

# Consumer Duty – What does it mean for wholesale firms?

## 1. Speed read

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The FCA published its final rules on the Consumer Duty in a Policy Statement on 27 July 2022 (**PS22/9**) and firms now have until **31 July 2023** to fully implement such rules for new and existing products or services and until **31 July 2024** for closed products or services.

Firms must establish implementation plans by **October 2022**. This briefing discusses implications of the regime for firms engaged in wholesale markets whose products or services may be consumed by UK retail investors.

A separate briefing summarising the basic requirements of the regime is available [here](#).

## 2. Scope: to whom, and when, does the Consumer Duty apply?

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The Consumer Duty applies to UK-authorized firms. Firms not authorised under the Financial Services and Markets Act 2000 (**FSMA**) are not subject to the requirements. A separate briefing regarding the territorial scope of the Consumer Duty and, in particular, its application to third-country firms and outbound services is available [here](#).

The Consumer Duty captures firms that are involved in the manufacture or supply of products and services to retail clients, even where those firms do not have a direct relationship with the retail client. The related guidance indicates that the duty applies where a firm has ‘a material influence over, or determine[s],

*retail customer outcomes*<sup>1</sup> – where it makes, or influences, decisions about the design, operation or distribution of products or services, but not where it operates within a mandate determined by another firm in the chain. This is broadly consistent with the application of product governance requirements under MiFID II (albeit that the Consumer Duty applies to a wider product set than MiFID II).

PRIN 3.2.6R states that the Consumer Duty applies to a firm’s ‘*retail market business*’ only. A firm’s business is retail market business, and therefore within the scope of the Consumer Duty, if it relates to retail clients and does not fall within an exclusion.

<sup>1</sup> Finalised Guidance (FG) 22/5 para 2.13.



Retail clients for these purposes captures the various categories of retail client or customer which fall under the conduct of business requirements applicable across the FCA Handbook. Retail market business excludes the following:

- (a) the manufacture of products not intended for distribution to retail customers (NB that this condition would appear not to be met where UK distribution is limited to non-retail but foreign distribution includes retail);
- (b) activities relating to non-retail financial instruments – those are, in summary:
  - (i) those which carry a disclaimer<sup>2</sup> stating they are not intended for retail customers, provided that the issuer (for primary market activities) or distributor (for secondary market activities) takes reasonable steps to ensure that the offer is not promoted to retail customers; or
  - (ii) those with a minimum denomination or investment amount of £50,000;

(c) acting for the issuer or holder of non-structured -traded instruments<sup>3</sup> in relation to their offer, issue, underwriting, repurchase, exchange or redemption, or variation of terms. The effect of this exclusion is to carve out capital market activities associated with non-structured securities which are admitted to trading on (i) UK regulated markets (including MTFs operated by them), (ii) Recognised Overseas Investment Exchanges (including Deutsche Börse AG, Euronext Amsterdam N.V., Borsa Italiana SpA, Bolsa de Madrid and SIX Swiss Exchange) or (iii) non-UK markets which meet comparable requirements and on which the financial instruments are “*of a quality comparable to those in*” a UK regulated market;

(d) administration of a benchmark, any ancillary activity to that activity and any activities undertaken by a benchmark administrator for the purpose of complying with the Benchmarks Regulation; and

(e) certain activities related to: (i) insurance of non-UK risks; and (ii) insurance activities carried out in respect of group policies.

### 3. What does it mean for wholesale firms?

For wholesale firms, we expect that the Consumer Duty is likely to be largely relevant to structured product business where such products are ultimately sold to retail clients. The FCA has previously called out “poor practice” in the market for structured products and we expect that there will be significant regulatory focus on these types of products given their relative complexity and given the difficulty that retail customers may have in understanding the products.

The duty will impact both distributors and manufacturers of such products. We have distilled the key details on each of the so-called ‘Four Outcomes’ into the table at the end of this briefing which identifies: (a) the high level obligations on manufacturers and distributors under each of the outcomes; and (b) high-level practical guidance for compliance with each outcome. In addition to the Four Outcomes, the table also considers the governance and monitoring requirements imposed under the Consumer Duty.

