

Discussion Paper

FCA: Duty of Care

November 2018

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About Age UK

Age UK is a national charity that works with a network of partners, including Age Scotland, Age Cymru, Age NI and local Age UKs across England, to help everyone make the most of later life, whatever their circumstances.

In the UK, the Charity helps more than seven million older people each year by providing advice and support. It also researches and campaigns on the issues that matter most to older people. Its work focuses on ensuring that older people: have enough money; enjoy life and feel well; receive high quality health and care; are comfortable, safe and secure at home; and feel valued and able to participate.

About this discussion paper

The Financial Conduct Authority (the “**FCA**”) has issued a Discussion Paper on whether a new duty is needed to protect consumers and make markets work better for consumers. This Discussion Paper follows extensive discussion on the need for a duty of care as a result of perceived failings in the current principles based approach to treating customers fairly.

Key points

- We are pleased that the FCA has issued this Discussion Paper on a New Duty
- We see numerous examples of where the ‘Treating Customers Fairly’ principle (TCF) has not had the impact it was intended to have in protecting consumers and ensuring competition works in the interests of consumers. Many of these examples have resulted in serious detriment over many years
- In particular this highlights that there is still a need for culture change within the industry and a new understanding of fairness
- Firms have had many years to understand TCF and to improve their response, we are therefore not convinced that the FCA should simply wait for further improvements
- A new duty has the potential not just to make enforcement easier but to prevent detriment and make markets work better for consumers

Age UK Response

Q1: Do you believe there is a gap in the FCA’s existing regulatory framework that could be addressed by introducing a New Duty, whether through a duty of care or other change(s)? If you believe that there is, please explain what change(s) you want to see.

We identify two types of gap within the FCA's existing regulatory framework and approach to consumers which make us increasingly supportive of the concept of a duty of care. Firstly, gaps where firms create harm but do not appear to be breaching any existing rules or principles. Secondly, we see gaps where the behaviour may be in breach of existing rules or the Treating Customers Fairly principle but where enforcement has been slow, difficult or has not happened at all. Examples of harm that the existing regulatory regime has failed to protect customers from as a result of these gaps could include:

- Loyal customers penalised in the cash savings market
- Loyal customers penalised in home and motor insurance
- Loyal customers penalised in the mortgages market (where 16% of customers on standard variable rate were 65+ compared to only 5% of other types of mortgage holders)¹
- Harm caused to customers in the retirement incomes market by firms promoting loyalty rather than shopping around
- Treatment of vulnerable customers
- Lack of protection for customers targeted by authorised push payment fraud

We recognise that in some of these areas the FCA has recently made significant strides in addressing the harm using their existing rules and more commonly using existing powers to create new rules which deliver on their objectives. In particular the remedies proposed in the Retirement Outcomes Review and the Price Discrimination in the Cash Savings Market are encouraging. We also recognise the importance of the FCA's work on improving outcomes for customers in vulnerable circumstances.

When we consider these issues further, however, we find they demonstrate the need for much greater cultural change within the industry. All of these examples represent long-standing, straightforward and obvious detriment, with consumer groups and others calling for change for over a decade. All of these examples demonstrate that significant external pressure has been required to achieve change – consumer groups and responsible industry figures have called on the FCA to intervene and the FCA has then needed to take action. We agree that in each of these cases TCF could be interpreted to require firms to behave differently however in practice this is not how many firms are interpreting the principle. Given that TCF has applied for almost 20 years and the outcomes used to support it for 12 years and both have been applied by two different regulators (the FCA and before, the Financial Services Authority) it is difficult to anticipate that the introduction of the Senior Managers regime alone will be enough to cause a completely different understanding of TCF. We recognise the impact that increased understanding of

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<https://www.citizensadvice.org.uk/Global/CitizensAdvice/Consumer%20publications/Exploring%20the%20loyalty%20penalty%20in%20the%20mortgage%20market.pdf>

behavioural economics and willingness to engage in discussions on price discrimination has had in starting to address some longstanding detriment. These are such important developments that it is important the principles behind them are set out clearly so that all parts of the industry and consumers understand how they are intended to operate.

