

# The FCA's Consumer Duty

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Consumer Duty Series: Regulatory Consulting, DWF LLP

# Consumer Duty – an overview

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The FCA identified that the level of harm to consumers was too high, and better protection was needed in retail financial markets. Accordingly, pursuant to the Financial Services Act 2021, the government required the FCA to conduct a public consultation on whether it should make general rules providing that authorised persons owe a duty of care to consumers. Cementing the 'outcomes based' strategy set by the FCA in its 2022 Business Plan, the Consumer Duty is the name for a programme of regulation by the FCA comprising of three key elements:

1. A new Principle for Business: the "Consumer Principle" which requires firms to "act to deliver good outcomes for retail customers"
2. "Cross-cutting rule" setting out three overarching behavioural expectations that apply across all areas of firm conduct
3. "Four Outcomes", which are a suite of rules and guidance setting more detailed expectations for firms



The Consumer Duty will apply to the regulated activities and ancillary activities of authorised firms connected to the provision of a product or service that is or will be distributed to a retail customer. 'Retail customer' is defined differently depending on the product, aligning with the scope of the FCA Handbook in the respective sectors e.g. in relation to investments, to "retail clients" as defined in COBS; in relation to mortgages, to customers with regulated mortgage contracts as set out in MCOB and as applied through ICOBS.

The application will capture all firms throughout the distribution chain that could have an impact on retail customer outcomes, regardless of whether they have a direct relationship with the customer. However, the application is intended to be proportionate to the firm's role in relation to the product or service, nature of the products or service, and the characteristics of customers.

The Cross-cutting rules and the Four Outcomes are both intended to support the new Consumer Principle,

by setting clear expectations for firm's cultures and behaviours. This new approach to regulating the financial services industry is driven by FCA desire to move away from prescriptive rules and ensure it is a regulator which encourages innovation by providing firms flexibility.

The FCA has confirmed that the Consumer Duty will be forward looking, applying to products (new and existing) that will be sold to customers from the implementation date. However, relevant parts of the Consumer Duty will also apply on a forward-looking basis to closed products and services that are not being sold or renewed, and firms will be required to undertake an historic view of such products during the implementation period. Significantly, where a firm identifies potential consumer harm, they will be required to take appropriate action.

Firms are expected to be able to demonstrate and evidence how they have met and continue to meet the Cross-Cutting rules.



**Firms are also expected to have undertaken an assessment against outcomes for consumers in each area of the Four Outcomes and be able to provide an assessment at any given points about how products and services meet the expectations of the regulator under each of the Four Outcomes.**

### The three Key Elements expanded upon

#### 1) The Consumer Principle

The new Consumer Principle is:

- "A firm must act to deliver good outcomes for retail customers".  
This is the high level expected standard of behaviour.

The Consumer Principle will be:

- A new Principle 12, with Principles 6 & 7 dis-applied if the Consumer Duty applies. FCA considers Principle 12 sets a higher standard than Principle 6 & 7.

The new Principle 12 is intended:

- To put retail customers' needs at the forefront of firms' minds, and firms must have regard to this whenever performing activities in relation to retail customer. This may require significant change to the policies, procedures, and governance of a firm throughout all layers (even for firms which already focus on ensuring good customer outcomes).

#### 2) Cross-Cutting Rules

The three cross-cutting rules are:

1. Act in good faith towards retail customers
2. Avoid foreseeable harm to retail customers
3. Enable and support retail customers to pursue their financial objectives

They are designed to set out how firms should act to deliver good outcomes for consumers.

#### Acting in Good Faith

This is categorised by honesty, fair and open dealing, and consistency with the reasonable expectations of consumers. A number of examples given by the FCA of firms not acting in good faith include:

- **In relation to product service or design** – designing features to exploit behavioural biases to create demand
- **In relation to communications** – promoting products or services in a way that misleads consumers about benefits or risks
- **In relation to consumer support** – setting up systems that a firm knows will frustrate a customer or prevent them enjoying the use of their products

#### Avoiding Foreseeable Harm

The FCA considers that this includes firms taking both proactive and reactive steps to avoid customers suffering harm from a firm's conduct, products and services. Firms are only required to consider reasonably foreseeable harm in light of what they know or could reasonably be expected to have known.

This rule will apply throughout the customer journey and lifecycle of a product or service.

Firms with ongoing relationships will also have an ongoing obligation to avoid foreseeable harm.

#### Enable and Support Retail Customer to Pursue Their Financial Objectives

This rule requires firms to think about the financial objectives of their customers, and create the right environment where those customers can make informed decisions in their interest. This rule will apply throughout the customer journey and lifecycle of a product and service.

Firms must proactively and reactively focus on putting customers in a better position to make decisions in line with their needs and financial objectives. This would include recognising and taking account of consumers' behavioural biases and the impact vulnerability can have on their needs.

A large part of this is ensuring clients have all the information they need, that services/products are as simple as they can be, communications are clear, and clients are supported to make their decisions (e.g. remove unnecessary friction).

