

The Responsibilities of Providers and Distributors for the Fair Treatment of Customers (RPPD)

This Annex sets out the text of the new Regulatory Guide “The Responsibilities of Providers and Distributors for the Fair Treatment of Customers”. All the text is new and is not shown underlined.

Introduction

- 1.1 In this Regulatory Guide ("Guide") we give our view on what the combination of Principles for Businesses ("the Principles") and detailed rules require respectively of providers and distributors in certain circumstances to treat customers fairly. However, it is not, and does not seek to be, a complete exposition of all of a provider's or a distributor's responsibilities to the customer or to each other; nor does it alter, replace or substitute applicable Principles, rules, guidance or law, such as those relating to unfair contract terms (Note (1)).
- 1.2 A customer's experience should not be affected by whether a product or service was provided and distributed by a single institution or by two or more institutions.
- 1.3 This Guide is guidance issued under section 157 of the Financial Services and Markets Act 2000 ("the Act"). As such, it is not binding on those to whom the Act and rules apply and need not be followed in order to achieve compliance with rules or other requirements. There is no presumption that departing from this Guide indicates a breach of a rule. However, the Guide may be relevant in an enforcement context, for example to explain the regulatory context. If a person acts in accordance with the Guide in the circumstances contemplated by the Guide, then the FSA will not take action against that person in relation to the aspects of the rules to which the Guide relates. The Guide will also be a useful tool for supervisors, particularly when they deal with TCF issues at firms. Supervisors may use the Guide in their discussions with firms. The issues it covers will continue to be dealt with in our supervision work as they are now, for example in the risk assessment framework we use for supervising firms (ARROW) or in pieces of focused thematic work.

The applicable rules

- 1.4 Under the Principles (Note (2)), providers and distributors of products and services have various responsibilities that have an impact on customers. Detailed rules within the FSA Handbook further specify what these responsibilities are in certain defined circumstances.
- 1.5 The Principles apply to all authorised firms. This Guide looks particularly to the following Principles (Note (3)):
 - Principle 2 ('A firm must conduct its business with due skill, care and diligence');
 - Principle 3 ('A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems');

- Principle 6 ('A firm must pay due regard to the interests of its customers and treat them fairly'); and
- Principle 7 ('A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading').

1.6 What a firm has to do to meet the requirements of a Principle will depend on the circumstances, including the riskiness or complexity of the product or portfolio, who the firm is dealing with (another firm or a customer, for example) and the financial sophistication of the target market (Note (4)). Firms should bear all of these factors in mind in order to interpret the requirements of the Principles in a way that is proportionate. The responsibilities described in this Guide apply to the extent that the Principles themselves apply.

Scope

1.7 This Guide is intended to be relevant to all regulated firms involved in the supply of products or services to retail customers. Although we have drafted it to be of particular relevance where there is more than one firm in the supply chain, many of the responsibilities described in the Guide are also relevant where there is only one firm involved in providing and distributing a product or service. Our intention is not to change the existing responsibilities of providers or distributors in delivering fair outcomes for consumers. Rather, it is to articulate the existing regulatory responsibilities. Nor does this Guide seek to determine or change whether or how consumers can seek redress in any individual case or from which firm in the supply chain. This Guide does not determine or change whether or how one firm in a distribution chain may seek redress from another firm; this too will depend on the circumstances of the case.

1.8 The supply chain may not comprise only authorised firms, but this Guide does not deal with the position where an unauthorised firm is involved unless expressly stated otherwise. Where there is a non-U.K. element to the supply chain, the Guide only applies to the extent that the Principles themselves apply.

1.9 This Guide is not intended to imply that a firm must take on the regulatory responsibilities of other firms in the distribution chain nor that there is a requirement for any firm to 'police' any other firm in the chain.

Interpretation

1.10 In this Guide we use 'must' where an action is required by a Principle or detailed Rule. We use 'should' where we think a firm ought to consider a particular action (not specified in a Principle or Rule) at a reasonably high level to comply with a Principle (not that they should follow a detailed or prescribed course of action). We use 'may' where an action is only one of a number of ways of complying with a Principle.

1.11 Where we refer to the 'customer' in this Guide we use it as a convenient name for the end-customer in the retail supply chain (which may include potential customers). However, it is important to note that the term 'customer' as used in the Principles or

detailed rules themselves is a defined term in the FSA Handbook. This Guide does not seek to alter or affect any definitions within the Handbook.

