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Insights

WHAT WILL THE DISPUTES LANDSCAPE LOOK LIKE FOR FIRMS SUBJECT TO THE CONSUMER DUTY?

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SUMMARY

On 27 July 2022, the FCA published its policy statement, PS22/9, setting out its final rules for its new Consumer Duty ("Duty"), together with accompanying non-Handbook guidance. The Duty aims to set higher standards of consumer protection across the financial services sector and consists of:

- A new Consumer Principle requiring firms to act to deliver good outcomes for retail customers (new Principle 12 of the FCA's Principles for businesses, which will replace Principles 6 and 7 for retail business);
- Cross-cutting rules providing further detail on the FCA's expectations under the Duty (these require firms to: act in good faith towards retail customers; avoid foreseeable harm to retail customers; and to enable and support retail customers to pursue their financial objectives); and
- Rules relating to the four outcomes that the FCA wants to see under the Duty (these outcomes relate to: products and services; price and value; consumer understanding; and consumer support)

The Duty represents one of the most significant FCA regulatory developments in recent times and will, in the most part, come into force on 31 July 2023 after an initial implementation period. In this blog, we set out our expectations for what the disputes landscape is likely to look like for firms who are subject to the Duty.

NO PRIVATE RIGHT OF ACTION

There is, at least for the moment, no private right of action ("**PROA**") in relation to the Duty under s138D Financial Services and Markets Act 2000 – this is because the rules relating to the Duty are set out in the PRIN (Principles for Business) section of the FCA Handbook and the PROA does not apply to the PRIN rules.

In the consultations leading up to PS22/9, the FCA did consider the merits of opening up the PROA to the Duty (and its Principles more generally). Consumer groups argued that this would have a powerful deterrent effect to breaching the Duty. Industry respondents, however, expressed strong concerns against this – for example:

- that the threat of private court actions under the Duty would cause financial institutions to become too risk-adverse and withdraw products from the market;
- that it would push up the cost of financial institutions' PI insurance and that this cost would ultimately be passed on to retail customers; and
- that it could create a feeding frenzy for claims management companies.

The argument that appears to have won the day with the FCA for the moment is that firms should be given time to implement the changes that the Duty requires without the threat of private action being taken. This implies that the FCA's position may change once the Duty has been given time to bed-in, although the FCA has confirmed that it will not apply the PROA to the Duty without further consultation.

Firms should note that the above does not mean that the courts will be entirely excluded from the development of the Duty for the moment:

- Challenges to Financial Ombudsman Service ("**FOS**") decisions relating to the Duty may be heard by the courts through the judicial review process (see further below); and
- The Upper Tribunal and the appeal courts will also deal with any disputes arising from FCA supervisory and enforcement decisions against firms in relation to the Duty (also see further below).

COMPLAINTS

The most common routes to redress for retail customers for breach of the Duty are likely to be through firms' complaints handling procedures under the FCA's DISP (Dispute Resolution) rules and through complaints to the FOS.

A significant concern from a complaints-handling perspective arises from the fact that the Duty is an outcomes-based set of rules. The FCA has produced guidance on those rules and sought to provide some examples of behaviour that it considers will breach the Duty. However, its guidance and examples do not come close to legislating for the vast array of scenarios to which the Duty's four outcomes will apply. The Duty still, therefore, remains open to wide interpretation and that gives rise to risks from a complaints-handling perspective:

- First, there is the risk that the FOS will use the flexibility granted to it by its wide remit to make a determination on the basis of what it considers to be "fair and reasonable in all the

circumstances of the case" to find that the Duty imposes obligations on firms that go beyond firms' own legitimate interpretations of the new rules;

- Second, there is a risk of inconsistent decision-making by the FOS. The FCA dealt with this latter concern head-on in PS22/9, saying that it will work with the FOS to ensure that there is a consistent interpretation of requirements under the Duty. We wonder how realistic it is to ensure consistent decision-making by the FOS in this context, particularly where such a large number of FOS adjudicators and ombudsman will be applying the Duty across a huge range of products. In our view, there remains a real risk of inconsistent FOS decision-making in relation to the Duty, at least in the immediate aftermath of its implementation. That may well necessitate challenges to FOS decisions in relation to the Duty by way of judicial review. In addition, because firms are required to take into account FOS decisions in their own DISP complaints handling, such inconsistency could also cause obvious difficulties for firms in deciding DISP complaints relating to the Duty.