Although the Discussion Paper gives examples where there has been enforcement action directly against breach of the TCF principle these examples seem rare. It seems more common that the TCF might be referred to in the development of further rules or guidance which gives the impression that it is in fact difficult for the FCA to take direct enforcement action against a TCF breach. The New Duty could therefore play a useful role in making it easier for the FCA to enforce directly against a principle, where appropriate.

it is important to note that TCF creates a significant potential mismatch of expectations. A 'normal' consumer reading the TCF principle would probably be extremely surprised to learn that it didn't prevent the PPI scandal and hasn't stopped firms charging higher prices and giving lower savings rates for years. If consumers understand that firms are supposed to treat them fairly but have still been allowed to do these things, then it has the potential to undermine trust in financial services and in financial services regulation.

Our view is that a significant benefit of a New Duty is that it would be an effective way to achieve what most consumers would understand by the idea of 'treating customers fairly'. Many firms and to some extent past actions of the regulators have undermined TCF, in particular through the application of the principle requiring 'customers to take responsibility for their own decisions'. Even where the FCA has identified clear and significant harm to consumers we continue to see firms failing to comply even with the letter of, let alone the spirit of the regulator's interventions. The failings of some major firms in complying with the rules around PPI redress and the fears, including those expressed by the FCA, that interventions in the cash savings and retirement income markets could be gamed are recent examples of these. These factors all make it difficult to accept that we should simply wait for the Senior Managers regime to bed in and then review. There is a clear need for a major cultural shift in financial services which must be backed up by clear requirements that are easy to enforce against when breached. Without a clear and powerful overarching provision the regulators will largely be reacting to harm rather than preventing it.

A New Duty will not automatically result in better outcomes for consumers, it will need to be complemented by a new approach to fairness from the FCA – a shift that we are pleased is starting to happen (e.g. approach in the Price Discrimination in the Cash Savings Market Discussion Paper). It is important that any New Duty is well thought out, clear and simple to understand. It must be grounded in the real world behaviour of

consumers, firms and regulators. Whilst we recognise that future detriment will not always follow the same course as past problems we think there are some patterns and so we suggest that the FCA takes forward the work on the New Duty by:

- Developing 2 or 3 different forms of a potential New Duty;
- Undertaking a detailed review of the past and current examples of consumer detriment referred to in this response and ask:
 - Was/is there any breach of TCF involved in this detriment?
 - Should/did firms know that there was a breach and should this have prevented the detriment arising?
 - Could the FCA have enforced against any breach of TCF?
 - Was the time taken for the FCA to intervene and take substantive action (e.g. in the case of the Cash Savings Market the Discussion Paper on Price Discrimination) appropriate and could TCF or any of the FCA's other existing rules/powers have been used differently?
 - What difference could the different approaches to a New Duty make in closing the regulatory gap identified in the first paragraph of our response to this question?

There is also a risk that the development of a New Duty is endlessly delayed and generates more consultations and reports than it does consumer protection and better functioning markets. If the FCA disagrees with the need for fundamental change now it should say how it intends to close the current regulatory gap, and what indicators/outcomes it will be looking for to demonstrate that it has really been closed. The FCA must be ready to introduce a New Duty if these indicators are not met. To enable this to be meaningful, work on developing a New Duty should continue apace.

i. The types of harm and/or misconduct any changes would address.

As noted above there are numerous examples of where customers have experienced significant harm over an extended period which we would hope the New Duty would address. We would also hope that the New Duty would improve markets such as that for 'guaranteed acceptance life insurance or 'over 50s plans' where despite the existing rules around clear, fair and not misleading communications customers are still buying poor value products.

ii. Whether a New Duty should be introduced and, if so, what form it should take.

