UCONN
LIBRARY

University of Connecticut
OpenCommons@UConn

Connecticut Insurance Law Journal | School of Law

2014

Payment Protection Insurance (PPI) Misselling: Some Lessons From the UK

Andromachi Georgosouli

Follow this and additional works at: https://opencommons.uconn.edu/cilj

Part of the Insurance Law Commons

Recommended Citation
Georgosouli, Andromachi, "Payment Protection Insurance (PPI) Misselling: Some Lessons From the UK" (2014). *Connecticut Insurance Law Journal*. 140.
https://opencommons.uconn.edu/cilj/140

PAYMENT PROTECTION INSURANCE (PPI) MISSELLING: SOME LESSONS FROM THE UK

ANDROMACHI GEORGOSOULI

***

The misselling of Payment Protection Insurance ("PPI") is a longstanding problem in the UK. The Treating Customers Fairly ("TCF") initiative was introduced to tackle this problem but, despite its sophisticated inception, its effectiveness has been limited. This Article canvasses the main features of TCF as a management-based approach to regulation and highlights its initial appeal. Against this backdrop, it draws on the recent UK experience with recurring instances of PPI misselling to offer an account of the principal causes of its shortcomings in the retail financial sector. It argues that the perceived failure of this regulatory approach may be attributed to the following three factors: (i) the rulification of TCF; (ii) several shortcomings of the existing data resource management; and (iii) the absence of a system of credible deterrence to support the Financial Conduct Authority's attempts to be proactive and to inflict cultural change at regulated firm level. The Article concludes with a summary of key lessons that may be drawn from the UK experience.

***

I. INTRODUCTION

Financial misselling describes selling practices in the retail financial sector that exploit the customer's reliance on the expertise, advice, and professionalism of the provider of the financial product or service in question. Typically, it is a deliberative strategy to sell financial products that customers do not need.[1] Financial misselling has a long

---

*Dr Andromachi Georgosouli (a.georgosouli@qmul.ac.uk), Centre for Commercial Law Studies, QMUL. I am grateful to the University of Connecticut Insurance Law Centre for granting me a generous honorarium for writing up this Article. Further, I wish to thank Patricia McCoy, Sharona Hoffman, and the participants of the Workshop 'Big Data and Insurance' of the University of Connecticut Insurance Law Centre (Hartford, Connecticut, 3 April 2014) for useful comments and, also, to extend a special thanks to Miriam Goldby for feedback on

history in the UK. In the 1990s, misled workers pulled out of company final-salary pension schemes and enrolled in plans that were linked to stock market returns.[2] During the same period, mortgage endowment policies and Card and Identity Protection Insurance ("CIPI") were missold to consumers.[3] The misselling of Payment Protection Insurance ("PPI") has perhaps been worse.[4] It started off in the 1980s and has been recurring ever since.[5] In view of its magnitude, this Article will focus on the regulatory response to PPI misselling as a case study.

---

an earlier version of this Article and to Matteo Angelini for his assistance. Any errors are my own.

[1] Practices of predatory lending in the US are similar but not identical to financial misselling in the UK. A major difference concerns the locus of these phenomena. The majority of predatory lending has been associated with the subprime sector. In the UK, financial misselling occurs in the mainstream retail financial sector. *See* Richard V. Ericson & Aaron Doyle, *The Institutionalization of Deceptive Sales in Life Insurance: Five Sources of Moral Risk*¸ 46 BRIT. J. CRIM. 993, 993–1010 (explaining the impact on the life insurance sector by financial misselling in the US through empirical studies); Nicole L. Fuentes, *Defrauding the American Dream: Predatory Lending in Latino Communities and Reform of California's Lending Law*, 97 CALIF. L. REV. 1279, 1279–1335 (2009) (discussing predatory lending in the United States); SYNOVATE LTD., CONSUMER MARKET STUDY ON ADVICE WITHIN THE AREA OF RETAIL INVESTMENT SERVICES – FINAL REPORT (2011), *available at* http://e.c.europa.eu/consumers/archive/rights/docs/investment _advice_study_en.pdf (providing investment advice to 27 member states of the EU).