- 1.12 We use 'provider' to include persons who offer services such as portfolio management (through distributors or otherwise) as well as those who develop, manage or package products such as life insurance, general insurance or investment products or who develop or enter into home finance transactions (i.e. mortgages, home reversion plans and home purchase plans).
- 1.13 We use 'distributor' to mean those persons who then make up the rest of the supply chain taking the product or service to the customer. This could include, for example, financial advisers, third party administrators, appointed representatives, banks, building societies, and those who sell insurance as a secondary part of their business.

The responsibilities

- 1.14 Providers and distributors should consider the impact of their action (or inaction) on the customer in various stages of the product life-cycle, or the various stages of provision of the service (Note (5)). Depending on the precise nature of a firm's business, this could mean addressing the fair treatment of customers at the following stages: design and governance; identifying target markets; marketing and promotion; sales and advice processes; after-sales information and service; and complaints handling. This Guide gives our view of the respective responsibilities of providers and distributors under the Principles during the product life cycle or while the service is provided.
- 1.15 In this Guide we have distinguished between providers and distributors. While we consider the labels 'provider' and 'distributor' useful for the purposes of this Guide, we recognise that responsibilities flow from the actual roles or functions undertaken in a transaction, and firms should take this into account in considering their responsibilities under the Principles. In considering which responsibilities apply to it, a firm should consider the functions and roles that it undertakes in the product life-cycle. Whether a particular role or function is fulfilled by the distributor or provider (or both) may vary based on the product or service, or particular arrangements in place, and it may be possible for a firm to act as both provider and distributor at the same time in respect of different products or services. For example:
- (1) It is possible that a provider creates a product or service to meet criteria or designs specified by a distributor. In such instances, many of the responsibilities fall to the commissioning distributor, as 'retail manufacturer' of the product (Note 6)) or service (Note 7)), rather than the 'pure manufacturer' of the commissioned product or service. Of course, if what the pure manufacturer delivers fails to meet the agreed specification, the retail manufacturer may seek its own redress under the contract between them or the applicable law. That said, the pure manufacturer must act with due skill, care and diligence in accordance with Principle 2 and, where it conducts a regulated activity for the underlying customer (for example, it enters into a contract with a customer), must treat that customer fairly. Other Principles and detailed rules may also apply.

- (2) It is also possible that a product manufacturer creates components that are later (and possibly without the component manufacturer's knowledge) subsumed into retail products designed and marketed to customers by 'retail manufacturers'. In such instances, the pure manufacturer may not have a contractual or other relationship with the underlying customer. The pure manufacturer may not be aware (nor is it necessarily the case that it ought to be aware) of whether the retail manufacturer is using the product for itself or for an underlying customer. However, the pure manufacturer should act with due skill, care and diligence in designing its products (Principle 2). The skill, care and diligence that are 'due' under Principle 2 will be determined taking all the circumstances into account. These may include the manufacturer's knowledge of whether the product or service is provided to a firm, rather than an underlying customer, and the information needs of the firm. In addition, the pure manufacturer will normally be obliged to communicate information to the retail manufacturer in a way that is not misleading (Principle 7) (Note (8)).

1.16 Whether providers and distributors can agree between themselves how to apportion responsibilities between themselves will depend on the circumstances. In particular, it depends on the nature of the regulatory responsibility, the extent to which such an agreement would be reasonable, whether the arrangement is clear to both parties and properly recorded and the systems and controls used to monitor whether the agreement continues to be appropriate in the circumstances.

Provider responsibilities (Note (9))

1.17 **When undertaking product or service design, Principles 2, 3 and 6 are particularly relevant.** In particular, a firm:

- (1) should identify the target market, namely which types of customer the product or service is likely to be suitable (or not suitable) for;
- (2) should stress-test the product or service to identify how it might perform in a range of market environments and how the customer could be affected;
- (3) should have in place systems and controls to manage adequately the risks posed by product or service design (Note (10)).

1.18 **When providing information to distributors, Principle 2 is particularly relevant.** In particular, a firm:

- (1) should make clear if that information is not intended for customer use;
- (2) should ensure the information is sufficient, appropriate and comprehensible in substance and form, including considering whether it will enable distributors to understand it enough to give suitable advice (where advice is given) and to extract any relevant information and communicate it to the end customer. As part of meeting this standard, the provider may wish to consider, with regard to each distribution channel or type of distributor, what information distributors of that type already have, their likely level of knowledge and understanding, their information needs and what form or medium would best

meet those needs (which could include discussions, written material or training as appropriate).