<sup>2</sup> From a mainstream debt capital markets perspective, the legends used to identify a target market of professionals and eligible counterparties and/or the legends and selling restrictions prohibiting sales to retail under the PRIIPs Regulation are likely to be helpful in this regard.  
<sup>3</sup> A financial instrument meeting all the following criteria: (i) it is when issued, traded or intended to be traded on an RIE or trading venue operated by a regulated market; (ii) it does not involve any actual or potential liability for the investor that exceeds the cost of acquiring the instrument; (iii) it does not incorporate a clause, condition or trigger that could fundamentally alter the nature or risk of the investment or pay out profile, such as investments that incorporate a right to convert the instrument into a different investment or where the return of initial capital invested at the end of the investment period is linked by a pre-set formula to the performance of an index, a combination of indices, a ‘basket’ of selected stocks (typically from an index or indices), or other factor or combination of factors; (iv) it does not include any explicit or implicit exit charges that have the effect of making the investment illiquid even though there are technically frequent opportunities to dispose of, redeem or otherwise realise it; (v) it is not a collective investment scheme or an AIF; and (vi) it is not a structured finance product.



## 4. General approach to wholesale business

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The FCA has been at pains to stress that the impact of the Consumer Duty on wholesale business should be limited. In its feedback to consultation it emphasised that obligations on firms must be interpreted proportionately, in a manner that reflects the firm's role in the distribution chain and its ability to influence retail customer outcomes.

It has given helpful guidance around the relationship between manufacturers and distributors, emphasising that firms are not responsible for the compliance of others and that firms should merely take reasonable steps where distributors with which they deal do not provide information to them.

## 5. Next steps: what do I need to do?

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Although the new regime should be of relatively limited impact across wholesale firms there will need to be a programme of work to ensure it meets the FCA's expectations.

*(a) Create and approve an implementation plan – 31 October 2022.*

The FCA expects firms to have approved an implementation plan by 31 October 2022. For a wholesale firm, this entails assessing which of the obligations apply; conducting a gap analysis against existing processes and controls; and identifying changes needed to meet the requirements. This document should be signed off by the board or branch management.

We have identified in the table below where changes are likely to be needed.

*(b) Communications with other firms in the chain – 30 April 2023*

The new rules will require information to pass down, and up, the distribution chain – particularly in respect of the value assessment. Firms will likely need to commence conducting value assessments in Q1 2023 in order to enable them to communicate with distributors by the 30 April 2023 deadline. To the extent that firms intend to use investor feedback to inform assessments they will also need to commence outreach in advance.

*(c) Implementation with respect to new/open products – 31 July 2023*

*(d) Implementation with respect to closed products – 31 July 2024*

## 6. What can we do for you?

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We are well placed to support you in navigating the process of implementation of the Consumer Duty starting with developing your implementation plan due by October 2022.

To understand more about how we can assist you, please see our **'How we can help you'** guide and should you wish to have a more detailed conversation with one of our specialists, please do get in touch.