[2] Nearly one million of them eventually won compensation totaling £11.8 billion. FIN. SERVS. AUTH., NATIONWIDE AVC & PENSION SCHEME INTEREST RATE FINAL RETURNS, *available at* http://www.fsa.gov.uk/static/pubs/fsavc-review/fsavc-bs-returns.pdf.

[3] *Card and Identity Protection Policyholder to Claim Compensation by 30 August 2014*, FIN. CONDUCT AUTH. (Mar. 3, 2014), http://www.fca.org.uk/news/compensation-for-card-and-identity-protection-policyholders; *see also* FIN. SERVS. AUTH., ENDOWMENT MORTGAGE COMPLAINTS: FEEDBACK ON CP75 AND 'FINAL' TEXT (2001), *available at* http://www.fsa.gov.uk/pubs/policy/ps75.pdf.

[4] *See* Luis Lobo-Guerrero, Uberrima Fides, *Foucault, and the Security of Uncertainty*, 26 INT'L J. SEMIOTICS L. 23, 31–32 (2013) (explaining the practice of PPI misselling and its history in the UK).

[5] Julia Black & Richard Nobles, *Personal Pensions Misselling: The Causes and Lessons of Regulatory Failure*, 61 MOD. L. REV. 789, 789–820 (1998) (pointing out that misselling is one of the key drivers that led to reform of the system of financial regulation in the late 1990s); James Pickford, *PPI Dominates as Consumer Complaints*

PPI provides insurance against the risk that a borrower will be unable to maintain credit repayments for specified reasons as, for example, when he is unable to work or due to an accident.[6] PPI is not suitable for everyone. Suppose, for instance, that X is applying for a loan in order to buy a car. He is perfectly healthy, he is educated, and his family can help him out financially if he finds himself temporarily out of work in the future. He does not need a PPI, but he is forced to buy PPI. For example, he is told that it is better to purchase PPI, because otherwise he will have to pay an increased interest for the loan that he is applying for. In other instances, it may be the case that PPI goes together with a personal loan (or a mortgage) as a compulsory component, but customers are never alerted of that fact.

The predecessor of the Financial Conduct Authority ("FCA") on matters of consumer protection and conduct of business – the Financial Services Authority ("FSA") – made PPI misselling an early priority when it assumed responsibility for the regulation of general insurance intermediation in 2005.[7] Initially, the FSA tried to work with the industry. The Treating Customers Fairly initiative ("TCF") stood at the epicentre of the regulator's approach and it was launched in 2006 with the aim of intensifying the FSA's attempt to attune business culture with the delivery of fair treatment for customers as part of its consumer protection mandate.[8]

The TCF is sophisticated in its inception, but thus far has proved to be ineffective in deterring instances of financial misselling. Between 2006 and 2008, selling practices in the retail financial sector revealed poor suitability checks and training, ineffective systems and controls, and

---

Hit Record High, FIN. TIMES (May 19, 2014), http://www.ft.com/cms/s/0/24610976-df6d-11e3-a4cf-00144feabdc0. html#axzz38gfKumLG.

[6] *See* Ellis Ferran, *Regulatory Lessons from the Payment Protection Insurance Mis-selling Scandal in the UK*, 13 EUR. BUS. ORG. L. REV. 247, 250 (2012) (providing various working definitions of PPI); Final Notice from Fin. Servs. Auth. to Lloyds TSB Bank plc and Bank of Scotland plc (Feb. 15, 2013), *available at* http://www.fca.org.uk/static/fca/documents/final-notices/ lloyds-banking-group.pdf.

[7] FIN. SERVS. AUTH., TREATING CUSTOMERS FAIRLY AFTER THE POINT OF SALE 7 (2001), *available at* http://www.fsa.gov.uk/pubs/discussion/dp7.pdf; Clive Briault, Managing Dir. Retail Markets, Fin. Servs. Auth., Treating Customers Fairly: Progress and Future Plans at the FSA Treating Customers Fairly Conference (Oct. 4, 2005) (transcript *available at* http://www.fsa.gov.uk/library/communication/speeches/2005).

