



## FCA CP21/36: A new Consumer Duty

The Institute and Faculty of Actuaries (IFoA) is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide, and oversee their education at all stages of qualification and development throughout their careers.

### Key points

We welcome the new Consumer Duty. We agree that the change in regulatory focus, from compliance with rules to good customer outcomes, should increase trust in financial services markets. It should also be commercially positive for firms in the long term by supporting more sustainable business models, as well as being good for customers and for society as a whole.

We urge the FCA to give further consideration to calls from the IFoA and other respondents to CP21/13 for explanatory paragraphs (within the Consumer Duty framework) to support the Cross-cutting Rules and to avoid ambiguity for firms and consumers. Our response includes suggested short explanatory paragraphs to support each of the three proposed Cross-cutting Rules.

We would also welcome further consideration about how the new regime will be enforced. We think it is important that all Senior Managers and Certification Regime employees believe the FCA will take effective enforcement action against them in the event of serious or widespread breaches of the Consumer Duty, and that junior employees feel able to raise concerns without fear of reprisals.

1. We thank the FCA for its further consultation on its proposals for a new Consumer Duty.
2. Last July, the IFoA submitted a comprehensive response to the FCA's previous consultation on this area, CP21/13, with input from a wide range of our membership including the Finance and Investment, Pensions, Life Insurance and Regulation Boards, as well as from members active in banking. We believe that the majority of our previous comments remain relevant to the current consultation. In responding

to this consultation, we think that it will be more helpful for the FCA if we limit our comments on this occasion to a number of areas which we support and to two areas (Cross-cutting Rules and enforcement) to which, in our view, further consideration should be given.

## Summary

3. We support the new Consumer Duty and many of the proposals in the Consultation Paper. We agree that the focus on good customer outcomes should increase trust in financial services markets. Also, it should be commercially positive for firms in that, although the elimination of some industry practices might reduce profits in the short term, it should support business models that are more sustainable for firms, as well as being good for customers and for society as a whole. In relation to the implementation of the new Consumer Duty, we suggest that further consideration be given to amplification of the Cross-cutting Rules and to how the new regime will be enforced.

## New Consumer Duty and other proposals

4. The survey results in paragraph 1.2, and the examples in Chapter 2, underline the need for action - and they strengthen the case for a 'reset' rather than for just amending existing rules or adding new rules. We support the FCA's intention to encourage a 'reset' from rules-based regulation to outcomes-based regulation, and believe that the new Consumer Duty, with its Consumer Principle, Overarching Cross-cutting Rules and Four Outcomes, provides a good framework for achieving the intended 'reset'.
5. Reasons for our support for the intended new approach include:
  - a. The new Consumer Duty will directly require firms to think about things from a consumer's point of view, rather than to focus on their own internal compliance with sets of rules.
  - b. The Four Outcomes provide a good framework for thinking about good outcomes for consumers. We think that the revised words chosen to describe the consumer understanding and consumer support outcomes are better than the words used in CP21/13.
  - c. The applicability of the new Consumer Duty across all retail sectors regulated by the FCA will make it easier for consumers to understand what they can expect from providers, whatever the product.<sup>1</sup>

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<sup>1</sup> We would welcome more clarity on whether the Consumer Duty applies to the investment managers of trustees of smaller pension funds if those trustees are not considered professional investors. Would such trustees be regarded as retail investors or as a third category?

- d. The new approach should avoid innovation being inhibited by narrow compliance with specific rules. An example is Open Banking, an important part of the rapid transition of retail banking to the digital age, which is leading to the development of innovative online products and services. Improving consumer outcomes in these markets would mean firms finding innovative ways both to serve consumers and to reduce the inherent risks, particularly of scams and fraud.
6. In addition to supporting the new Consumer Duty, we support many other proposals in CP21/36, including those discussed below.
7. Chapter 1: The intended change from rules-based regulation to outcomes-based regulation represents, as stated in paragraph 1.18, 'a significant undertaking'. Faced with such a significant change in approach, it is not surprising that industry respondents to CP21/13 raised concerns that outcomes-based regulation would be inherently less clear than detailed rules, as stated in paragraph 1.25. We are pleased that: (1) the FCA has proposed draft rules and Handbook and non-Handbook guidance to help provide examples of behaviour which would be likely or unlikely to satisfy the Consumer Duty, (2) the FCA is considering whether and how it can give more regular updates to provide further clarity on its expectations, and (3) the FCA intends to communicate its expectations and actions through Dear CEO letters, speeches and industry engagement (paragraphs 1.26, 1.29 and 1.56).
8. Chapter 5: We agree with the preference for Option 1 for the wording of the Consumer Principle. As stated in our response to Q5 in CP21/13, we prefer it because it is more aligned with the objective of good outcomes<sup>2</sup>. Also, looking at Option 2, we thought that the phrase 'best interests' was inappropriate for the intended 'reset' because it could be misunderstood as merely a re-statement of what was already there before. We also thought that the notion - albeit mistaken - of a duty to act in each individual consumer's best interests could make some firms oppose the proposals.
9. Chapter 5: We support the proposal to disapply Principles 6 and 7 when the Consumer Duty applies. As stated in our response to Q9 in CP21/13, we think it desirable to avoid firms having to comply with two different approaches at the same time. We note, in paragraph 5.32, the proposal to retain the Handbook and non-Handbook material linked to Principles 6 and 7. We would have preferred updated Handbook and non-Handbook material to be available to support the intended 'reset', but understand that this would involve a lot of work and might have the undesirable consequence of delaying the implementation of the Consumer Duty.