1.19 When providing information to customers (Note (11)), Principles 3, 6 and 7 are particularly relevant. In particular, a firm:

- (1) should pay regard to its target market, including its likely level of financial capability;
- (2) should take account of what information the customer needs to understand the product or service, its purpose and the risks, and communicate information in a way that is clear, fair and not misleading (Note (12));
- (3) should have in place systems and controls to manage effectively the risks posed by providing information to customers.

1.20 When selecting distribution channels, Principles 2, 6 and 7 are particularly relevant. In particular, a firm:

- (1) should decide whether this is a product where customers would be wise to seek advice;
- (2) should review how what is occurring in practice corresponds to (or deviates from) what was originally planned or envisaged for the distribution of its products or services given the target market. This involves collecting and analysing appropriate Management Information (MI) (Note (13)) such that the firm can detect patterns in distribution as compared with the planned target market, and can assess the performance of the distribution channels through which its products or services are being distributed;
- (3) should act when it has concerns, for example by ceasing to use a particular distribution channel.

1.21 In the area of post-sale responsibility, Principles 2, 6 and 7 are particularly important. In particular, a firm:

- (1) in supplying information direct to the customer, must ensure that the information is communicated in a way which is clear, fair and not misleading (Note (14));
- (2) should periodically review products whose performance may vary materially to check whether the product is continuing to meet the general needs of the target audience that it was designed for, or whether the product's performance will be significantly different from what the provider originally expected and communicated to the distributor or customer at the time of the sale (Note (15)). If this occurs, the provider should consider what action to take, such as whether and how to inform the customer of this (to the extent the customer could not reasonably have been aware) and of their option to seek advice, and whether to cease selling the product;

- (3) should communicate to the customer contractual 'breakpoints' such as the end of a long tie-in period that may have a material impact on a customer that the customer cannot reasonably be expected to recall or know about already;
- (4) should act fairly and promptly when handling claims or when paying out on a product that has been surrendered or reached maturity. In doing this, the provider should meet any reasonable customer expectations that it may have created with regard to the outcomes or how the process would be handled;
- (5) must establish, implement and maintain effective and transparent customer complaint-handling systems.

Distributor responsibilities

1.22 In the area of financial promotions, Principles 3, 6 and 7 are particularly relevant. In particular, a firm:

- (1) should have in place systems and controls to manage effectively the risks posed by financial promotions;
- (2) in passing on a promotion created by a provider, must act with due skill, care and diligence. A firm will not contravene the financial promotions rules where it communicates a promotion produced by another person provided the firm takes reasonable care to establish that another firm has confirmed compliance with the relevant detailed rules, amongst other matters (Note (16)).

1.23 When providing information at or before the point of sale to a customer, Principles 2, 6 and 7 are particularly relevant. In particular, a firm:

- (1) should consider, when passing provider materials to customers, whether it understands the information provided (Note (17));
- (2) should ask the provider to supply additional information or training where that seems necessary to understand the product or service adequately;
- (3) should not distribute the product or service if it does not understand it sufficiently, especially if it intends to provide advice;
- (4) when providing information to another distributor in a distribution chain, should consider how the further distributor will use the information, such as whether it will be given to customers. Firms should consider what information the further distributor requires and the likely level of knowledge and understanding of the further distributor and what medium may suit it best for the transmission of information.

1.24 When advising on selection of a provider, Principles 2 and 6 are particularly relevant (Note (18)). In particular, a firm:

- (1) should consider the nature of the products or services offered by the provider and how they fit with the customer's needs and risk appetite;

- (2) should consider what impact the selection of a given provider could have on the customer in terms of charges or the financial strength of the provider, or possibly, where information is available to the distributor, how efficiently and reliably the provider will deal with the distributor or customer at the point of sale (or subsequently, such as when queries/complaints arise, claims are made, or a product reaches maturity).

1.25 **In the area of post-sale responsibility, Principles 3 and 6 are particularly relevant.** In particular, a firm:

- (1) should comply with any contractual obligation it has to the customer, for example to provide ongoing advice or periodic reviews. In connection with this, it should also consider its responsibility to maintain adequate systems and controls to deliver on such reviews;
- (2) should consider any implied or express representation it made (during meetings, correspondence or promotional material, for example). Where a customer has reasonable expectations based on the prior statements of a distributor, for example that performance will be monitored, the distributor should meet these expectations;
- (3) where involved in handling claims or paying out on a product that has been surrendered or reached maturity, should meet any reasonable expectations that the distributor has created in the customer's mind with regard to how the process would be handled;
- (4) must establish, implement and maintain effective and transparent customer complaint-handling systems;
- (5) should pass any communications received from customers (intended for or suited to providers to act upon) to providers in a timely and accurate way.

