

The Consumer Duty: a significant shift in retail financial services

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08-08-2022

United Kingdom

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On 27 July 2022, the Financial Conduct Authority (**FCA**) published a Policy Statement ([PS22/9](#)) and Finalised Guidance ([EG22/5](#)) setting out final rules and guidance on the new Consumer Duty (the **Duty**). The Duty sets higher expectations of the standard of care that firms give consumers. Firms will need to consider the actual impact of their products and services on consumers. The FCA wants firms to ensure that the interests of customers are central to their culture and purpose and are embedded throughout their organisations. The new requirements represent a significant shift in the regulation of retail financial services in the UK. In this article, Claire Carroll and Sumitra Subramanian of Eversheds Sutherland discuss what the Consumer Duty means for firms and their senior managers.

Setting higher standards and putting consumers' needs first is central to the [FCA's strategy](#), and the Consumer Duty is at the heart of this. The Duty encompasses a more outcomes-focused approach to regulation. The FCA believes the Duty will give firms greater flexibility to adapt and innovate, although in the immediate future firms are unlikely to have much bandwidth to consider new products and services. The FCA also believes it will advance the FCA's statutory objectives of securing an appropriate degree of protection for consumers and promoting effective competition in the interests of consumers.

What is the Consumer Duty?

The Consumer Duty will comprise the following elements:

- A new Consumer Principle (**Principle 12**) which will require firms to "*act to deliver good outcomes for retail customers*".
- Three **cross-cutting rules** that purport to provide greater clarity on the FCA's expectations under Principle 12. These rules will require firms to:

- act in good faith towards retail customers
- avoid causing foreseeable harm to retail customers
- enable and support retail consumers to pursue their financial objectives

Rules relating to four **outcomes** that the FCA wants to see under the Duty. The FCA considers that these outcomes represent key elements of the firm-consumer relationship that are instrumental in helping to drive good outcomes for consumers. The outcomes relate to:

- **Products and services:** the FCA wants all products and services for consumers to be: fit for purpose; designed to meet the needs, characteristics and objectives of the target group of customers; and distributed accordingly
- **Price and value:** the FCA wants all consumers to receive fair value. Value is about more than just price, and the FCA wants firms to assess their products and services in the round to ensure there is a reasonable relationship between the price paid for a product or service and the overall benefit a consumer receives from it
- **Consumer understanding:** the FCA wants firms' communications to support and enable consumers to make informed decisions about financial products and services and for consumers to be given the information they need, at the right time, and presented in a way they can understand
- **Consumer support:** the FCA wants firms to provide a level of support that meets consumers' needs throughout their relationship with the firm. This means that firms' customer service should enable consumers to realise the benefits of the products and services they buy and ensure they are supported when they want to pursue their financial objectives

Under the Duty, firms will be required to consider the needs, characteristics and objectives of customers, and how they behave, at every stage of the customer journey. As well as acting to deliver good customer outcomes, firms will need to understand and evidence whether those outcomes are being met.

The FCA is not introducing a private right of action for breach of the Duty, although this will be kept under review. However, firms should note that the FCA is strengthening its redress requirements under the Duty: where a firm causes harm to consumers, it will be required to be proactive and take action to rectify the situation, including providing redress where appropriate.

Detailed rules and guidance relating to Principle 12, the cross-cutting rules and the outcomes will be introduced into the FCA Handbook and are set out in PS22/9. The new requirements are broad in scope and relate to matters including product governance, distribution arrangements, price and value, customer communications, customer support, governance and culture, outcomes monitoring, redress, and the sale and purchase of product books. A new Individual Conduct Rule requiring conduct rules staff to “*act to deliver good outcomes for retail customers*” will also be introduced. The FCA has set out extensive non-Handbook guidance on the Duty in FG22/5.

Application of the Consumer Duty

The Duty will apply proportionately, based on what is reasonable in the circumstances, to all firms that can determine or “*materially influence*” retail customer outcomes. The extent of a firm’s responsibilities will depend on its role and the extent of the firm’s influence over retail customer outcomes. It will not have a retrospective effect, so actions taken before the Duty comes into force will continue to be subject to the rules in force at the time. The Policy Statement clarifies that where firms are already subject to FCA rules on product design or the assessment of value (for example, in the PROD, COLL or COBS sourcebooks), complying with those rules will also satisfy the relevant elements of the Duty.