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<sup>2</sup> 'Good outcomes' must be adequately explained so that neither complacent firms nor customers with unrealistic expectations can reinterpret it for their own agendas (see also paragraph 17)

10. Chapters 7-10: We find the discussion in these chapters, about responses to CP21/13 and the FCA's responses and proposals, interesting and useful. The FCA's responses and proposals show that it has heard the concerns of respondents to CP21/13 and has taken them seriously, as stated in paragraph 1.40. For example, we agree with the calls for the FCA to be more specific about how fair value should be assessed (see paragraph 8.9), and are pleased that the FCA is now consulting on rules requiring firms to offer fair value to consumers (see paragraph 8.16). We share the view that vulnerable consumers should not be disadvantaged, and are pleased that the FCA will monitor outcomes experienced by different consumer groups to check that this does not happen (see paragraph 7.9). In some other areas, such as the need to focus on digital communications (see paragraph 9.20), and the need to ensure that the advice/governance boundary does not limit the provision of guidance (see paragraphs 9.34-9.35), we accept the FCA's rationale for not making changes to its proposals at present, but encourage the FCA to re-consider such feedback in future, and be willing to make amendments if appropriate, as it progresses with the implementation of the Consumer Duty, which it expects to be iterative, as stated in paragraph 1.29.
  
11. Chapter 11: In our response to Q8 in CP21/13, we suggested that there should be an additional Cross-cutting Rule for vulnerable consumers. We note, in paragraph 6.20, that the FCA has not proposed an additional Cross-cutting Rule for vulnerable consumers, because the draft rules have instead embedded consideration of these consumers at every part of the consumer journey. However, while many employees in firms will become familiar with the components of the new Consumer Duty (represented in the diagram at the top of page 33), they will not all be as familiar with the detailed rules. We therefore still think that there is a case for an additional Cross-cutting Rule for vulnerable consumers. This could be supported by references to diversity and inclusion in each of the Four Outcomes, as mentioned in paragraph 11.19.
  
12. Chapter 12: We agree with the proposal not to attach a private right of action to any aspects of the Consumer Duty at this time. As stated in our response to Q21 in CP21/13, we would prefer firms and the FCA to work together on implementing the new regime, with a common objective of achieving good outcomes for consumers. We remain concerned that the availability of a private right of action might lead to an adversarial approach and possibly to the withdrawal of some products. In relation to our preferred approach, we are pleased that the FCA is working closely with the Financial Ombudsman to ensure a consistent view on the interpretation of the Consumer Duty, as explained in paragraphs 1.31 to 1.34.

#### **Areas to which further consideration may be given**

13. We agree that the move from rules-based regulation to outcomes-based regulation will require a significant change in both culture and behaviour, and that the Consumer Duty will survive or fail based

on how it is supervised and enforced by the FCA (see paragraphs 1.12 and 1.18). One risk is that, despite all the good intentions to encourage judgment, the new approach will drift back to compliance with a new set of rules. Another risk is that some employees do not take the new Consumer Duty sufficiently seriously, because of a lack of concern about personal sanctions (see paragraphs 16 to 18 in our response to CP21/13).

14. We therefore suggest that further consideration be given to avoiding narrow compliance with the Cross-cutting Rules, and to ensuring that employees take the Consumer Duty seriously. We consider each of these below.

### **Cross-cutting Rules**

15. A benefit of the intended new approach is that the Cross-cutting Rules will be applicable across all relevant products, and in all situations, including situations that cannot be envisaged at the outset. We therefore consider it important that firms are encouraged to observe the spirit, and not just the letter, of the Cross-cutting Rules - and that they are able to make judgements, as recognised in paragraph 1.32. We note the request in paragraph 6.5, from respondents to CP21/13, for guidance to support the rules and to avoid ambiguity for firms and consumers. To provide such guidance within the Consumer Duty, we suggest that the Cross-cutting Rules should be supported by short paragraphs of text, in the way that the principles in The Actuaries Code<sup>3</sup> are supported by an explanatory paragraph. We provide below comments on explanatory paragraphs that might be included for each of the three proposed Cross-cutting Rules.