Notes:

- (1) The Guide represents our view based on the law, regulation and other circumstances that exist as at the publication date, but also takes into account changes to the Handbook including those to implement the Markets in Financial Instruments Directive (MiFID) that have already been made or consulted on and are due to come into force on 1 November 2007. (*Paragraph 1.1*)
- (2) The Principles are set out in PRIN 2. (*Paragraph 1.4*)
- (3) Of course, other Principles apply as appropriate. For example, under Principle 9, a firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment. (*Paragraph 1.5*)
- (4) PRIN 1.2.1G. (*Paragraph 1.6*)

- (5) For example, many brokers and investment managers have on-going relationships with intermediaries by virtue of which their services are provided to the intermediary's underlying clients. (*Paragraph 1.14*)
- (6) For example, an insurer could be commissioned by a distributor to create a payment protection insurance product where the criteria for the product are specified by the distributor. (*Paragraph 1.15(1)*)
- (7) For example, a portfolio manager could be commissioned to develop a branded service specifically for a distributor where the criteria for the service are specified by the distributor. (*Paragraph 1.15(1)*)
- (8) Principle 2 may not apply to a pure manufacturer that is a MiFID investment firm in certain circumstances, for example in relation to eligible counterparty business: see PRIN 4 for further guidance. In some circumstances Principles 6 and 7 will apply even when the retail manufacturer is the only client of the pure manufacturer. (*Paragraph 1.15(2)*)
- (9) As explained in paragraph 1.15, although we use the terms 'provider' and 'distributor' we recognise that responsibilities flow from the actual roles or functions undertaken by a firm. (*Paragraph 1.17*)
- (10) For example, SYSC (Senior Management Arrangements, Systems and Controls). (*Paragraph 1.17(3)*)
- (11) This includes providing information to distributors for onward transmission to customers. (*Paragraph 1.19*)
- (12) For example, COBS 4 (Communicating with clients, including financial promotions); ICOB 3.8 (Form and content of non-investment financial promotions); MCOB 3.6 (Form and content of non-real time qualifying credit promotions); MCOB 3.8A (Form and content of financial promotions of home reversion plans); MCOB 2.2.6AR (Clear, fair and not misleading promotions for home purchase plans). (*Paragraph 1.19*)
- (13) See, for example, SYSC 3.2.11 -12. See also TCF cluster report on TCF considerations for Management Information:
http://www.fsa.gov.uk/pages/Doing/Regulated/tcf/pdf/management_info.pdf
(*Paragraph 1.20(2)*)
- (14) For example, COBS 4 (Communicating with clients, including financial promotions), ICOB 2.2.3R (Clear, fair and not misleading communication), MCOB 2.2.6R (Clear, fair and not misleading communication). (*Paragraph 1.21(1)*)
- (15) For example, SYSC 3.2.11G (Management information); SYSC 3.2.17G (Business Strategy). (*Paragraph 1.21(2)*)
- (16) COBS 4.10.10R, ICOB 3.7.5R, MCOB 3.9.5R (Communicating a financial promotion where another firm has confirmed compliance). This exemption is not available in relation to MiFID or equivalent third country business.

(Paragraph 1.22(2))

- (17) For regulated activities other than designated investment business, a firm must take reasonable steps to communicate information in a way that is clear, fair and not misleading (e.g. ICOB 2.2.3R and MCOB 2.2.6R). In doing so, it may be reasonable for a distributor to rely on information produced by a provider unless the distributor is, or ought to be, aware of grounds to question its compliance. For designated investment business, a firm must ensure that any communication to a client is fair, clear and not misleading regardless of whether it has been produced by a provider (COBS 4.2.1R). The standard for designated investment business is an absolute standard, which does not permit reliance unless an exemption applies. *(Paragraph 1.23(1))*
- (18) These Principles are also relevant for non-advised sales, where there may be a need to consider a customer's needs and circumstances, for example see COBS 10 (Appropriateness (for non-advised services)), COBS 7.2.4R (Specifying demands and needs), ICOB 4.4 (Statement of demands and needs). *(Paragraph 1.24)*