# A duty to be good – like it or not

*Richard Northedge assesses how the new consumer protection measures will affect the mortgage industry, which has called them unnecessary and unworkable*

There are two standard responses when regulators reveal new rules: first, that they will be impossible to implement; second, that firms are already doing what is proposed. The Consumer Duty announced by the Financial Conduct Authority (FCA) is, according to the mortgage lenders and brokers it affects, simultaneously both unnecessary and unworkable. But, like it or not, it is coming soon.

This consumer protection measure targets not only poor products and bad value but also the time taken to answer phones, why it is easier to enter a contract than end one, hiding key points in lengthy terms and conditions, and jargon. Indeed, the FCA refers to 'rip-off fees' without waiting for the tabloids to translate its own legalese. But even for firms that pride themselves on customer service, the Consumer Duty will mean revising systems and training staff. And, in future, customers may have a right to sue firms for damages.

> *The regulator boasts that the new code should fundamentally change how firms serve their customers*

'Customer first' could be the overall slogan. The overriding principle of Consumer Duty is to deliver good outcomes for consumers. Beneath that are what the FCA calls cross-cutting rules – to act in good faith, avoid foreseeable harm and support customers to pursue financial objectives. And then there are four outcomes: products and services; price and value; consumer understanding; and customer support.

Why did the FCA think a new code necessary? Well, it didn't but MPs, critical of regulatory failures such as the Woodford Equity Income Fund suspension and London Capital & Finance collapse, forced a consumer-protection requirement into the Financial Services Act 2021. That resulted in quick action: two consultation papers in 2021, a final scheme in July 2022, and firms told to agree implementation plans by October 2022. Even with a three-month delay, the July 2023 start date for current products is just a year after publication and old products will be covered a year later.

The regulator boasts that the code should fundamentally change how firms serve customers. It is intended to change the culture and behaviour of financial services firms but the FCA admits it will lead to high costs in the short term "and probably in the longer term".

### The worst offenders

Consumer Duty applies to all 50,000 UK financial services providers but surveys suggest the worst offenders are not in the mortgage sector. The regulator's 2020 Financial Lives survey found banks were more trusted than any other group, scoring 6.5 out of 10, with mortgage lenders second on 5.9. (The government score was just 4.1, with only social media below that.)

The main mortgage complaints concerned complex product information, delays in changing loans and poor customer service. But firms offering credit cards, funeral plans, shares, insurance and other products have far worse reputations.

Mortgage firms may think they have less work to do, therefore, but the new regime doesn't just require them to be good, they have to demonstrate that they are. They will have to assess and measure their processes and operations, but the FCA is not specifying what the firms should monitor. They could choose phone-answering times, complaints received or training programmes, for instance.

The regulator is keen on measuring outcomes rather than input because it allows comparison between different sized firms operating different models. The hope is that firms study the results and remedy their own faults – prevention being a key objective. Yet considering concepts such as 'fair value' gives wide scope for subjective assessment and, despite the flexible approach, the FCA will need to collate results if, as it says, Consumer Duty is part of its transformation to becoming a "more aggressive and data-led regulator".

### Will it help?

The Building Societies Association gave Consumer Duty a harsh rejection last year, stating that it is "unnecessary, undesirable, premature and we are concerned that it may be a reaction to the FCA's own past inability to effectively supervise and enforce". UK Finance was equally scathing, saying its introduction would lead to more harm than the benefits it sought to achieve.

The benefits to the consumer are seen as not only financial but also a saving in time and a reduction in stress when dealing with financial firms. The regulator does not attempt to quantify that gain but believes it outweighs the costs, which it has tried to estimate. The one-off expense for firms was put at between £688m and £2.4bn, an average of up to £46,000 per firm, although the size of firms varies considerably. The training bill could exceed £150m, with IT costs approaching £1bn. On top of that would be costs of £74m to £176m every year, plus the unquantified loss of profit from a tighter crackdown on 'ripping off' customers.


> *There is a danger that smaller firms may find the costs or bureaucracy too much and sell up or merge*

There could, too, be fines for miscreant firms. The FCA's full range of sanctions can be employed for breaches of Consumer Duty, including redress for disadvantaged customers. At the consultation stage, the FCA proposed a new Private Right to Act – an ability to bring private court proceedings against advisers or product providers for damage suffered. That is not included in the regime that starts next July and the regulator has purposely avoided using the term 'duty of care'. It says it wants to allow firms to embed the published Consumer Duty, but that it is keeping under review the possibility of a Private Right to Act.

The right to sue would seem an invitation to the ambulance-chasing lawyers who have proved so zealous in recovering payment protection insurance or endowment policy compensation for the public and who are pursuing class actions over scandals such as Woodford. In terms of profits, insurance and compliance, the litigation threat would worry many firms. But there is also an important principle: the FCA's word would no longer be final if it can be overturned by independent judges in the courts. And in practical terms, an already slow regulatory process could be stretched greatly as disputes work their way through the judicial labyrinth. Firms will be watching for any hint of the FCA reviving this idea.

Even without the threat of the courts, one worry is how products supplied in the past will be regarded in the future. Is a historically high fixed-rate mortgage still fair value if market rates fall? Can inflated standard variable rates be justified? Do past high loan-to-income mortgages still seem fair? What of 'mortgage prisoners' unable to switch lender? There are no answers yet, but can lenders risk waiting to find out?

There is a danger that applying a consumer duty makes firms more risk averse. Despite the regulator arguing that the regime allows firms to be more competitive and innovative, it could reduce the range of products offered because of the cost of tailoring them to a small market. It could also make them more expensive as additional costs are passed on to consumers. Rather than help consumers, providing extra protection and increasing trust in firms could also make people less responsible for their own actions.

But improving standards is good for the industry as well as consumers. Big providers may already be monitoring their service but they also need to look at products. For instance, do exit fees stop clients exiting? Smaller firms, as with previous rule tightening, may find the costs or bureaucracy too much and sell up or merge. Indeed, consolidation may itself enhance consumer protection.

Most firms will cope with this new rules regime but history shows that the regulatory screw turns only one way. Today's common practices could be outlawed tomorrow. Consumer Duty is the latest of many rule revisions, including the Mortgage Market Review, Retail Distribution Review and Mortgage Credit Directive. It won't be the last seismic change to have an impact on the industry. ■

***Richard Northedge*** *is a former Banking Journalist of the Year and has spent the past decade at a leading investment bank*