### **Cross-cutting Rule: Act in good faith towards retail customers**

16. In our response to Q5 in CP21/36, we suggested that the phrase “Act in good faith” could sound legalistic and archaic. We think that explanatory paragraphs would be helpful, especially for younger people and/or for those for whom English is not their first language. Such paragraphs could explain that acting in good faith is not just telling the truth: it is also about avoiding (1) misleading statements, (2) exploiting consumers’ behavioural biases or (3) sludge practices. A version of the useful words “clear, fair and not misleading” (from the to-be-disapplied Principle 7) might be included.

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<https://www.actuaries.org.uk/system/files/field/document/Revised%20Actuaries%27%20Code%20FINAL.pdf>

### **Cross-cutting Rule: Avoid foreseeable harm to retail customers**

17. Paragraph 5.23 recognises that it is not possible for all consumers to receive (or feel that they have received) a good outcome, and paragraph 5.24 says that neither the Consumer Principle nor the Cross-cutting Rules mean that consumers can or will be protected from all harm. Paragraph 6.24 says that this Cross-cutting Rule does not require firms to protect consumers from unforeseeable harm, all poor outcomes, or risks that the customer reasonably understood and accepted. We think that it would be helpful to include an integrated version of such statements in explanatory paragraphs. Absent this, in the future, when paragraphs 5.23, 5.24 and 6.24 may have been forgotten, this Cross-cutting Rule might be interpreted as saying that firms must avoid all harm to retail customers that could have been foreseen.

### **Cross-cutting Rule: Enable and support retail customers to pursue their financial objectives**

18. We remain concerned that firms may face a dilemma between ‘meeting consumers’ needs’ (as in the first bullet point in paragraph 1.16) and ‘consumers pursuing their financial objectives’ (as in the Cross-cutting Rule). As we said in our response to Q6 in CP21/36, on page 33 of ‘Our future Mission’, the FCA pointed out that consumers focus on the ‘here and now’. For example, a financial objective of many consumers may be to get the best price in the short term, even if there might be contingent charges or long-term risks. We note that the end of the second bullet point in paragraph 4.28 in Appendix 2 (on page 140) says that “if a customer insists on a course of action that the firm regards as harmful, they are not obliged to prevent it. However, the firm should take steps to ensure that customers understand the risks of their action”. This seems a sensible way to address the potential dilemma, provided that the number of such cases is not too large. To avoid ambiguity about the meaning of the Cross-cutting Rule, we think that it would be helpful to include paragraphs to support the Cross-cutting Rule, including the substance of this part of paragraph 4.28 in Appendix 2.

### **Enforcement**

19. While we agree that the new Consumer Duty should help firms to get things right in the first place, we believe that, in the event of serious or widespread breaches of the Consumer Duty or individual conduct rules, Senior Managers and Certification Regime (SM&CR) individuals should be liable to sanctions. In paragraphs 17 and 18 in our response to CP21/13, we said that:

“17. It is not clear that fines imposed on firms are leading to the desired improvements in the culture of firms or the behaviour of individuals within firms. To support the intended change in culture, we think that employees must believe that the FCA will take effective enforcement action

against individuals, not just for breaches of the FCA’s rules but also for breaches of the Consumer Principle”.

“18. Sanctions against junior employees might be considered unfair, given their lack of executive power. An alternative, to ensure the involvement of junior employees, might be to devise a regime in which they had more to gain by speaking up about breaches than by keeping silent to protect their superiors. Sanctions would be applicable to more senior employees for not taking reasonable steps to investigate concerns raised with them, or for treating employees badly because they raise concerns.”

20. We therefore support the proposals to amend the SM&CR individual conduct rules in the Code of Conduct sourcebook to reflect the higher standard of the Consumer Duty, and to include as part of this new individual conduct rule obligations that reflect the Cross-cutting Rules (paragraphs 15.4 and 15.6). We also support the expectation that firms will provide relevant training to their staff, so that they can understand their obligations under the Consumer Duty and the individual conduct rules (paragraph 15.7).
  
21. We note, in Nikhil Rathi’s speech at the launch of the HM Treasury Women in Finance Charter Annual Review on 17 March 2021, that the FCA was considering the addition of a sixth conduct question: “Is your management team diverse enough to provide adequate challenge and do you create the right environment in which people of all people of all backgrounds can speak up?”. The second part of this question could provide a framework for implementing what we suggested in paragraph 18 of our response to CP21/13. If firms were required, or at least encouraged, to hold ‘speaking up sessions’, it would be much easier for junior employees to raise concerns without fear of reprisals. SM&CR managers could be required to investigate concerns raised. These actions could be very useful in helping firms to get things right in the first place.
  
22. If you would like to discuss any of the points raised in this response, please contact Matthew Levine, Policy Manager ([matthew.levine@actuaries.org.uk](mailto:matthew.levine@actuaries.org.uk)).