope that consumers will be empowered to seek assistance from the FCA as soon as they become aware that a product is likely to lead to a bad outcome and possibly even that the FCA will itself proactively identify the need to act, instead of having to wait until a bad outcome actually crystallises - by which time paperwork will have been lost, senior managers moved on, and firms and their insurers folded, merged or disappeared. We believe it is important that this is explicit in the final wording of the Cross-Cutting Rules, to eliminate in advance the defence (which may be exercised by authorised person, regulator or both) that nothing can be done about an example of poor treatment of consumers until the harm turns into a verifiably bad outcome, many years later.

Q6: Do you agree with our proposal to disapply Principles 6 and 7 where the Consumer Duty applies?

Q7: Do you agree with our proposal that Handbook and non-Handbook material related to Principles 6 and 7 should remain relevant to firms considering their obligations under the Consumer Duty?

We 'admire' the FCA's *chutzpah* in attempting to swerve a legal obligation to consult and bring forth rules on a duty of care by instead creating tougher-sounding wording for its Principles for Business, and believe it is essential that the change is implemented in that fashion so it is clear to Parliamentarians that this is what the FCA has actually done - which means that the Principles *do* have to change.

We therefore believe that complying with the existing Principles 6 and 7 is not sufficient to comply with the New Consumer Duty, we are very concerned that the detailed non-Handbook guidance in relation to NCD frankly undermines this message.

As it currently stands, the draft non-Handbook guidance does not consistently set a higher bar than Treating Customers Fairly, especially regarding product targeting, marketing, and governance. We believe Principles 6 and 7 material should be reviewed and removed where necessary.

Q8: Do you have any comments on our proposed cross-cutting rules and the related draft rules and non-Handbook guidance?

We would like to reiterate and amplify the point we made about par 6.25 in response to Q5. Just as authorised persons' (not 'firms'') behaviour must be guided by reasonable foreseeability, so must the regulator's. A 'good outcomes' test cannot only be applied *ex post*; it can and must be applied, and thus regulatory action must be initiated, as soon as it becomes reasonably foreseeable that the outcomes of a particular product or course of action are likely not to be good.

Q9: Do you have any comments on our proposed requirements under the products and services outcome and the related draft rules and non-Handbook guidance?

Overall, we are supportive of the measures proposed. However we see a gap: in focusing on a manufacturer/distributor model, there is a risk of downplaying the importance of ongoing delivery. Manufacture and distribution is very important when a new product is created or when a consumer is considering a purchase. A third leg of the tripod - delivery - is critical once the purchase has taken place.

The authorised persons responsible for delivery are in many ways more important than those charged with manufacture and distribution. They are responsible for ensuring that the product is delivered as described, and to a high standard; they may also, under the proposed Consumer Duty - and definitely would, under a genuine duty of care - be responsible for ensuring that it continued to meet the wants and needs of the customer and that it complied in full with the obligations set out in the FCA's Handbook and Principles for Business. Their impact on a consumer may extend over months, years or decades, and the standard to which they perform may make a huge difference to outcomes.

We are concerned at this omission and believe that a section on the expectations placed on those responsible for delivery should be added, if the intention is to proceed with the Consumer Duty.

Q10: Do you have any comments on our proposed requirements under the price and value outcome and the related draft rules and non-Handbook guidance?

We believe that it is difficult to reconcile the objectives of the fair value section with the FCA's stated position (par 8.7) that the Consumer Duty will not prohibit firms charging different prices to consumers in different circumstances. We recognise, for example, that a car insurance policy for a 19 year-old is a different product to the same level of cover on the same vehicle for a 55 year-old, because risk tends to correlate with age. But we cannot see a justification for charging different prices for new and existing customers (indeed, the FCA has banned dual pricing in the general insurance market, though it persists in many other regulated sectors), for people who purchase via different channels or even using different computer operating systems, browsers or email hosts. All too often, these are proxies for financial sophistication and thus can lead to rent extraction from the vulnerable.

There should be a loyalty discount and not a loyalty premium. High levels of churn increases the costs for the supplier of the service. Low churn reduces the cost and the benefits of this should be passed on to the consumer. This basic tenet of economics is not reflected in many financial services markets.

Q11: Do you have any comments on our proposed requirements under the consumer understanding outcome and the related draft rules and non-Handbook guidance?

We are supportive of these measures, but we believe they may be subject to a similar cognitive bias to the one we identified in our response to Q9: it is not enough to test the quality of communications; you should also test whether communications were sent out when the Consumer Duty might reasonably be held to give rise to a need to do so. Again, this implies that the Consumer Duty is an *ongoing* set of obligations, not a one-time one when a product is bought or terminated.