The definition of *retail* will apply in line with the approach in the FCA’s existing sectoral sourcebooks. While a deceptively logical approach, this means there will be no single in scope customer population: the interpretation of retail will vary depending on either the characteristics of the product itself (e.g. in CONC) or the customer characteristics (e.g. in MCOB). This will lead to complexities for firms when identifying the perimeter of the Duty. Where the same product is offered to both retail and non-retail customers, will this mean that firms will, for simplicity and consistency, apply the Duty across all customers and, if so, accept the consequence that they will be held to that higher standard by non-retail customers? The FCA has also rejected the suggestion that the Duty should not apply to SMEs, stating that SMEs of various sizes can suffer poor outcomes.

The Consumer Duty will apply to “*retail market business*”. Broadly, this is defined as regulated activities (and “*ancillary activities*”), payment services (and connected activities), and issuing e-money (and connected activities) carried on by a firm in a distribution chain (including manufacturers and distributors) which involves a retail customer. An ‘ancillary activity’ for these purposes is an activity that is carried on in connection with a regulated activity or held out as being for the purposes of a regulated activity. This includes unregulated activities that are necessary for the completion of a regulated activity. For example, activities such as the design of a product or service, or ongoing customer support services, are not regulated activities in themselves but are necessary activities linked to regulated activities.

The Duty will not apply to cryptoassets or ‘Buy Now, Pay Later’ products as these are not currently regulated by the FCA. However, in view of the risks of consumer harm posed by these products, this is likely to change if and when these sectors are brought within the UK regulatory perimeter.

Products or services that are not designed for retail customers are not generally in scope of the Duty. Perhaps unsurprisingly, the FCA has stated that incorrectly classifying a product or service as non-retail with the aim of avoiding the Duty, and then distributing it to retail customers, would be in breach of the Duty.

Where the Duty applies, the FCA’s existing Principle 6 (customers’ interests) and Principle 7 (communications with clients) will be disapplied. Existing Handbook and non-Handbook material linked to Principles 6 and 7 will still be relevant as it may help firms in considering their obligations under the Duty. The FCA has made it clear that a failure to act in accordance with existing guidance on Principles 6 and 7 is likely to breach Principle 12. But, given that the FCA has determined that compliance with Principles 6 and 7 is not enough, firms will need to go above and beyond existing practices on treating customers fairly and reassess existing customer communications in order to comply with the Duty.

What does this mean for senior managers?

Senior management accountability is a core aspect of the Consumer Duty. Senior managers will be accountable for delivering good consumer outcomes within their areas of responsibility, in line with the Duty of Responsibility and the Conduct Rules under the Senior Managers and Certification Regime. Firms should also have a Consumer Duty ‘champion’ at board level (or equivalent management body). The Finalised Guidance sets out examples of the questions firms’ boards should be asking about the Duty on a regular basis, and which firms can expect the FCA to ask of them.

Firms’ boards will be required to issue an annual board report setting out how they have met the Duty and highlighting any areas that need improving, and the FCA may ask to see this report. While the basis of the report will be the firm’s management information (MI) relating to the Duty, senior managers may want to consider taking additional steps to satisfy themselves of the accuracy of the report, in view of the personal liability they may face should it transpire that the firm is failing to comply.

The FCA expects firms’ boards and senior management to ensure that they are embedding a culture in which good outcomes for consumers are central. Firms should have appropriate oversight of customer outcomes through their systems and controls, while risk functions should pay attention to consumer risks, which should also be a key lens for internal audit.

What does this mean for firms’ culture?

The FCA believes that the Consumer Duty will require “*a significant shift in both culture and behaviour by many firms*”. Culture is an essential element of the Duty, and the FCA has strengthened its final rules on governance and accountability with this in mind. Changes in culture and behaviour will need to be driven by firms’ senior management, with strong championing and oversight. The FCA has also indicated that it expects firms’ strategies, governance, leadership and people policies (including on remuneration) to be updated to reflect the Duty.

A theme running throughout the Policy Statement and Finalised Guidance is that firms should consider whether they are applying the same standards and capabilities to delivering good consumer outcomes as they are to generating sales and revenue. For some firms this will require a recalibration of priorities and a shift in culture, to ensure that delivery of good consumer outcomes is not outweighed by an excessive focus on sales and profitability.