[8] *See infra* pp. 8–12 (discussing the nature of TCF).

inadequate provision of information to customers. There were also problems with the resolution of disputes, the taking of disciplinary action, and delays in the provision of financial redress. For example, it was not until the second half of 2011 that large-scale redress of past misselling began. Things do not seem to have improved.[9] In July 2014, a new set of complaints about "another PPI scandal" hit the news this time challenging the capabilities of the new regulator – the Financial Conduct Authority – to do a better job than its predecessor.[10] As it transpired, more than 60,000 small businesses were missold fixed-rate business loans to protect them against interest rate changes without being informed that a swap was added to the transaction or that the swap could possibly have the reverse effect.[11]

These introductory remarks give rise to the following question: Why is TCF failing to deliver? In this Article, I will attempt to offer an answer to this question. I will start with a brief account of the legal underpinnings and the nature of the TCF. Against this background, I will try to demonstrate that the shortcomings of this approach may be attributed to a combination of the following three factors: (a) the rulification of TCF namely a regulatory strategy that was originally conceived as informal, flexible, and responsive in nature; (b) certain flaws in the data resource management that is currently in place to facilitate the electronic reporting of PPI related data and other conduct of business and consumer protection issues; and (c) the absence of a system of credible deterrence to back up proactive intervention that aims to inflict cultural change and to attune business ethics with the delivery of public policy objectives – here, that of fair treatment for customers.

These parameters do not exhaustively account for all of those market, institutional, legal, behavioural, and cognitive conditions that inhibit the effective implementation of TCF. Poor standard setting, capture, creative compliance, the implementation of a regime of corporate governance regulation that falls short of providing rewards for the delivery of good quality of services to retail financial customers, and the level and nature of competition in the relevant industry are only some of a plethora of other considerations that could be enlisted as factors that circumscribe the effectiveness of TCF. However, in view of space constraints, the purpose of this Article is not to offer a comprehensive account of all the causes of

---

[9] *See infra* pp. 14–24 (examining the main causes).

[10] Adrian Quine, *Banks Face New Mis-selling Scandal*, BBC NEWS (Jul. 3, 2014), http://www.bbc.co.uk/news/business-28037608.

[11] *Id.*

the TCF failings, but to discuss those of them that, in the opinion of the author, have not received the attention they deserve.

II. THE REGULATION OF PPI: A BRIEF OVERVIEW OF THE LEGAL FRAMEWORK

Pre-crisis, the Financial Services Authority was the single UK mega-regulator with a wide range of powers at its disposal. Consumer protection was one of the four FSA statutory objectives under the Financial Services and Markets Act ("FSMA") 2000.[12] The other three were market confidence, financial stability, and the reduction of financial crime.[13] The Financial Services Act 2012 changed this. As of April 2013, the FSA was abolished and replaced by the Financial Conduct Authority ("FCA") and the Prudential Regulation Authority ("PRA"), the latter being a subsidiary of the Bank of England.[14] The FCA and the PRA are focus-specific with a separate set of statutory objectives to deliver. They are operationally independent and at least on paper of equal institutional standing. The strategic objective of the FCA is to ensure that financial markets function well.[15] To this effect, the FCA is responsible for consumer protection, market integrity, and competition in the interests of consumers.[16] The PRA is the primary micro-prudential regulator and part of its mandate is to offer a helping hand to the Financial Policy Committee of the Bank of England in delivering its financial stability objective.[17]

Despite their distinct institutional standing, the statutory objectives of the PRA and the FCA are not exclusive to the regulatory agency that they are attached to. This is particularly evident in relation to the regulation of the insurance sector for the purposes of policyholder

[12] *See* Financial Services and Markets Act, 2000, c. 8, § 5 (U.K.).

[13] *Id.* at §§ 1(3), 6, 26(1)(a), 3, 3A, 9 (showing that the fifth objective, "public awareness," § 4, was eventually omitted by virtue of amendments that were introduced under §§ 2(3) and 26(3) of the Financial Services Act, 2010 (Commencement No. 1 and Transitional Provision) Order 2010, S.I. 2010/2480, 2)).

[14] Andromachi Georgosouli, *The FCA-PRA Coordination Scheme and the Challenge of Policy Coherence*, 8 CAP. MARKETS L.J. 62, 62–65 (2013).

[15] Financial Services Act, 2012, c. 1, § 1B(2) (U.K.) (amending Financial Services and Markets Act 2000).

[16] *Id.* at §§ 1B(2), 1(C), 1D, 1E, 3 (promoting consumer protection, market integrity, and competition).