Often, when things go badly awry in financial services, there are authorised persons who were aware of this, but chose not to alert consumers in a timely fashion, in full or even at all. Even when things have not failed, catastrophically or at all, consumers' needs and market norms also change. When a fixed-rate savings product matures and defaults to a standard rate (these days, at or close to zero), does the Consumer Duty oblige the provider to notify the consumer? If so, what standard of communications are expected, in terms of timing, transparency, disclosure and frequency? Do these obligations change if the customer is deemed vulnerable (and if so, by whom, and on what grounds)? Likewise, what expectations are there on providers of pensions at different life stages, or of investment products if there's a period of market turbulence, underperformance, or a change to the manager, fee arrangements or governance?

The final rules should cover these issues and more.

Q12: Do you have any comments on our proposed requirements under the consumer support outcome and the related draft rules and non-Handbook guidance?

We believe that the 'unreasonable barriers' test (par 10.17) is insufficiently ambitious and is inconsistent with the higher standards set out in the product design and distribution section and indeed with the expectation (par 10.19) that a product should be 'at least as easy to exit as to enter.' Again, the FCA appears to be looking at financial services in transactional terms - in, out - and paying inadequate attention to the ongoing relationship aspect.

In the main, consumers' experiences of financial services relate to their ongoing relationships with firms; often, these fall short of expectations formed when arrangements are entered into.

It may be that the FCA's underestimation of the importance of the ongoing communications, service and value provided - or lack thereof - goes some way toward explaining why the industry under-delivers in this area.

In par 10.19, the FCA appears to endorse early termination fees, which in many cases amount to exit fees. We believe these are seldom, if ever, acceptable; they deter switching, which in turn tends to drive prices up and product/service quality down. In our view it is not acceptable to excuse them by stating that firms must draw consumers' attention to them. There are obvious asymmetries in the relationship. The consumer does not know, prior to contracting with a firm, whether representations made by it or on its behalf about product and service quality will be achieved; *ex post*, he or she will have a much better idea, but by then, will be bound by the exit clause. The consumer, *ex ante*, will also be unlikely to be aware of whether the exit fee is reasonable, or a commonplace or universal condition. And there are obvious financial incentives on the firm or its representative to 'forget' to bring the fee to the prospective client's attention, to downplay or otherwise misrepresent it.

The Consumer Duty could be an excellent opportunity for the FCA to signal that exit fees are unreasonable and anti-competitive, inappropriate for new contracts and unenforceable for existing ones. We cannot see how they are compatible with the wording of the Duty or with the FCA's objectives. We hope the FCA will take this opportunity to kill them off.

Q13: Do you think the draft rules and related non-Handbook guidance do enough to ensure firms consider the diverse needs of consumers?

Q14: Do you have views on the desirability of the further potential changes outlined in paragraph 11.19?

We believe the draft rules are broadly positive. Regarding the points raised in paragraph 11.19, we believe there is a risk of misdirecting the industry to be alert to diversity and inclusion which may be a poor proxy for vulnerability and different levels of consumer understanding. Anybody can be a vulnerable financial consumer, at a specific point in his or her life, or in specific circumstances; indeed, this may be as true of those who do not possess protected characteristics as it is of those who do.

Q15: Do you agree with our proposal not to attach a private right of action to any aspects of the Consumer Duty at this time?

No. As we explained in our answer to Q1 and extensively in our response to CP21/13, we believe that:

- Parliament required the FCA to consult and bring forward rules on a duty of care;
- The Consumer Duty, accompanied by a PRoA, could be said to amount to a duty of care;
- The Consumer Duty without a PRoA, is not a duty of care, so the FCA is in breach of FS 2021 if it proceeds as planned;
- A PRoA would empower consumers to bypass a weak and captured regulator and obtain financial redress through litigation if the regulator failed to obtain it through a restitution order or voluntary redress scheme;
- Gifting consumers this power would keep the FCA honest, as it would not want to be seen by politicians to fail in circumstances in which consumers then succeed;
- It would also empower the FCA: if it demanded redress from an authorised person, he/she/it would likely pay up to avoid the matter being subject to litigation in open court, with the legal costs, precedents and adverse publicity it would entail;
- For these reasons, it is likely that consumers would seldom need to use a PRoA; like a nuclear arsenal, its value lays in its existence and the threat of its use, not in its deployment

The need for a PRoA has subsequently been further evidenced by two developments. The first is the FCA's own admission (par 12.6) that, 'The PROA is a polarising issue. Most consumer representatives strongly supported it and most industry respondents warned against it.' If consumers want something that the industry wants to prevent them having, it is surely a reasonable supposition that the disputed thing tips the balance of power in the relationship between the two in consumers' favour. Given that the FCA has operational objectives to protect consumers and promote competition, it is surely obliged to side with consumers.