A core aspect of the FCA’s work to improve culture in financial services is diversity and inclusion, and the Duty aligns with and supports the FCA’s work in this area. That follow-up work is expected to focus on diversity and inclusion among firms’ workforces, while the Duty focuses on firms’ relationships with customers, but both are designed to drive better outcomes for consumers. In particular, the FCA has highlighted that diversity of thought (also known as cognitive diversity) is essential if firms are to understand and respond to the needs of customers. The FCA, in common with other regulators, believes that a lack of cognitive diversity can lead to group think, poor decision-making and conduct failings. Such failings are likely to result in poor outcomes for consumers, potentially in breach of Principle 12.

When do firms have to comply?

The FCA initially proposed that the Duty should be implemented in full by the end of April 2023. This was widely considered to be an unrealistic timetable and, in response to industry pushback, there has been some movement. Firms will now be required to apply the Duty to:

- new and existing products and services that are open to sale (or renewal) from **31 July 2023**
- closed products and services from **31 July 2024**

While the phased implementation approach is welcome, it will still be highly challenging for firms to make the changes necessary to achieve compliance by these deadlines. The rationale for the relatively short implementation period is that the FCA wants the Duty to come into effect as soon as practicable, so that consumers can start to benefit from enhanced protections. However, this does not give firms much time to assess what changes are required and then implement those changes, so it is critical that they make good use of this period and plan and prioritise their implementation work effectively. Assessing the impact of the Duty on closed products and services will present particular challenges, especially if relevant product or service information is not readily available, so firms should not delay the gathering this data.

Interim deadlines

As a further challenge for firms, the FCA has set two interim deadlines during the initial implementation period. The FCA expects firms’ boards (or equivalent management bodies) to have agreed their implementation plans, and be able to evidence that they have scrutinised and challenged the plans to ensure they are deliverable and robust, **by the end of October 2022**. In view of the short timescale (which, unhelpfully, coincides with the summer holiday period), the scope of the planning required, and the complexity of some firms’ governance processes, meeting this deadline will present real difficulties for many firms. Those plans will need to be in good shape by the October deadline, as firms should expect to be asked to share their implementation plans, board papers and minutes with FCA supervisors and be challenged on their contents.

The FCA also expects manufacturers to aim to complete all reviews needed to meet the outcomes required for their existing open products and services **by the end of April 2023**. This is to ensure that manufacturers can: by the end of April 2023, share with distributors the information necessary for distributors to meet their obligations under the Duty; and identify where changes need to be made to their existing open products and services and implement these remedies by 31 July 2023.

What should firms focus on?

The October 2022 deadline is approaching fast, so it is critical that firms prioritise implementation planning. The board and senior management will need to maintain close oversight of the implementation programme, to ensure that implementation remains on track. Implementation of the Duty is a major regulatory change and will require an appropriate change management programme, with clear objectives. Best practice for programmes of this type is for firms to develop a detailed programme plan which is broken down into distinct, but linked, workstream activities, with owners assigned and clear lines of dependency established. In view of the anticipated short time frame for implementation, many firms commenced implementation programmes prior to publication of the Policy Statement. Those programmes will have to be revisited in light of the final rules, to check that there are no gaps.

Although firms’ compliance and legal functions will obviously play an important role in implementation of the Duty, at its heart, this is a customer-focussed project. Therefore, those involved in product development, marketing and customer-facing roles will need to be heavily involved in identifying gaps in existing products and services and ensuring that effective processes are in place to comply with the Duty. Non-executive directors will have an important role in challenging management on implementation and compliance.

If firms will not be able to complete the work necessary to comply with the Consumer Duty before the implementation deadlines, they must notify the FCA. The FCA expects firms to be compliant, however firms should take a risk-based approach and prioritise the implementation work that is likely to have the biggest impact on consumer outcomes (for instance, by reviewing the most complex and risky products and the most significant communications first). Firms should also note that legally the Duty will apply from the implementation date, and so complaints could still be brought by customers in relation to any non-compliance with the Duty from that date. Firms should not need to discard the work they have already undertaken to embed Principles 6 and 7, as it should be possible to build on this.

