# A new Consumer Duty
# Fair4All Finance response

**February 2022**

## Introduction

We're supportive of the new Consumer Duty, which will raise the standards of care that people can expect from financial services providers. We believe that it will contribute to creating a financial services sector that provides more people with products and services that meet their needs.

Following our response to the first Consumer Duty consultation, we have focused our comments on the following key points:

- Implementing the Consumer Duty is a significant undertaking and smaller organisations like community finance providers will need support and engagement from the FCA to get it right. The FCA should ensure the implementation period provides enough time to embed the Duty
- While it will raise standards for many customers who are already served by financial services, we believe that there is the potential for the Duty to reduce or limit access to products and services for customers who are currently excluded
- We therefore want to see the Duty accompanied by more proactive activity to foster innovation and increase the provision of products and services to excluded customers, such as promoting financial inclusion through the regulatory sandbox.

fair4all finance

## About Fair4All Finance

Fair4All Finance is a not for profit organisation founded in early 2019 to improve the financial wellbeing of people in vulnerable circumstances by increasing access to fair, affordable and appropriate financial products and services. We have three main priority areas:

- Expanding provision of affordable credit initially through a scaled community finance sector
- Partnering with banks and financial services providers to support the delivery of products and services for customers in vulnerable circumstances
- New product and market development – catalysing change by developing and scaling products and services to address market gaps

You can find our full strategy here.

## Our response

We're supportive of the new Consumer Duty and the FCA's ambitions to raise the standards of care that firms give customers.

We believe that the Consumer Duty will contribute to creating a financial services sector that provides more people with products and services that meet their needs, with more supportive communications and customer service that enables people to pursue their financial objectives.

The FCA is right that financial services markets do not always work well for consumers and in many cases fail to provide adequate consumer protection and competition. We believe the Duty will help tackle harmful practices, such as unfair pricing, the exploitation of customers' behavioural biases, and 'sludge' practices that stop customers pursuing their financial objectives.

A new principle with the duty to 'act to deliver good outcomes' for customers is a significant step up on the current requirement to have due regard to customers' interests and treat them fairly. We're pleased to see this shift towards outcomes-based regulation as, through our work in the short-term lending space, we have seen how community finance providers and high-cost credit providers can deliver significantly different outcomes despite following the same rules and often serving similar customer groups.

We welcome the proactive nature of the Consumer Duty which will require firms to be able to demonstrate how their business models provide customers with good outcomes. If it is combined with a robust authorisation process and an agile and assertive supervisory approach, the Duty will help prevent consumers being harmed in the first place, and allow the FCA to intervene more quickly when things go wrong.

## Implementing the Duty

In our response to the FCA's first consultation we said that firms would need guidance and support to successfully implement the Consumer Duty. We're pleased that this consultation paper, including draft rules and guidance, gives firms greater clarity about the expectations the Duty will place on them. Examples such as those in 14.22 on the types of information firms may want to collect to monitor customer outcomes provide a helpful steer to firms.

We welcome the strong focus on getting implementation right in this consultation paper. The FCA should take seriously the nearly unanimous feedback from respondents that the Consumer Duty will succeed or fail based on how it is supervised.

We still believe that successfully implementing the Duty will be a significant undertaking for firms and for the FCA. We are pleased that the FCA is planning to work closely with firms, trade bodies and stakeholders during the implementation period.

The community finance sector, which Fair4All Finance works closely with, is still emerging from the pandemic where it has faced serious challenges in supporting customers financially affected by the pandemic, transitioning to remote lending and work, and coping with lost income.

Community finance providers are typically small not-for-profit organisations that operate in a challenging market, with fine margins of sustainability. They have less resources than larger commercial firms do to interpret, implement and embed the new rules. And as referenced in the consultation paper, firms are already working on significant regulatory reforms such as the Senior Managers and Certification Regime.

The Consumer Duty is of course drafted to apply across all of financial services, and the FCA doesn't want firms to take a 'tick-box' approach to compliance, particularly as it shifts to outcomes-based regulation. However, we would like to see sector specific engagement, good practice and case studies to help smaller sectors such as community finance better understand what's required of them to successfully implement the new Duty. It's also right that the FCA has recognised the need for proportionality on certain expectations placed on firms like these, such as on the information they are able to collect to monitor customer outcomes.

We want consumers to start experiencing the benefits of higher standards of treatment as soon as possible, but it's also important that firms are able to properly embed the new Consumer Duty. Given the challenges they are facing, we don't believe the proposed implementation timetable provides enough time for community finance providers. The FCA should ensure that the implementation period is long enough to conduct appropriate sector-specific engagement and outreach in an iterative way, and for firms to make necessary assessments and changes.

It's vital that the FCA and the Financial Ombudsman Service (FOS) work closely together on the implementation of the new Consumer Duty. There should not be a perceived discrepancy between the rules as communicated during this period and decisions taken by the FOS on complaints.

In the high-cost credit market, many customers experienced significant harm due to unaffordable lending practices. This led to high volumes of complaints, facilitated by claims management companies (CMCs), which contributed in part to the collapse or withdrawal of many high-cost lenders. Customers who had suffered harm from unaffordable lending were therefore also unable to claim the redress they deserved. Addressing breaches in affordability rules through a supervisory approach would have avoided this double harm experienced by customers.