The second piece of evidence unintentionally emerged (Q223) from the FCA's own Chief Executive in his recent testimony to the Treasury Committee. Responding to a question from Julie Marson MP about why the FCA was choosing the industry side on the PRoA issue, Nikhil Rathi said, 'You need to be careful not to create excessive risk aversion in the provision of products by firms' which, we would respectfully suggest, clearly and unambiguously indicates that the Chief Executive of the FCA thinks that a PRoA would succeed in reducing the incidence of companies introducing harmful products; and for that reason is opposed to the idea. Is there any more proof needed that the FCA seems rather confused, conflicted and captured around its priorities and loyalties?

For the avoidance of doubt, the Consumer Duty would establish identical expectations of firms, whether or not a PRoA existed. Likewise, the other routes to redress he referred to would exist in either eventuality. So Rathi clearly believes that the existence of a PRoA would lead to firms behaving differently than they would if it were not introduced. Or, to put it bluntly, he accepts that the prospect of consumers having litigation rights would change industry behaviour when the theoretical risk of regulatory action does not.

Rathi used the word 'excessive' to qualify the 'risk aversion in the provision of products' that he believes could result from the introduction of a PRoA. But there are huge barriers to consumers litigating: inequality of financial resources; information asymmetries and time, to name but three. And even in the case of group litigation, consumers pursue this option only when there's a compelling reason to do so, including redress being unavailable through other means, not least because litigation funders take such a high proportion of any awards, and in turn the backers need a very strong case and a large number of claimants and quantum of claims to merit proceeding. So any PRoA would be utilised only in really strong cases; its deterrent effect would not, in our view, therefore be remotely 'excessive'; indeed, the fact that Rathi sees it this way is in our view further evidence that it is needed.

Of all the points advanced against a PRoA, the only one for which we have even a little sympathy is par 12.19, which argues that the Consumer Duty constitutes a significant package of changes and that understanding and implementing them correctly may take a while. Firms have 'strong concerns… about the potential impact and unintended consequences of attaching a PROA to the Consumer Duty from Day 1.' In lay terms, they're worried that they won't be able to comply with the new rules from the get-go and are worried that consumers will start suing them. They would prefer a situation in which 'firms and consumers will gain greater understanding of the impact of the Duty over time through supervisory action, complaints and our communications' - code for an expectation that their captured regulator will go easy on them in the early days of the Consumer Duty while they get their heads round fully implementing it.

In spheres of life other than financial services, it is unusual for new laws or rules to be accompanied by a grace period during which breach leads to advice rather than action. But we understand that the industry is operating under a regulatory environment that has been very flawed, for a very long time, so its capacity for compliance may not be as we'd like, and its expectation of leniency may be likewise elevated.

There are hints in the consultation document and in Rathi's exchange with Julie Marson MP that the FCA may intend to revisit a PRoA at a later date. We suggest a compromise: the FCA should provide a firm commitment to introduce one on a specified date a material period of time after the inception date of the Consumer Duty. Doing so would also provide time for it to consult on the precise wording and operation of the PRoA.

This would meet consumers' legitimate and warranted demand for a PRoA while also meeting the industry's questionable but perhaps understandable desire not to be subject to litigation for breaches of the Consumer Duty until it has had an extended period of time working with the FCA to implement it fully. The only parties whose aspirations would go unmet would be bad actors in the industry who don't intend ever to comply with the Consumer Duty and are hoping the FCA will forever shield them from the consequences. It is right that they should come out of this exercise empty-handed.

We hope that this constructive proposal for a workable compromise will be taken up by the FCA and the honest majority in the industry alike, and we hope that the FCA will signal that it accepts the need for a delayed PRoA in its response to this consultation. For this to be of any value to consumer representatives, it must be a firm commitment, backed up by an indicative timeframe for a further consultation and implementation.

We believe a grace period is a very generous concession, given that there is a strong natural justice argument to demand that all financial services firms ought to be able to comply with any regulatory requirement to treat customers fairly at all times.

It is in our view indisputable that a PROA is needed, because the general regulatory laxity displayed by the FCA is such that we cannot be confident in its willingness to use the statutory powers available to it. Among the most powerful recommendations (page 371-392) made by John Swift QC in his review of the regulator's handling of Interest Rate Hedging Products are those calling for more proactive regulation, clearer rules, greater use of statutory safeguards, greater use of statutory and regulatory powers, ensuring adequate resourcing, being more transparent and accountable, and improving the perception and actuality of its independence. Bluntly, if politicians are hoping the FCA will use its Enforcement powers against every firm that breaches the Consumer Duty and its Section 382/384 Restitution and Section 404 Redress powers (under FSMA), they're about to be disappointed.