more significant compliance uplift expected



compliance uplift may be required in some cases



no compliance uplifted generally expected

	Products and services (PRIN 2A.3)	Price and value (PRIN 2A.4)	Consumer understanding (PRIN 2A.5)	Consumer support (PRIN 2A.6)	Governance and monitoring (PRIN 2A.8/9 – pervades all outcomes)
<b>Manufacturers</b>	<p>Wholesale firms generally have well-developed product governance arrangements in relation to their MiFID business. These should be sufficient to meet the products and services outcomes although firms may wish to revisit their compliance with the relevant parts of the Product Intervention and Product Governance Sourcebook part of the FCA Handbook (<b>PROD</b>).</p>	<p><b>Rules</b></p> <p>Manufacturers must carry out a value assessment of their products which must include the consideration of at least:</p> <ul style="list-style-type: none"> <li>– the nature of the product or service, including the benefits that will be provided or that consumers may reasonably expect, and their quality;</li> <li>– any limitations that are part of the product/service;</li> <li>– the expected total price customers will pay; and</li> <li>– any characteristics of vulnerability in the target market for the product or service.</li> </ul> <p>Manufacturers must consider the fair value assessment at every stage of the product approval process, including in particular when:</p> <p>(i) designing the product; (ii) identifying retail customers in the target market for whom the product needs to provide fair value; and (iii) selecting distributions methods/channels.</p> <p>The final rules contain further guidance on the factors to be considered in making the value assessment.</p> <p>The FCA expects firms to regularly review their value assessments to satisfy themselves that the products and services they manufacture or distribute continue to provide fair value, although the rules do not prescribe a specific form for this assessment.</p>	<p>The consumer understanding outcome applies to firms involved in the production, approval or distribution of retail communications. Generally speaking, this outcome will be less relevant to wholesale manufacturers. To the extent that the manufacturer is producing materials that will be provided to retail customers (e.g. a prospectus or KID), see details in row below.</p>	<p>The consumer support outcome applies to all firms responsible for interacting directly with and providing support to retail customers. Generally speaking, unless a manufacturer is in a position where it expects to communicate directly with a customer, we anticipate that manufacturers will not need to take action under this outcome.</p>	<p><b>Rules</b></p> <p>Both manufacturers and distributors must ensure, among other things, that:</p> <ul style="list-style-type: none"> <li>– the Consumer Duty obligations are reflected in their strategies, governance, leadership and people policies, including incentives at all levels;</li> <li>– the four outcomes are a central focus of their risk control framework and the internal audit function;</li> <li>– they monitor the outcomes retail customers are experiencing from their products;</li> <li>– they prepare a report for the board with details of such monitoring; and</li> <li>– their board reviews such report on an annual basis and takes action to address risks or failings identified and to ensure the business strategy remains consistent with the Consumer Duty.</li> </ul> <p>Manufacturers that do not have contact with retail customers should: (i) monitor the outcomes of the service they provide; (ii) consider the information they already have about consumer outcomes; and (iii) take steps to obtain relevant information about such outcomes.</p> <p>In relation to the products and services outcome, any monitoring carried out under PROD may be used to comply with Consumer Duty.</p>

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<b>Manufacturers</b>		<p><b>Practical guidance</b></p> <p>To a large extent, the assessment of value in relation to a structured product involves an inherent assumption as to the market risk that a customer will take on. Providing customers exposure to such market risk necessarily involves certain costs to a manufacturer (e.g. hedging cost and origination costs). To some extent the value assessment should therefore already be part of the well-developed product governance frameworks that manufacturers have in place.</p> <p>The additional requirements under the Consumer Duty are likely to therefore build on this framework and provide an additional layer of governance and formality.</p> <p>In order to meet the value assessment requirements a manufacturer will need to:</p> <p>(a) create a value assessment policy (VAP), to cover:</p> <ul style="list-style-type: none"> <li>(i) arrangements for co-manufacture (allocation of responsibility);</li> <li>(ii) triggers for conducting a value assessment;</li> <li>(iii) the process to be followed for the generation of the value assessment;</li> <li>(iv) inputs (see item (c) below);</li> <li>(v) sign-offs;</li> <li>(vi) generation and reporting of relevant management information;</li> <li>(vii) review;</li> <li>(viii) post-review actions: mitigation, notification and redress; and</li> <li>(ix) dissemination to distributors (this would not have to include sensitive information such as a breakdown of margins/ risk-based pricing);</li> </ul>			<p><b>Practical guidance</b></p> <p>In order to ensure compliance with the governance and monitoring requirements under the Consumer Duty, both manufacturers and distributors should:</p> <ul style="list-style-type: none"> <li>(a) engage the board in the design of the Consumer Duty programme (NB the requirement to approve an implementation plan by the end of October);</li> <li>(b) design a framework to monitor consumer outcomes, escalate details of such monitoring (both positive and negative) and take appropriate action where issues are identified;</li> <li>(c) update relevant policies and procedures, management information flows and board/ committee agendas to include relevant details of the Consumer Duty compliance programme and monitoring framework referred to in items (a) and (b) above;</li> <li>(d) reflect Consumer Duty objectives in staff incentives (including remuneration), performance management and conduct requirements; and</li> <li>(e) establish a procedure for annual reporting to the board of Consumer Duty failings.</li> </ul>

