

Consumer duty part 1 - 'The drill-down' into the 'cross-cutting' rules

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What are the ramification of 'good faith'?

This article is the first in a series aimed to help firms get to grips on a practical basis with the 'cross-cutting rules' within the new 'Consumer Duty' framework.

1. 'Good faith' as a component in the 'consumer duty'

On 31 July 2023 the Financial Conduct Authority (FCA) rules on the 'Consumer Duty' (CD) take effect. The corner stone for the new rules will be Principle 12: "A firm must act to deliver good outcomes for retail customers" (not limited to "consumers").

The principal framework is set out from PRIN 2A.1 (see eg via the FCA Handbook's 'timeline' feature).

The rules in PRIN 2A include the "Cross-cutting obligations", with the following at PRIN 2A.2.1 R: "A firm must act in good faith towards retail customers."

2. How the CD rules address good faith

'Good faith' is not defined in the rules, nor is it a concept used previously in FCA regulation (excluding 'utmost good faith', a specific feature of insurance contract law addressed in PERG 6.6). However, the FCA gives guidance as to the attributes of good faith.

- PRIN 2A.2.2: "Acting in good faith is a standard of conduct characterised by honesty, fair and open dealing and acting consistently with the reasonable expectations of retail customers."
- PRIN 2A.2.3 gives "examples" of "not acting in good faith":
 - "failing to take account of retail customers' interests, for example in the ... [design of] a product or [presentation of] information;
 - seeking inappropriately to manipulate or exploit retail customers, for example by manipulating or exploiting their emotions or behavioural biases to mis-lead or create a demand for a product;
 - taking advantage of a retail customer or their circumstances, for example any characteristics of vulnerability, in a manner which is likely to cause detriment;
 - carrying out the same activity to a higher standard or more quickly when it benefits the firm than when it benefits the retail customer, without objective justification"
- Applying a degree of limitation to the above (albeit with some circularity), PRIN 2A.2.4 provides "[This] does not mean a firm is prevented from pursuing legitimate commercial interests or seeking a profit, provided it does so in a manner which is compliant with Principle 12 and PRIN 2A."

3. Understanding good faith from outside the CD rules

3.1 Other FCA Rules

It's worthwhile considering how the above terms and concepts have been previously used by the FCA.

3.1.1 Customers interests

'Customers' interests' have been a feature of mortgage regulation since 2016 (see [MCOB 2.5A](#)), insurance since 2018 (see [ICOBS 2.5](#)), and funeral plans since July 2022 (see [FPCOB 2.1.2](#)) with rules to the effect that "A firm must act honestly, fairly and professionally in accordance with the best interests of its customer."

The above rules have not been put to the test through reported enforcement proceedings, although the concept of 'customer's best interests' was used by the FCA in relation to a failure by an asset management firm to manage conflicts of interest fairly ([GAM International Management Limited](#)).

3.1.2 Emotional exploitation

This concept has been used in mortgage regulation since 2016 ([MCOB 3A.8.4R](#)): "A firm must not in any financial promotion of a regulated sale and rent back agreement exploit the vulnerable nature or circumstances of any customer who may be in financial difficulties and at risk of losing his or her home. As such, the firm must avoid using phrases or terms such as "fast sales", "rescue" or "cash quickly" or any other similar expression." This has not however been tested through reported enforcement.

3.1.3 Taking advantage on a personal basis

This concept is a feature of [ICOBS 6B](#) (ie at 6B.2.40(5): "A firm should not selectively close individual channels in order to take advantage of the premium difference between channels when setting an equivalent new business price"). It is a feature of the FCA rules against 'price-walking' which took effect at the start of this year. As above, the provision has not been tested.

3.1.4 Relative operational disadvantage for the customer

This is a form of conflict of interest – addressed for example at [SYSC 10.1.5 G](#). The concept can be illustrated by forms of activity in the capital / wholesale and investment markets. For instance, [COBS 11.3.7A](#) provides that:

"Investment firms shall not carry out a client order or a transaction for own account in aggregation with another client order unless ... it is unlikely that the aggregation of orders and transactions will work overall to the disadvantage of any client whose orders is to be aggregated ... [and such disadvantage] ... is disclosed to each client ... in relation to a particular order ..."

The 2015 fine of [Barclays Bank PLC](#) for FX market misconduct involved trading practices which disadvantaged, or risked disadvantaging, the bank's customers, and gave benefits to the bank - or at least certain of its employees.

3.2 Other FCA guidance

The FCA published [EG22/5](#) by way of non-Handbook guidance alongside [PS22/9](#), which set out the new CD rules and gave feedback on the prior ([CP21/36](#)) consultation responses. Some of the additional guidance contains practical (albeit anonymised) examples of acting (or not) in good faith, including:

"An insurance firm has a complex claims process which deters many customers from pursuing claims ... [including] a requirement for customers to provide hard copies of all evidence. The firm refuses to consider any requests from customers to waive this ... [a] firm should not impose unreasonably restrictive, rigid or arbitrary administrative requirements ..."

By contrast: "A bank identifies where its customers do not have sufficient funds in their accounts to make regular direct debit payments. [It] sends its customers a short, effective communication through its mobile app or via text message ... allowing them time to deposit the funds needed to make payments and avoid additional charges"

4. Legal ramifications

It is possible that arguments may yet develop in both the regulatory and litigation context to the effect that the FCA's rules cause many contracts in the financial services markets to contain duties of good faith as a matter of law, even if the contracts themselves do not contain express provisions in this regard.

The attributes of good faith identified by the FCA for firms party to financial services (product) contracts are similar to the hallmarks of a legal obligation of good faith:

- honesty
- fidelity to the purpose of the contract
- to not use powers for an ulterior purpose

- to deal fairly and openly
- to consider and take into account their own interests while also having regard for the other party's interests

(see eg Unwin v Bond [2020] EWHC 1768 (Comm)).

Good faith in financial services contracts has been recently considered in terms of the 'duty to act rationally': making decisions by taking into account all, and only, matters that should be taken into account and not coming to a conclusion that no reasonable decision maker could ever have come to (see eg UK Acom Finance Ltd v Markel (UK) Ltd [2020] EWHC 922: insurer obliged to act rationally when deciding if it was 'satisfied' that any non-disclosure was unintentional).

While the legal concept of good faith is not generally regarded as unduly demanding, there is the potential for financial services products to have consequences not previously considered.

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