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## **AFM Response to FCA Discussion Paper on a duty of care and potential alternative approaches**

1. I am writing in response to this consultation paper, on behalf of the Association of Financial Mutuals. The objectives we seek from our response are to:
  - Comment on the idea of a duty of care and whether and how this could be applied in financial services.
2. The Association of Financial Mutuals (AFM) represents insurance and healthcare providers that are owned by their customers, or which are established to serve a defined community (on a not for profit basis). Between them, mutual insurers manage the savings, pensions, protection and healthcare needs of over 30 million people in the UK and Ireland, collect annual premium income of £19.6 billion, and employ nearly 30,000 staff<sup>1</sup>.
3. The nature of their ownership and the consequently lower prices, higher returns or better service that typically results, make mutuals accessible and attractive to consumers, and have been recognised by Parliament as worthy of continued support and promotion. In particular, FCA and PRA are required to analyse whether new rules impose any significantly different consequences for mutual businesses<sup>2</sup> and to take account of corporate diversity<sup>3</sup>.

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<sup>1</sup> ICMIF, <https://www.icmif.org/publications/market-insights/market-insights-uk-2016>

<sup>2</sup> Financial Services Act 2012, section 138 K: <http://www.legislation.gov.uk/ukpga/2012/21/section/24/enacted>

<sup>3</sup> <http://www.legislation.gov.uk/ukpga/2016/14/section/20/enacted>

4. We welcome the debate that FCA has fostered about the merits of a duty of care. As the paper states, the roots of the discussion emanate from a concern expressed by some stakeholders that FCA's regulatory framework, including the Principles for Business, "may not be sufficient or applied effectively to prevent harm to consumers and protect them appropriately".
5. We note that FCA has adopted a relatively neutral position on whether or not to take this forward in the discussion paper, and we consider this is appropriate in light of the complexity of the issue and the diverse and competing views that the discussion paper may produce.
6. FCA summarises the arguments in favour of a duty of care as relating to an obligation on providers of financial services to avoid conflicts of interest, to act in customers' best interests, and to deter from mis-selling products and services. These are all legitimate concerns, as too is the expectation that firms exercise greater care when dealing with more vulnerable customers.
7. In our assessment, from reviewing the paper, and from attending the recent workshop run by FCA, it is difficult to distinguish how a new Principle for Business on a duty of care for firms will substantively deliver on these arguments, or equip FCA with any additional powers or tools they do not already possess. The examples of potential harm highlighted by the FS Consumer Panel and others appear to be covered by existing Principles and are also covered extensively in the rulebook.
8. The existing framework is set out comprehensively in chapter 2 of the paper, and FCA rightly focuses on the expansion of the Senior Managers' Regime, as well as that as this becomes more fully embedded, it offers the potential to more effectively address the outcomes a duty of care obligation might be expected to deliver. Coupled with Principle 6 in particular, covering treating customers fairly, the toolkit provides extensive support for effective regulatory action. In addition, the Insurance Distribution Directive, introduced this month, highlights for relevant organisations the expectation of "doing the right thing for your customers".
9. A key question therefore is to what extent is FCA taking full advantage of the tools already available to it. For example:
  - a. TCF is a very powerful and wide-ranging tool, that is frequently drawn on in enforcement action, to reinforce infringements of rules, and to enable action which might fall between the gaps in rules otherwise.

- b. The volume of cases reviewed directly by the Financial Ombudsman Service should enable FCA to spot emerging issues early and to act on them effectively.
  - c. An absence of supervisory engagement encourages FCA to constantly ramp up rules, to ensure broadly compliant firms remain constantly vigilant about regulatory standards, increasing compliance costs. However it does little to incentivise less compliant firms to raise performance.
  - d. Amongst AFM members, the breadth of the flexible portfolios for life and non-life insurers, the small scale of our firms, and the regulatory priorities which largely focus attention elsewhere, mean that there is very little prospect of a small mutual coming into direct contact with FCA supervisors, unless data analysis indicates they are an outlier. Knowledge of the sector is therefore limited, both in policy and supervisory areas. By contrast, PRA seeks to resolve this by running annual 'regional visits' to a subset of small mutuals.
10. In our view, the risks of introducing a principle or rules on a duty of care are significantly greater than the potential gains. We consider the consequences might include less use of intermediaries by providers who are worried about being implicated by failings in a financial adviser or broker, and the potential for firms to withdraw from markets where the risk of being censured under a duty of care principle are greater. We also envisage Claims Management Companies would see the potential for a principle to offer a lucrative source of action against companies, particularly where it offers a relatively open-ended and subjective interpretation of what a duty of care involves.
11. We do however consider that FCA can do more to promote the issue, and in this light we offer the following suggestions:
- a. Extra guidance on a duty of care, with a range of case studies such as those used in the paper, would helpfully set FCA's views on their responsibilities to customers, without creating extra layers of rules;
  - b. The current six Treating Customers fairly outcomes could be extended, to set a duty of care within this framework;
  - c. The work undertaken by the Competition and Markets Authority for large banks on publication of a range of 'quality of service' indicators could be extended to other sectors, to give consumers a better understanding of which firms deliver better customer outcomes;
  - d. It does not seem practical to envisage that all conflicts of interest can be removed, as some stakeholders have suggested. After all, in a listed company, the primary responsibility of management

is to develop a return to shareholders. But we do think FCA can do more to explore how different business models and product offerings create or mitigate potential conflicts of interest: for example, as mentioned in paragraph 3, the Bank of England and Financial Services Act introduced a new requirement for FCA to take proper account of corporate diversity, in all its activities. So far, we have seen no evidence that FCA has acted on this: for example, the FCA Business Plan and annual report make no mention of corporate diversity or mutuality.

- e. It remains too easy for people to obtain an authorisation, where they were previously involved in a firm or activity that gave rise to consumer harm, and consumers remain at risk of mis-selling from companies based overseas. We believe FCA can improve its intelligence gathering and liaison with other agencies.

12. We have not answered the specific questions in the paper directly, but we hope the comments above provide a clear view of our preferences for taking this initiative further.

13. We would welcome the opportunity to discuss further the issues raised by our response.

Yours sincerely,



Chief Executive  
Association of Financial Mutuals