[17] *Id.* at § 2B ("The PRA's general objective").

protection. Granted that policyholders are a sub-group of consumers, one would expect that their protection would fall within the remit of the FCA in view of the FCA's statutory objective of consumer protection. However, the UK legislator opted for a more complex route. The Financial Services Act 2012 entrusts the protection of policyholders to the PRA and not the FCA, presumably to highlight the fact that the protection of this special group of consumers is a matter of prudential regulation calling primarily for solvent and sound insurance firms.[18] Nevertheless, the FCA complements the work of the PRA. The tackling of PPI misselling, in particular, falls within the competence of the FCA, given its primary responsibility on matters of conduct of business, part of which is the fair treatment of customers.

A combination of primary and secondary legislation alongside common law doctrines on contract, agency, and tortuous liability comprises the regulation of PPI. Until recently, the regulation of consumer credit fell under the province of the Office of Fair Trading ("OFT") under the Consumer Credit Act ("CCA") 1974.[19] Credit agreements financed PPI premiums under CCA, while the writing and marketing of the policies were regulated under the FSMA, causing unnecessary overlaps and inconsistencies.[20] As of April 2014 and in light of amendments to the Financial Services and Markets Act 2000, which were introduced by the Financial Services Act 2012, the FCA is now the regulator of consumer credit, taking over the responsibilities of the OFT and thus bringing consumer credit firms under its consumer and conduct of business mandate.[21]

---

[18] *Id.* at § 2C ("Insurance objective").

[19] *See* Consumer Credit Act, 1974, c. 39, §§ 1(1), 3 (U.K.).

[20] *See* Consumer Credit Act, 2006, c. 37 §§ 9(4), 20(1), 60, 61, 54 (U.K.). *See generally* Consumer Credit (Total Charge for Credit), 2010, S.I. 2010/1011, 4 (U.K.) (TCC Regulations); Consumer Credit (Agreements), 2010, S.I. 2010/1014 (U.K.); Financial Service Act (Consumer Credit), 2013, Stat. R. & O. 2013/1882 (U.K.) (transferring regulatory powers from the Office of Fair Trading to the Financial Conduct Authority, which became responsible for consumer credit as of April 2014); *see also* Eva Lomnicka, *The Future on Consumer Credit Regulation: A Chance to Rationale Sanctions for Breaches of Financial Services Regulatory Regimes*, 34 COMPANY LAW., 13, 13 (2013) (documenting the problems with the previous regime).

[21] FIN. CONDUCT AUTH., CONSUMER CREDIT SOURCEBOOK (2014), *available at* http://fshandbook.info/FS/html/FCA/CONC (setting out the main rules for those firms providing consumer credit).

Not unlike the FSA, the FCA has a wide range of disciplinary and enforcement powers at its disposal.[22] Some of them are discussed in further detail later.[23] For the time being and as a general remark, it is important to note that the FCA has, *inter alia*, the power to (a) impose administrative fines, (b) withdraw authorisation and permissions, (c) apply for injunctions and restitution orders, and (d) prosecute certain criminal offences.[24] Of particular relevance to the tackling of PPI misselling is new section 138D (former section 150) establishing a civil law remedy for the aggrieved party to seek compensation,[25] sections 225 to 233 setting out the role of the Financial Ombudsman Service ("FOS") in handling consumer complaints and in granting compensation where appropriate, and section 404 on consumer redress schemes.[26] To ensure that the regulator's disciplinary action will be visible enough to have an impact on the conduct of market actors, new section 391 (1ZB) also enables the FCA to publish information about warning notices in certain cases.[27] On paper, this looks like a significant departure from the previous regime, under which the earliest that the FSA could publish details of a disciplinary matter was when it issued a final notice at the conclusion of a case (e.g., after the Tribunal had reached a decision). In reality, the effect of this amendment must not be blown out of proportion. A careful reading of the relevant provision reveals that the regulator must, *inter alia*, consult with the person to whom the notice is given. In addition, the FCA's power to publish information

---

[22] *See* Financial Services and Markets Act, 2000, Part XI (amended 2012) (U.K.), for the disciplinary powers of the FCA. *See id.* at Part XIV for the powers of FCA to gather information and conduct investigation.

[23] *See infra* note 30 and accompanying text.