We are increasingly convinced by the case for a New Duty. We think a New Duty should include:

- Requirement to avoid conflicts of interest

- Requirement to act in the best interests of customers
- An understanding that failure to act can also cause harm
- An understanding that the duty is anticipatory and aims to prevent customers experiencing harm

Some of these are already present in FCA rules in respect of certain products or services. Given the need for cultural change we see considerable value in a New Duty which wraps up some of these concepts and makes them common across the industry. When combined with some of the additional elements (such as the anticipatory nature of the duty) this would set a new code of ethics for financial services, setting much clearer expectations for firms and consumers.

iii. What additional consumer protection and benefit this would provide, above the current regime (including over and above the existing implied term in the Consumer Rights Act for reasonable care and skill).

We agree with a number of other consumer groups who have considered this issue that a New Duty could help in the following ways:

- Anticipating the needs of customers will help prevent harm before it happens, reducing the volume of complaints either to individual firms or the Financial Services Ombudsman
- Increasing public awareness that a duty of care exists will enhance consumer trust and encourage people to discuss their circumstances with financial services providers and seek the support they need.
- An effective duty of care will help customers become more financially capable, helping them take greater responsibility for their decisions, as well as enabling them to maintain their financial wellbeing at times of vulnerability and acute need. This is because if firms comply with the New Duty products would become both better tailored to the needs of real consumers and easier for them to understand and operate.
- Reducing the gap between contract-based law and trust-based law, which is particularly important in pensions.

iv. How a New Duty could and should act to mitigate or remove conflicts of interest, including the types of conflicts which exist in the provision of financial services?

It is widely accepted that holding yourself out as the agent for an individual introduces a duty to avoid and manage conflicts of interest. Somehow it appears to be less easy for firms to spot and manage conflicts of interest with large groups of people – the selling of PPI is one example. This is particularly pertinent as increased digitisation within the industry is changing the nature of how firms interact with their customers and the risk is that the individual will increasingly be lost. An example could be the move from branch based to online banking: an extremely successful protocol has been set up to deal with

suspected frauds in-branch, but the experience of APP scams shows how difficult it is to set up something similar in a digital context. Therefore we believe that a New Duty would be very valuable in helping firms to manage systemic conflicts of interest. We would hope that by encouraging firms to identify conflicts with large groups of individuals it would contribute both to improved product design and to the management of emergent risks.

v. Whether a New Duty could reduce complexity and bring greater clarity, or whether it could result in an additional layer of regulation and make it more complex, and, if so, how?

We hope that the anticipatory element of a New Duty has the potential to reduce complexity and bring greater clarity by setting a less ambiguous approach to treatment of customers. By providing a clear overarching requirement we envisage that the New Duty would reduce the need for additional rules to prevent gaming of other rules and should in time prevent the need for new rules being imposed. For example the New Duty should be constructed in such a way that it would be a clear breach to charge a loyal customer much more for the same product than the firm would have done if the customer had called and asked for a better rate. It should therefore not be necessary to add new rules to prevent this particular harm.

vi. Whether other alternatives could help address any gaps, for example, extending the clients' best interests rule to different activities.

For the reasons mentioned in our opening paragraphs, we consider that there is a need for a significant break from the existing culture within many firms with respect to consumer protection. While it may be possible to make minor changes which improve matters technically we think it is unlikely that these could achieve the cultural change required. In particular it is difficult to envisage alternatives which would deliver the requirement for firms to anticipate the needs of customers. One example is in the development of suitable decumulation products for DC pensions. Three and a half years after the introduction of freedom and choice, we are still only discussing minor changes, for example firms' duties to provide improved information at retirement and the speed with which DC-to-DC transfers are carried out. A New Duty could ensure firms are obliged to be proactive with encouraging people to seek guidance and offering a greater range of appropriate options, including from outside their business. The FCA has already promised to develop a drawdown comparison tool, which if left to 'engagement' alone might have limited impact. However, combined with a Duty of Care, it could provide the ideal platform to boost shopping around. We believe this approach would also help the FCA meet its obligation of promoting competition.

vii. Whether we should introduce more detailed rules and guidance, and, if so, what specific rules and guidance are required?