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<b>Manufacturers</b>		<p>(b) embed the VAP in the new product design and approval processes (including launches of product packages, if relevant) and post-sale review process (both periodic and on any amendment to a product); and</p> <p>(c) create a framework for the assessment of fair value, to include:</p> <ul style="list-style-type: none"> <li>(i) product characteristics;</li> <li>(ii) benefits (financial and non-financial);</li> <li>(iii) quality;</li> <li>(iv) total price (accounting for any ancillary costs and charges); and</li> <li>(v) nature of clients (segmenting groups within the target market, if necessary).</li> </ul>			
<b>Distributors</b>	See row above.	<p><b>Rules</b></p> <p>Distributors must ensure that they do not distribute products or services unless they are satisfied that their distribution arrangements are consistent with the product or service providing fair value.</p> <p>Practical guidance</p> <p>Distributors will also need to develop a VAP broadly in line with that described above. To do this, they must obtain information from the manufacturer to understand the intended value of the product or service.</p> <p>As well as considering product information shared by the manufacturer, a distributor should also consider the following in its VAP:</p> <ul style="list-style-type: none"> <li>(a) the impact that distribution arrangements, including remuneration, can have on value in the context of the product; and</li> <li>(b) the impact of investor feedback on its assessment of value.</li> </ul>	<p><b>Rules</b></p> <p>Firms involved in the production, approval or distribution of retail customer communications must ensure, among other things, that they:</p> <ul style="list-style-type: none"> <li>– support retail consumer understanding so that their communications: (i) meet the information needs of customers; (ii) are likely to be understood by the average customer intended to receive the communication; and (iii) equip customers to make decisions that are effective, timely and properly informed;</li> <li>– communicate information to retail customers in a way which is clear, fair and not misleading;</li> <li>– tailor communications by taking into account the characteristics of the retail customers intended to receive the communication (including any characteristics of vulnerability), the complexity of the product, the communication channel used, and the role of the firm;</li> </ul>	<p><b>Rules</b></p> <p>Firms responsible for interacting directly with and providing support to retail customers are required to ensure that they, among other things:</p> <ul style="list-style-type: none"> <li>– provide an appropriate standard of support to retail customers such that it meets the needs of customers, including those with characteristics of vulnerability;</li> <li>– ensure retail customers can use products as reasonably anticipated;</li> <li>– include appropriate friction in their customer journeys to mitigate the risk of harm and give retail customers sufficient opportunity to understand and assess their options, including any risks; and</li> </ul>	See row above.



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<b>Distributors</b>			<p>– tailor communications to meet the information needs of individual customers and check the customer understands the information, where appropriate, when a firm is interacting directly with a customer on a one-to-one basis; and</p> <p>– monitor, test and adapt communications to support understanding and good outcomes for retail customers.</p> <p><b>Practical guidance</b></p> <p>In order to meet the consumer understanding requirements, a firm should:</p> <p>(a) identify where it makes retail customer communications;</p> <p>(b) review existing policies and procedures on disclosure to retail investors;</p> <p>(c) assess changes needed to</p> <ul style="list-style-type: none"> <li>(i) meet information needs,</li> <li>(ii) be comprehensible and</li> <li>(iii) support effective decisions by target market; and</li> </ul> <p>(d) consider conducting market testing.</p>	<p>– ensure retail customers do not face unreasonable barriers (including unreasonable additional costs) when they want to pursue their financial objectives.</p> <p><b>Practical guidance</b></p> <p>In order to meet the requirements under the consumer support outcome, a firm should:</p> <p>(a) identify the channels through which it provides support to retail customers;</p> <p>(b) review existing policies and procedures concerning support provided to retail customers;</p> <p>(c) assess the changes needed to: (i) identify characteristics of vulnerability and service those needs appropriately; (ii) ensure sufficient friction in customer journeys; and (iii) assist customers in avoiding barriers such as additional costs where appropriate; and</p> <p>(d) consider conducting market testing of consumer support outcomes.</p>	

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