[24] *See* FIN. CONDUCT AUTH., ENFORCEMENT INFORMATION GUIDE (2013), *available at* http://www.fca.org.uk/your-fca/documents/enforcement-information-guide.

[25] Only "private persons" are eligible to make use of this statutory civil law remedy. *See* Financial Services and Markets Act 2000 (Rights of Actions), 2001, S.I. 2001/544 (U.K.); Titan Steel Wheels Ltd. v. The Royal Bank of Scot. PLC, [2010] EWHC (Comm) 211, [76] (Eng.) (finding a corporation did not qualify to bring an action under § 150 of the FSMA because it was acting in the course of business); Figurasin v. Cent. Capital Ltd., [2014] EWCA (Civ) 504 (Eng.).

[26] These are to be read in conjunction with the Consumer Redress Schemes Sourcebook (CONRED) of the FCA Handbook. *See generally* FIN. CONDUCT AUTH., CONSUMER REDRESS SCHEME SOURCEBOOK (CONRED) (2014), *available at* http://fshandbook.info/FS/html/FCA/CONRED.

[27] *See* Financial Services Act, 2012, c. 21, § 37 (U.K.).

about warning notices is restricted by virtue of section 391(6), which prohibits the FCA from publishing information when the publication would be (a) unfair to the person against whom that action was proposed to be taken; (b) prejudicial to the interests of consumers; or (c) detrimental to the stability of the UK financial system.

Secondary legislation adds a further layer of detail with regard to the conduct of business in the retail financial sector and the procedural aspects of supervision, compliance, and enforcement.[28] Of particular relevance here is the Insurance Conduct of Business Sourcebook ("ICOBS"). This constitutes a more concrete statement of the FCA Principles for Businesses and comprises the main body of rules and guidance that underpins the conduct of business of insurance services providers.[29] Alongside general and transitional provisions, the ICOBS sets out, *inter alia*, the details regarding the identification of, and provision of advice to, clients (chapter 5), product information, including PPI requirements (chapter 6), cancellation rights (chapter 7), and claims handling (chapter 8). Further, and with respect to the selling of PPI, firms are under the legal obligation to establish the eligibility of the customer in question (ICOBS, 5.1.2R) and to bring to the customer's attention the importance of reading the policy contract documentations prior to the expiry of the period of cancellation (ICOBS, 6.4.5R).[30] Finally, the FCA Handbook contains a comprehensive set of rules and guidance on dispute resolution and complaints handling, including the handling of PPI complaints.[31]

III. THE NATURE OF TCF AND THE GROUNDS THAT INFORMED ITS IMPLEMENTATION

Under Principle 6 (customers' interests) of the FCA Principles for Businesses, "a firm must pay due regard to the interests of its customers

---

[28] *See* FIN. CONDUCT AUTH., INSURANCE: CONDUCT OF BUSINESS SOURCEBOOK ch. 5–6 (2014), *available at* http://media.fshandbook.info/ content/full/ ICOBS.pdf.

[29] The Principles for Businesses are set out in PRIN 2.1.1 and they are identical to the FSA High Level Principles for Business. FIN. CONDUCT AUTH., PRINCIPLES OF BUSINESS § 2.1.1 (2014), *available at* http://fshandbook.info/ FS/html/FCA/PRIN/2/1.pdf.

[30] FIN. CONDUCT AUTH., s*upra* note 28, ch. 5–8.

[31] FIN. CONDUCT AUTH., DISPUTE RESOLUTION: COMPLAINTS §§ 1.3, 3, app. 3 (2014), *available at* http://fshandbook.info/FS/html/FCA/DISP.

and treat them fairly." In pursuance of this Principle, TCF asks the industry to work out for itself what practices guarantee fair treatment for clients in a manner that is attuned to the policy goals and priorities of the regulator. These goals are encapsulated in the following six TCF outcomes:[32]

"Outcome 1: Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture.

Outcome 2: Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.

Outcome 3: Consumers are provided with clear information and are kept appropriately informed before, during, and after the point of sale.

Outcome 4: Where consumers receive advice, the advice is suitable and takes account of their circumstances.

Outcome 5: Consumers are provided with products that perform as firms have led them to expect, and the associated service is of an acceptable standard.

Outcome 6: Consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim, or make a complaint."