Depending on the exact nature of the New Duty and depending upon harm identified in the market it may be useful to include some more detailed rules and guidance. The New Duty must also be able to stand alone in order to incentivise firms to act in the best interests of consumers even in the absence of specific rules, this is important to ensure that the anticipatory nature of the New Duty is effective and firms do not wait until the FCA introduces more detailed rules or otherwise makes clear that particular issues are regulatory priorities.

A good example is the FCA's recent work on vulnerability which has resulted in a major step-change in the industry's interest in how to serve vulnerable consumers. Yet the problems faced by vulnerable consumers were longstanding and capable of being understood by all firms serving retail customers, who would in fact already have had extensive experience of serving customers in vulnerable circumstances. It should not have been necessary for the FCA to publish an Occasional Paper in order to improve outcomes for consumers who most needed protection. The fact that there has been significant movement (although there is still a long way to go) without any additional rules illustrates that detailed rules are not always immediately necessary but that TCF alone did not achieve the required focus. The development of rules and guidance can be helpful to firms and help to promote consistency of minimum standards across industry. However we also see some firms seeking to adopt a 'tick box' approach, focusing on their policies and procedures rather than the needs of customers. For example, despite the fact that most firms would now accept that vulnerable customers need additional protections we continue to see firms focusing on the challenges of 'getting customers to disclose their vulnerability'. A New Duty would support any rules in this area by ensuring they did not simply become a tick box exercise.

viii. Whether the scope of any changes should differ between markets and whether it should include wholesale transactions.

Q2: What might a New Duty for firms in financial services do to enhance positive behaviour and conduct from firms in the financial services market, and incentivise good consumer outcomes?

Q3: How would a New Duty increase our effectiveness in preventing and tackling harm and achieving good outcomes for consumers? Do you believe that the way we regulate results in a gap that a New Duty would address?

As discussed in particular in our introduction and responses to questions 1 and 5 we do see gaps in the current approach. We have set out more detail of ways the New Duty could help increase effectiveness in our response to question 5 in particular. More generally, we would expect the New Duty would make it easier for the FCA to enforce against principles and so act more quickly to prevent detriment.

Q4: Should the FCA reconsider whether breaches of the Principles should give rise to a private right for damages in court? Or should breaching a New Duty give this right?

We are in favour of the New Duty giving rise to a private right for damages in court, although it is not our primary reason for supporting further consideration of a New Duty. Given the costs and challenges involved for private individuals in bringing actions for damages to court it seems highly unlikely that firms should expect significant amounts of vexatious challenges, including those brought by groups of people. Therefore we would expect private actions generally to be limited to situations where existing redress routes had failed and (i) individuals had experienced high levels of harm; or (ii) where many individuals had experienced significant harm. In these cases it would seem reasonable that an individual should be able to seek redress directly. It also seems important to focus the mind of firms on the experience of consumers. We envisage that the New Duty should be entirely possible to comply with and therefore firms should not expect to be subject to high levels of claims.

Q5: Do you believe that a New Duty would be more effective in preventing harm and would therefore mean that redress would need to be relied on less? If so, please set out the ways in which a New Duty would improve the current regime.

We consider that the New Duty would improve the current regime. In addition to the examples provided in response to earlier questions we set out examples of current areas of FCA work where a New Duty could improve outcomes for consumers.

A. Pension information

Information on pensions is often complex and not well-communicated by providers. In the accumulation phase, we welcome the introduction of the new simplified annual statement, which we support and are hopeful it will improve clarity on the current and likely future values of people's pension savings.