Moving to outcomes-based regulation will pose challenges in interpretation for firms. The FCA should consider the impact that CMCs may have in driving complaints, and use the implementation period to ensure that firms have clarity about the expectations placed on them by the Duty. It should also take a proactive approach to supervision to ensure that any breaches of the Duty are not allowed to run on. A new surge of upheld complaints would be the ultimate test of the success or failure of implementation of the Duty.

## Protecting provision

As we said in our response to the original consultation, it is crucial that the introduction of the Consumer Duty doesn't inadvertently lead to an overall contraction in the provision of products and services to customers with low financial resilience or low incomes. We believe the Duty should be accompanied by proactive measures to boost provision to these customer groups.

We appreciate that the FCA is taking concerns about the risk of firms withdrawing products in response to the higher standards or increased compliance costs of the new Consumer Duty seriously. By conducting a thorough implementation period involving proactive engagement with firms and trade bodies, the FCA should be able to prevent the unintended consequence of firms withdrawing products that are working well for customers.

We're also pleased that this updated guidance tells firms that they should consider the foreseeable harm that they may cause by withdrawing their products from the market. In the consumer credit market this should mean that lenders who are creating a significant gap in provision by leaving the market, as many in the high-cost credit space have done in recent years, have a responsibility to help their customers find fair alternatives, for example by signposting to responsible community finance providers.

As well as considering how to avoid the withdrawal of products that serve customer in vulnerable circumstances, on low incomes or with low financial resilience, the FCA should also fully consider the impact the Consumer Duty will have on firms seeking to enter these markets, and whether higher standards and compliance costs could act as a disincentive to entry.

The FCA is committed to taking forward recommendation 10 of the Woolard Review, around boosting the role that mainstream lenders play in non-prime credit markets and providing alternatives to high-cost credit. We welcome the FCA's recent engagement with us and others on this work, exploring potential barriers to entry to serving customers with limited borrowing options.

Feedback from commercial lenders suggests that this market is seen as risky from a reputational and regulatory perspective, and that lenders would welcome greater clarity about what good lending looks like in this market. The FCA should ensure that this workstream is joined up with the Consumer Duty and the implications between them fully considered.

## Financial exclusion

We believe there is clear evidence that the financial services market is failing to serve people with low financial resilience:

- 1 in 4 households in the UK have no insurance at all
- One in five adults has less than £100 in savings
- 5.8m people are 'invisible' to the credit referencing system

In the consumer credit market in particular we estimate around 11m people struggle to access affordable credit. With the collapse or withdrawal of many high-cost lenders, there has been a significant contraction in the supply of credit to customers in vulnerable circumstances.

We believe the Consumer Duty will lead to better outcomes for many customers in vulnerable circumstances. It will raise standards of care for all of a firm's customers, requiring more targeted products, clearer communications and more supportive customer service, all of which will particularly benefit customers of that firm who are in vulnerable circumstances.

The Duty will also be supported by the FCA's guidance on the fair treatment of customers in vulnerable circumstances, which requires firms to seek to provide these customers with outcomes that are as good as for other consumers.

Firms cannot exclude customers based on protected characteristics. The FCA's strong leadership on vulnerability means that customers who have vulnerabilities and are included in the market can now expect much better treatment from firms. But there is nothing to stop firms, including large mainstream financial services providers, from excluding people with low incomes or low financial resilience.

In many markets, firms exclude or price out customers who are seen as riskier or less profitable. Despite calls in the Woolard Review, there has been little progress from industry to start providing the mid-cost short-term loans that customers with low financial resilience need as an alternative to high-cost credit. And in the insurance market, more granular risk-based pricing has led to people on low incomes paying a significant poverty premium or being excluded altogether[1].

We don't want to see the Consumer Duty's emphasis on the need for products to suit a particular target market to lead to an intensification of this sort of exclusion. And while the benefits of the Consumer Duty are likely to lead to greater innovation and competition for customers who are already served, we cannot assume it will lead to firms innovating to serve customers who they currently exclude.

The FCA's engagement with firms over the implementation period should prevent the unintended consequence of firms responding to the Consumer Duty by withdrawing products that deliver good outcomes. But the FCA accept that the Duty will lead to some products that don't work well for consumers being withdrawn from the market. This is a necessary move to protect consumers from harm - but it's not clear what will take the place of products that are withdrawn.

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[1] Fair By Design and the Institute and Faculty of Actuaries (2021), The hidden risks of being poor: the poverty premium in insurance

## Enabling provision

For the reasons set out above, we still believe there is potential for the Consumer Duty to reduce or limit the provision of products and services to excluded customers in certain vulnerable circumstances, such as those with low incomes and low financial resilience.

Therefore, alongside the Consumer Duty we would like to see more proactive activity to foster innovation and increase the provision of products and services to excluded customers. We welcome the FCA's recent engagement on the role of commercial credit and potential barriers to serving customers with limited borrowing options and we'll continue to work closely with the FCA on this workstream.

Potential ways we believe the FCA could support the provision of products and services to customers in vulnerable circumstances could include:

- Setting financial inclusion objectives for the regulatory sandbox, scalebox and nursery. This would support and guide firms to innovate and scale with confidence to address market gaps in the provision of fair products and services for excluded customers
- Provide support, guidance and good practice on what good lending looks like to customers in vulnerable circumstances. This would reduce the impact of perceived regulatory and reputational barriers to this market and encourage more firms to serve currently excluded customers
- Monitor and report publicly on access to financial products and services at a market level. For larger firms with significant market shares the FCA should require transparency over who they serve and who they do not, including representation and outcomes for different customer groups and demographics. This would increase accountability and drive firms to improve the inclusivity of their offer