PROACTIVE REDRESS

There is also a significant development within the new cross-cutting rules requiring firms to act in good faith towards retail customers. Amongst those rules is a requirement that, where a firm identifies (either through complaints, monitoring or any other source) that retail customers have suffered foreseeable harm, it must proactively take action to rectify the situation, including providing redress where appropriate - various amendments have also been made to the DISP rules to support this. In other words, even where retail customers have not complained, firms are now required to proactively consider whether to offer them redress under DISP if they have suffered harm. That raises the stakes for firms in relation to DISP and FOS complaints handling. For example, an unfavourable FOS decision in relation to one retail customer might now lead not just to an obligation to apply that decision to future complaints, but also potentially to a requirement to, in effect, undertake a proactive redress scheme in relation to all other retail customers impacted by the same issue. This is potentially a real minefield for firms.

FCA ENFORCEMENT/SUPERVISION

There is, of course, the risk of FCA enforcement action and the imposition of fines for firms who are found by the FCA to be in breach of the Duty. One point that stands out from PS22/9 is that the FCA will be looking to quickly identify actions that fall foul of the requirements of the Duty (including through its new "data-led approach") and to use its supervisory powers to prevent future harm before it occurs. The supervisory powers that the FCA specifically mentions in PS22/9 are its powers to impose requirements on firms and to impose variations on firms' permissions ("**OIVOP and OIREQ powers**"). Those are powers in respect of which the FCA has recently removed the more rigorous Regulatory Decisions Committee as the decision-maker and, instead, put decision-making in the hands of its staff acting under Executive Procedures.

Many, including this firm, have already expressed general concerns that this could significantly increase the frequency of the FCA's use of these powers and, at the same time, decrease the quality of its decision-making in these areas. If those concerns are borne-out to be correct, we could potentially see significant use of the FCA's OIVOP and OIREQ powers in order to address breaches (or potential breaches) of the Duty. We might also see a number of those decisions being challenged in the Upper Tribunal and the appeal courts if the recipients consider that those decisions lack the necessary justification and rigour.

In addition, the FCA has made clear in PS22/9 that it will look to secure redress for customers who have suffered harm through firms' breaches of the Duty. One point to be aware of is that, because there is no PROA in relation to the Duty, the FCA is not, at present, able to impose consumer redress schemes on firms under s404 FSMA to compensate customers for breaches of the Duty. The impact of this is, however, somewhat counteracted by firms' new obligations to proactively consider offering redress to retail customers who have suffered foreseeable harm, as discussed above. Moreover, there are still other routes through which the FCA could impose redress schemes on firms for breaches of the Duty if they are minded to:

- the FCA has powers, under s384 FSMA, to require firms to pay restitution to customers who have suffered harm as a result of breaches of its rules (including the Duty); and
- the FCA may be able to persuade firms to agree to voluntarily implement redress schemes as a means of avoiding (or lessening the consequences of) formal enforcement action.

CONCLUSIONS

Although it is of some comfort for firms that the PROA is not available in relation to the Duty (at least for the moment), our expectation is that the Duty will still generate a wide variety of disputes for firms when it comes into force on 31 July 2023 – both because of the challenges it is likely to pose from a DISP/FOS complaints-handling perspective and because of the vigour with which we expect the FCA will seek to enforce it. We will be carefully monitoring how the disputes landscape surrounding the Duty develops over time. In the meantime, the best way for firms to mitigate the risks is, of course, to use the implementation period granted by the FCA to carefully assess the extent to which each of their products and services in scope complies with the new rules and to make any necessary changes.

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