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Consumer Finance

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FCA to Further Investigate Motor Finance Commission

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The New Consumer Duty has been described as a "paradigm shift" by the FCA. But what will it actually do? In this alerter, we consider the duty in the context of mortgages and cryptoasset advertising - two of the issues of the day - as well as the broader picture of actionability of the new duty, which will apply to all firms affected.

BACKGROUND

1. In March 2019 the Financial Conduct Authority (FCA) published a report entitled "Our work on motor finance – final findings" (**the 2019 Report**). It included a detailed analysis of the various commission structures which were commonly in place between motor finance lenders and credit intermediaries such as car dealers and third-party brokers.

2. The FCA's overarching conclusion was that commission arrangements operating in the motor finance sector could lead to consumer harm, in particular, by lenders' reliance upon 'difference-in-charges' commission structures, also referred to as 'discretionary commission arrangements' (**DCA(s)**). Under a DCA, the lender gives the car dealer/credit broker a discretion (within limits) as to the interest rate that will apply to the finance deal offered to the customer – and the higher the interest rate, the greater the commission. It found that very few intermediaries properly complied

with the obligations under CONC 4.5.3R in the FCA Handbook to disclose the fact of commission[1] and, where necessary, that lenders were failing in their duty under CONC 1.2.2R[2] to take reasonable steps to ensure that they did.

3. In consequence of the 2019 Report, CONC 4.5 was amended on 28 January 2021. A ban was introduced on the use of DCAs and brokers were required to disclose not only the "existence" but also the "nature" of any other form of commission received.

4. Since those regulatory interventions motor finance commission 'mis-selling' litigation has become ubiquitous in the County Court. Claims are commonly made for bribery, for procuring a breach of the dealer/credit broker's alleged fiduciary duty, for breach of statutory duty under the Financial Services and Markets Act 2000 and/or for relief from an unfair relationship under the Consumer Credit Act 1974.

5. Following two final decisions of the Financial Ombudsman Service (**FOS**), on 11 January 2024, the FCA released a public statement confirming its decision to intervene in the motor finance market with immediate effect (**the Announcement**).

OMBUDSMAN DECISIONS IN 'L' AND 'Y'

6. On 10 January 2024 FOS published two very similar final decisions, respectively upholding complaints by 'Mrs Y' against Black Horse Limited and

[1] An obligation that applies when the existence or amount of commission "could actually or potentially: (1) affect the impartiality of the credit broker in recommending the credit agreement or the consumer hire agreement; or (2) if made known to the customer, have a material impact on the customer's transactional decision to enter into the credit agreement or the consumer hire agreement".
[2] "A firm must: (1) ensure that its employees and agents comply with CONC; and (2) take reasonable steps to ensure that other persons acting on its behalf comply with CONC."

'Miss L' against Clydesdale Financial Services Limited (**together, the Decisions**).

7. Both concerned allegations of unfairness in the parties' credit relationship arising from the lender's payment to a credit broker of commission calculated on a DCA without the complainant's knowledge. In both cases, the lender's position was that it had complied with all applicable legal and regulatory requirements and, in any event, the interest rates on the agreements were fair and competitive.

8. In summary, in both cases the complaints were upheld based on the ombudsman's view that:

   a. The use of a DCA *"created an inherent conflict between the interests of the Broker and the interests of [the complainant], as it gave the Broker an incentive to set a higher interest rate than [the lender] would have accepted so that the Broker received more commission."*

   b. The use of DCAs meant the lenders had failed to comply with the guidance at CONC 4.5.2G and Principle 6 to have due regard to the complainants' interests and treat them fairly.

   c. On the facts, a Court would be likely to find an unfair relationship between the parties under s.140A of the Consumer Credit Act based upon (i) the operation of the commission model, (ii) the inequality of knowledge and understanding between the parties, and (iii) the broker's failure to comply with CONC 4.5.3R.

   d. In light of all circumstances, the lenders did not act fairly towards the complainants.

9. Both Decisions recommended that the lender pay redress based upon the difference between the interest rate in fact charged and the lowest rate in its agreed range. Although they acknowledged the possibility that the

complainants may not have in fact been able to obtain the lowest rate, absent any evidence what other rate might have been available, the ombudsman considered that it was a fair approach based upon *"the only certainty"*.

THE ANNOUNCEMENT & PS 24/1

10. Immediately following the publication of the Decisions, on 11 January 2024 the FCA released the Announcement on its website.