Moreover, while the existing FCA Principles and proposed Consumer Duty are regulatory provisions and The Consumer Protection from Unfair Trading Regulations 2008 ('CPRs') are criminal ones, there are obvious parallels between them, in that the more egregious breaches of the former would also be breaches of the latter. The FCA has long been empowered under The Enterprise Act 2002 to enforce against the CPRs. We are unaware of a single case in which it has done so[1]. As is so often the case, there is a risk that the FCA is again consulting on new powers as displacement activity to distract politicians from its reluctance to use those already available to it. Against this background, a PROA is absolutely crucial, because it would empower consumers to act where the FCA doesn't, giving them a route to redress that is largely blocked off by a complacent or captured regulator - something the Consumer Duty, without a PROA, does nothing to change.

Q16: Do you have any comments on our proposed implementation timetable?

We are broadly comfortable with it, except that (as explained in our answer to Q15) we believe the implementation timetable must also include timings for consulting on and introducing a genuine PRoA.

Q17: Do you have any comments on our proposed approach to monitoring and the related draft rules and non-Handbook guidance?

We are broadly comfortable with these proposals, though would add that we believe that the FCA should require firms to report matters of concern that arise from the collection of information such as that outlined in par 14.22, and that the regulator should act on such information.

Taking for example the recent fine and redress package announced in relation to the practises of Lloyds Banking Group's General Insurance division, we know from whistleblowers that as far back as 2013 a mystery shopping exercise conducted by LBG in its branches showed that *every single sale sampled* - and they qualified as 'advised' - was non-compliant; the firm decided not to disclose this information to the FCA. It was also common practice for senior managers to order secretaries to complete mandatory online training modules for them, in their name; this too was never disclosed. When the whistleblower provided information on both matters to the FCA, no action was taken.

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[1] We have submitted a Freedom of Information Act request to the FCA to establish whether it has used these powers; the result is unlikely to be available prior to the deadline for submitting this consultation response

If the Consumer Duty does not result in the industry or its regulator changing their behaviours, it will amount to nothing more than a collection of 'motherhood-and-apple-pie' niceties designed to fool some politicians into believing that action has been taken. The introduction of a PRoA, even if delayed, would provide consumers with the power to ensure that the proposed measures result in genuine behavioural change.

Should anyone reading this paper doubt that consumers need this power and that the FCA cannot be left to police the industry alone, they should reflect on this passage from par 14.31's box about Enforcement:

'Where we identify *serious* misconduct by firms in relation to the Consumer Duty, we will use our full range of powers to tackle this, including investigating and *where appropriate* using our deterrent and remedial powers. This *could* include issuing fines against firms, and securing redress for consumers who have suffered harm through a firm's breach of the Consumer Duty.'

We have italicised three sections of the above paragraph. The use of the word 'serious' implies that the FCA will do nothing if it deems misconduct to be less than serious, and raises questions about who gets to decide what counts as serious, and on what basis. The 'where appropriate' qualification means that even when misconduct is serious, there is no guarantee that deterrent or remedial powers will be used. And the further qualification - 'could' - means that even when deterrent or remedial powers are deemed necessary, there's no certainty that wrongdoers will be fined (there's no mention of variance of permissions, removal from the register or prosecution - all of which are tools at the FCA's disposal) or, mentioned at the very end, of consumers being given redress.

We believe that *all* evidence and allegations of misconduct should be investigated, and that *all* of the FCA's statutory powers should be used if wrongdoing is proven. Taking as an example the LBG GI case mentioned above, whistleblower evidence about a mystery shopping exercise that demonstrated misselling and senior managers dodging mandatory training might have appeared to point to non-serious misconduct, but had it investigated the tip-off, it would have discovered extensive mistreatment of consumers, leading to widespread harms.

Against this background of regulatory timidity and complacency, we believe it is self-evident that a PRoA is desperately needed. Empowering consumers to litigate against those in the financial services industry who harm them is necessary both to give them a much-needed additional route to redress and to provide a credible threat to both industry and regulator that will encourage them to raise their game. The suggestion of a delayed implementation of a PRoA is, we believe, a generous concession and a genuine attempt to find common ground. We hope the FCA embraces it. The alternative is further reputational harm, as we set out in our answer to Q1.

Q18: Do you have any comments on our proposal to amend the individual conduct rules in COCON and the related draft rules and non-Handbook guidance?

No.

Q19: Do you have any comments on our cost benefit analysis?

We believe the FCA should, if it is determined to deny consumers a PRoA, publish a cost-benefit analysis. Any such exercise, if conducted in a competent and honest fashion, will show significant benefits to consumers and disbenefits to bad actors in the industry. There may be isolated disbenefits to good actors who make honest mistakes in the early days of implementing the Consumer Duty, if the PRoA is introduced on the same date. These disbenefits are largely eliminated by allowing for an extended period of implementation for the Consumer Duty before the PRoA becomes effective, as described earlier.

Q20: Do you have any other comments on the draft non-Handbook guidance?

Q21: Can you suggest any other examples you consider would be useful to include in the draft non-Handbook guidance?

No.