In the decumulation phase, for the majority of people who do not take financial advice, choosing what to do with their pension is an extremely difficult decision. It is often taken without full knowledge of the options available, or even basic knowledge of the products involved – in one survey over half of respondents thoughts drawdown provided a guaranteed income for life (PLSA, 2016). A Duty of Care should ensure that firms help people take better decisions when they come to access their pensions, for example by doing considerably more to persuade customers to use the Pension Wise service or help subsidise appropriate independent financial advice. The FCA has already used various

initiatives, for example the Retirement Risk Warnings included in pensions communications, which have been shown to have limited impact (Citizens Advice, 2016).

We welcome the FCA's proposals to send wake-up packs out earlier at age 50, which coupled with the proposed simpler format is a sensible development. A Duty of Care would complement this, as it would encourage providers to utilise the opportunity to ensure that consumers understand their options and are being offered products that meet their needs. It could also have wider benefits for example making firms develop more robust systems to ensure that people are not taking inappropriate decisions, for example through building a Pension Wise appointment in to the process of accessing the money.

B. Pension product distribution channels

Forthcoming Age UK research into how the pension product marketplace has developed since the introduction of 'freedom and choice' has found relatively limited overall product innovation, which is of concern – several products launched previously were then withdrawn, and were only available through advisers in any case. However, arguably where the Duty of Care could make a greater difference is in the development of tools to help people with their ongoing decision-making. While new tools have been developed to help customers manage drawdown, which has become the most common means of accessing a defined contribution pension, only basic calculators have been made available to all customers. More sophisticated models have only been made available through IFAs, meaning smaller and mid-sized savers, who are less likely to have access to financial advice, will typically be unable to access services that alert them if they are withdrawing too much or too little and provide safeguards to protect their longer-term interests. We believe a Duty of Care would mean firms either be encouraged to provide these tools to a wider range of customers, or at least implement a strategy of how to roll them out, for example by expanding the support they offer to their non-advised customers.

C. Post-sale pensions environment

As noted earlier in this response we welcome the FCA's proposed 'investment pathways' to help non-advised drawdown customers. The post-sale pensions environment is one of significant concern, and we believe there is the potential for a large amount of consumer detriment to occur, although it may be some time before we see evidence of this. The forthcoming Age UK research on the post-flexibilities marketplace suggests that firms are forging their own 'path of lowest risk' – meaning they are doing what they believe best to minimise the risk of future complaints and potential mis-selling. This often involves avoiding the provision of any support that goes above the minimum legislative requirements. There is no silver bullet, and while the proposed investment pathways will go some way to easing this difficulty, we believe that further action (which would be in stark contrast to the current state of inaction) from firms will be necessary to prevent future harm. A Duty of Care could invigorate firms' response to customer support, at least for existing customers, and mirror some of the requirements of fiduciary duty which applies to trust-based schemes. If implemented in a stronger way it could provide all customers - especially those who are dis-engaged and inactive – with the necessary help and prompts. For example, under a Duty of Care a drawdown customer who has been defaulted into a cash fund (identified by the FCA as being about 1/3rd of non-advised drawdown

customers, and a major problem) could potentially receive extra support from his provider that enables them to achieve better outcomes.

In 2016, as part of the response to Consultation Paper 15-12, the FCA amended the COBS handbook with the aim of encouraging people to explore their options and shop around on the open market. Given that today 94 per cent of non-advised drawdown customers stay with their existing provider (FCA, Retirement Outcomes Review (2018)), it is clear that this reform has had limited effect. A Duty of Care could require firms to go above and beyond the letter of the regulation, leading to more bespoke solutions tailored to a firm's customer base, which ultimately should lead to better outcomes.

D. DC to DC transfers/consolidation

There have been reports of undue delays for consumers trying to consolidate their DC pensions. A Duty of Care could place an obligation on firms to conduct this business speedily or incur a greater risk of falling foul of FCA regulations. This would align with current regulatory and public policy objectives.