11. The Announcement notes the *"high number of consumer complaints"* and claims in the County Court seeking compensation for commission arrangements in place prior to the January 2021 ban on DCAs. It contrasts lenders' routine rejection of most commission complaints, with views set out in the Decisions and the fact that *"some"* County Court claims by consumers have been upheld.

Skilled persons reviews under s.166 FSMA

12. In light of that position, the Announcement confirms the FCA's use of its powers under s.166 of the Financial Services and Markets Act 2000 *"to review historic motor finance commission arrangements and sales across several firms."*

13. S.166 is headed *"Reports by skilled persons"*. Amongst other matters, it empowers the FCA to require any authorised person to *"provide information or product documents with respect to any matter"* (subs.(1)) with a view to appointing *"a person to provide… a report on the matter concerned"* (subs.(3)(b)). The person providing such report *"must be a person appearing to the [FCA] to have the skills necessary to make a report on the matter concerned"* and be either *"nominated or approved by the [FCA]"* (subs.(6)). Where such skilled person is appointed the firm under investigation to give them *"all such assistance as [they] may reasonably require"* (subs.(7)), enforceable by way of injunction (subs.(8)).

14. Thus, the Announcement makes clear that the FCA – prompted by the volume of complaints and claims – has resumed active investigation into firms' historic use of DCAs. Insofar as they have not already been put in place, skilled persons will be appointed to investigate firms' practices and report to the regulator.

15. SUP 5.3.1 in the FCA Handbook gives guidance on the regulatory policy governing the use of the FCA's powers under s.166. Given the historic nature of the issue, however, it seems most likely that it is being deployed for one or both of the following reasons. First, to diagnose and monitor potential issues with firms' handling of such complaints. Secondly, with a view to *"remedial action"* in relation to historic failures – in other words, with a view to enforcement and sanction.

Pause on complaints-handling

16. In conjunction with the reference to its ongoing use of s.166 powers, the Announcement confirms the FCA's decision to immediately, and without consultation, pause the 8-week deadline for responding to customer complaints relating to DCAs. The pause will last for approximately 9 months and applies to any complaint received by firms between 17 November 2023 and 25 September 2024.

17. In conjunction, the deadline for consumers to refer such complaints to FOS will be 15 months, rather than the usual 6. The extension will apply to any complaint for which a final response was or is sent between 12 July 2023 and 20 November 2024.

18. These changes have now been enshrined with immediate effect by amendments to the DISP module of the FCA Handbook.

19. Further detail on the FCA's view of these matters is found in Policy Statement "PS24/1" (**PS 24/1**), also published on 11 January 2024. It refers to the need for urgent *"diagnostic work"* to address, in particular, *"whether firms' conduct means large number of consumers are owed redress"* (para 1.18). Pending completion of that work, however, the FCA is understandably unwilling to commit to what, if anything, will be the consequence.

20. It also identifies at length the risk of *"disorderly"*, *"inconsistent"* and *"inefficient"* outcomes for consumers as a result of a sudden escalation in complaints and claims. The regulator's ultimate objective is said to be (para 1.44):

> "to ensure that consumers who have been harmed by motor finance arrangements with [discretionary commission arrangements], and provided with appropriate redress from firms in an orderly, consistent and efficient manner and in a way that protects and enhances market integrity."

21. Crucially PS 24/1 confirms that, even while the pause is in effect, the rule at DISP 1.4.1R continues to apply. Thus, firms must continue *"to assess and investigate complaints promptly and diligently."* This means that the FCA encourage firms to continue to *"progress"* motor finance commission complaints by *"investigating and collecting evidence that could help with their eventual resolution."*

22. Thus, the pause must not be treated as a basis to simply 'down tools' and ignore consumer complaints relating to DCAs. Indeed, given the probable escalation in the volume of such complaints over the coming weeks and months, firms would be well-advised to keep momentum to avoid a deluge once the period of pause comes to an end.

THE FUTURE

23. The Announcement publicly signals the FCA's view that its 2019 Report and subsequent amendments to CONC 4.5 were not sufficient. The next phase is to commence investigation into individual firms' historic practices in order to ensure fair and consistent complaints-handing, with a view to enforcement action as necessary. This is potentially at odds with what anecdotal evidence suggests has been the comparatively receptive view of judges in litigation, even in the context of the unfair relationship provisions of the CCA.

24. Thus, the publication of Decisions and the Announcement in quick succession in the now shows that we are nowhere near the end of issues arising from historic motor finance commission arrangements. Indeed, we are more probably merely at the 'end of the beginning'.

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