Where a firm determines that it will not be able to complete the work necessary to be compliant with the Duty in time, it must notify the FCA in accordance with its obligations under SUP 15.3.11R. Also, if, as part of implementation of the Duty, a firm considers withdrawing or restricting access to a product or service in a way that will have a significant impact on vulnerable customers or on overall market supply, the firm should engage with the FCA in a timely manner, in accordance with its Principle 11 obligations.

At the end of each implementation period, the board and senior management should assure themselves that the firm is complying with its obligations under the Duty and ensure that the firm has identified any potential gaps or weaknesses in compliance, as well as any action needed to remedy this.

While firms have flexibility as to how they implement and comply with the Duty, they need to be able to evidence how they have implemented and complied with the Duty. This will require enhancements to record-keeping systems. Comprehensive, meaningful and timely MI will be critical to enable firms to evidence that they are delivering good customer outcomes.

Firms should not lose sight of their existing obligations under Principles 6 and 7. Where firms identify serious issues causing immediate consumer harm, they should prioritise action to remedy this. This is particularly important where the harm is likely to be a breach of existing requirements. Firms should report significant breaches of existing rules to the FCA.

Impact on authorisation and supervisory activity

Even though it will not apply until 31 July 2023, firms and individuals seeking FCA authorisation or approval will need to be able to demonstrate their readiness to comply with the Duty from now on. This is because the FCA assesses applications for authorisation or approval on a forward-looking basis.

FCA authorised or regulated firms should note that supervisors appear to already be looking at them through the lens of the Consumer Duty. Some communications with firms, including Dear CEO letters, indicate that the FCA is not waiting for the Duty to come into effect before it acts to improve consumer outcomes.

The FCA is implementing a supervisory strategy that is appropriate for different types of firms and different retail markets. This will include: an initial communication to firms later this year on the FCA's expectations for implementation of the Duty in their portfolio; and a follow-up communication in the second half of the implementation period highlighting examples of good and poor practice in firms' implementation plans. Firms with a dedicated supervision team should expect the FCA to request and regularly review implementation plans and use proactive engagement and annual strategy meetings to assess implementation progress.

What happens if firms fail to comply?

A key FCA activity during the implementation period will be the development of an enforcement strategy that enables the regulator to effectively detect, triage and act on breaches of the Duty. While we expect the FCA to be assertive in taking enforcement action, it is likely to be some time before the regulator commences any such cases. Firms will need sufficient time to implement and embed the higher standards required by the Duty, and the FCA has indicated that it is unlikely to take enforcement action for non-compliance before July 2024 at the earliest.

It is not only firms that could face enforcement action: given the emphasis on individual accountability, we may well see senior managers being placed under investigation and facing enforcement action for their conduct in relation to implementation of, and compliance with, the Duty.

Identifying the compliance gap for closed products and services will be challenging if relevant information is not readily available, so it is likely to be these products and services that present the highest risk of non-compliance, leading to early intervention by the FCA and potential enforcement action.

There is an 'informant' aspect to the Duty, which will introduce a requirement for a firm in a distribution chain to notify the FCA if it becomes aware that another firm in the chain is not or may not be complying with the Duty. There will also be a requirement for a firm to notify relevant parties in the distribution chain if it identifies consumer harm. Firms should note that breach of these reporting obligations may put them at risk of enforcement action.

Other implications

In view of its scope and higher standards, the Consumer Duty is likely to be accompanied by an increase in compliance activity both during and after the implementation period. This will result in further growth of firms' compliance departments, competition for a limited pool of suitably skilled and experienced compliance professionals, and increased compliance costs for firms. This may lead to unintended consequences, such as an increase in the cost of retail products and services, or the withdrawal of certain products and services that are deemed to no longer be commercially viable, potentially causing harm to consumers.

While the FCA believes that the Duty will give firms the flexibility to adapt and innovate, it may end up having the opposite effect. In particular, due to the implementation challenges, in the immediate future firms are unlikely to have much bandwidth to consider new products and services. In the longer-term, increased compliance costs may prove to be a disincentive to the development of truly innovative products and services, as firms may decide it is simpler and cheaper to build on what they already offer rather than investing in something new.

Our podcast series explores different aspects of the Consumer Duty. You can [listen to the full series here](#).



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