### 3) The Four Outcomes

The Four Outcomes are a suite of rules and guidance setting more detailed expectations for firm conduct across four areas that represent key elements of the firm – consumer relationship. These are:

- **Products and Services**
- **Price and Value**
- **Consumer Understanding**
- **Consumer Support**

The FCA's rules require firms to:

- **Monitor** and regularly review customer outcomes from products and services to ensure they are aligned with the Consumer Duty
- **Identify** where, and why, customers or group of customers are not receiving good outcomes
- **Respond** to and address any risks or issues identified, and to stop them occurring again

#### Products and Services

The rules and guidance for this outcome relate to the design and distribution of products or services (including any significant adaptation). They include requirements, building on PROD, for firms to:

- Identify a target market (including both manufacturers and distributors)
- Ensure product or service design meets the needs, characteristics and objectives of that target market
- Ensure the distribution strategy is appropriate for the target market

- Obtain and share information along the distribution chain – including between manufacturers and distributors
- Carry out regular reviews/monitoring to ensure the product or services continue to meet the needs, characteristics and objectives of the target market

#### Price and Value

Firms will be required to consider the price of a product or service to be distributed to a retail customer, and determine whether that constitutes fair value. The FCA is not prescriptive as to how this assessment is undertaken, but states that as a minimum it must include a consideration of:

- The nature of the product or service, including the benefits that will be provided or that customers may reasonably expect and their quality
- Any limitations that are part of the product/service
- The expected total price customers will pay (including any costs to be incurred throughout the distribution chain – this might not be known to manufacturers, but distributors with direct customer contact will need to take this into account specifically)
- Any characteristic of vulnerability in the target market for the product or service

#### Consumer Understanding

The FCA wants to ensure that communications enable customers to understand the products and services being marketed to them, including risks and features and implications of any decisions to be made. The consumer understanding outcome builds on the existing "clear, fair and not misleading" rules, and requires firms to:

- Support their customers' understanding by ensuring that their communications meet the information needs of retail customers, are likely to be understood by the average customer intended to receive the communication, and

equip them to make decisions that are effective, timely and properly informed

- Communicate in a way that is clear, fair and not misleading
- Tailor communications taking into account the characteristics of intended recipients, including any vulnerability, complexity of products, communication channel, and role of the firm
- Ensure information is accurate, relevant and provided on a timely basis
- Test, monitor and adapt communications as required to support good understanding and customer outcomes

### Consumer Support

The FCA notes that customers can only pursue their financial objectives if the firms supports them in using their products and services, and the FCA therefore expects firms to provide support to meet their customers' needs. More specifically, the rules and guidance in support of this outcome require firms to:

- Consider the support customers need and meet those reasonable expectations
- Support customers in light of their needs, such as not designing processes with unreasonable barriers that prevent them from realising the benefits of the product or service or acting in their best interests (including unreasonable additional monetary and non-monetary costs)
- Monitor the support offered, look for evidence of areas falling short of the outcome, and act promptly to remedy these
- Ensure they do not disadvantage particular groups of customers, including those with characteristics of vulnerability

One question firms can ask themselves is whether they are applying the same consumer support standards to

deliver good outcomes as they are to generate sales and revenue. For example:

- Firms should make it at least as easy to switch product, leave their service or make a change, as it is to buy the product or service in the first place
- The quality of any post-sale support envisaged in the customer relationship should be as good as the pre-sale support
- Obvious areas which firms should be considering include their IT infrastructure, operational resilience and client services and operation teams
- Prevent unreasonable barriers / friction to allow consumers to exercise rights or options relating to the product – do you allow e-signature to open account but a wet signature to transfer away without good reason? How do you justify any applicable exit fees and/or penalties? Will funds still be able to justify different share classes? This does not prevent reasonable barriers / friction being introduced – risk warnings / pauses in the process for high risk / important decisions etc.

“The new duty will drive a change in culture at firms. We expect firms to step up and put consumers at the heart of what they do and we'll be holding senior managers accountable if they do not. The duty will also help create an environment for healthy competition between firms, encouraging them to be innovative in developing products and services that meet consumer's needs.”

Sheldon Mills, Executive Director of Consumers and Competition at the FCA

# What should firms do next?

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Starting with appropriate project governance (e.g. milestones, owners, approval processes etc.) firms will need to decide with input from relevant stakeholders, on a plan of action. We would suggest that firms start with a gap analysis.

Beginning with a review of relevant firm-wide procedures and policies, firms should determine where changes should be made to comply with the Consumer Duty expectations (e.g. against the financial promotions, complaints, product governance policies). This 'top down' review will provide a view from a framework level as to how the Consumer Duty can be best embedded.

Depending on the business, there may be a need to consider at a products and services level undertaking a 'bottom-up review', and considering how to best embed the consumer duty from this perspective (e.g. the relevant client agreements or on-boarding processes for

each line of business). This should be informed by considering which products will continue to be offered post implementation deadline, understanding the FCA has explicitly noted it will not require firms to undertake any past-business type exercises.

## How can we help?

We are uniquely well placed with our combination of lawyers and regulatory consultants and can help with any or all of your Consumer Duty needs. Whether you want ad hoc support of various questions, an independent third party review of plans and progress, or for us to work closely with your internal teams to manage and implement the Consumer Duty, DWF's team is able to help.

## Contact Us

If you would like to discuss Consumer Duty and the impact it may have on your firm, please contact:

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