TCF is not a new set of secondary legislation. It is a guidance that reflects key elements of the UK regulator's strategy in the retail financial sector. The outcomes that firms are expected to deliver are communicated through informal means as, for example, Policy Statements ("PS") and "Dear CEO Letters." From this, however, it does not follow that this otherwise informal guidance has no bearing on the taking of enforcement action.[33] Indeed, the six TCF outcomes enlisted above do not stand in isolation from the FCA Handbook, despite the fact that strictly speaking they do not form part of secondary legislation.[34] For all intended purposes,

---

[32] *See* FIN. SERVS. AUTH., TREATING CUSTOMERS FAIRLY – A GUIDE TO MANAGEMENT INFORMATION (2007), *available at* http://www.fca.org.uk/firms/being-regulated/meeting-your-obligations/fair-treatment-of-customers.pdf.

[33] Ferran, *supra* note 6, at 259 (characterizing the TCF outcomes as "non-binding guidance").

[34] John Tiner, Address at the Ins. Sector Conference (Sept. 21, 2006), *available at* http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2006/0320_jt.shtml.

they echo the FCA Principles for Businesses.[35] Further, they are linked to a range of other Handbook provisions in the sense that they constitute a set of more concrete benchmarks against which compliance is to be assessed.

Arguably, TCF can be described as a management-based approach to regulation.[36] It combines elements of performance-based and process-oriented strategies whereby the focus is on processes, systems and controls, internal management, and the monitoring of performance in delivering tangible outcomes pertaining to the fair treatment of customers. Quite often, the management-based, performance-based, and process-oriented approaches to regulation are used interchangeably in the literature, but for systematic purposes, it is important to highlight some key differences. In the case of management-based regimes, firms are expected to develop plans and monitoring systems for the delivery of certain public policy objectives. Accordingly, compliance is assessed in terms of whether the implemented systems and controls are fit for purpose. Process-oriented regulation focuses on the firms' engagement in a process of comprehensive self-evaluation, design, and management of their business. Finally, performance-based regulation constitutes an extension of principles-based regulation in the sense that it focuses on the attainment of outcomes, leaving the regulated population to decide how best these can be achieved.

Similar to the approach that was adopted by its predecessor, the FCA's intervention takes the form of a combination of proactive and reactive measures. The purpose of proactive measures is to mitigate the risk that the customers of a specific firm will not be treated fairly. Reactive intervention typically takes the form of disciplinary and enforcement action, the aim of which is primarily to provide some sort of redress to the aggrieved party and to deter future misconduct. Over the years, there has been a clear preference for proactive intervention and industry engagement (e.g. through road shows, working with the industry, mystery shopping, etc.), while enforcement has been generally regarded as a measure of last resort.

---

[35] These were formerly labelled as the FSA High-Level Principles of Business. FIN. CONDUCT AUTH., *supra* note 29.

[36] *See* Andromachi Georgosouli, *The FSA's Treating Customers Fairly (TCF) Initiative: What is so Good About it and Why it May Not Work*, 38 J.L.S. 405, 410 (2011); Cary Coglianese & David Laser, *Management-Based Regulation: Prescribing Private Management to Achieve Public Goals*, 37 LAW & SOC'Y REV. 691, 693–694 (2003) (considering the distinction between management-based, process-oriented and performance-based approaches).

Specifically, in pursuing its proactive intervention agenda, the UK regulator has the power to take a range of intrusive measures with respect to issues such as the allocation of resources and competences, the nature of staff training, and the kind of remedial action that may be deemed necessary in the event of a customer complaint. Moreover, the regulator has a comprehensive toolkit to attune business culture and patterns of self-governance to match TCF targets.[37] For example, the "product life-cycle" is a regulatory device that guides firms in their attempt to align their TCF strategy with the priorities and the expectations of the FCA from the early stages of planning and production through to after-sale services. Other regulatory measures that work in a similar fashion include the FCA's Culture framework, which intends to help firms build TCF into their culture, and Management Information ("MI"), the purpose of which is to make it easier for senior managers to keep things in perspective when managing data, while making it possible for the FCA to get a more accurate view of the firms' capacity to deliver TCF outcomes.[38]

The regulator's reactive intervention essentially reflects its strategy of compliance and enforcement. The case of Alliance & Leicester ("A&L") is a classic example not least because it set the tone of the regulator's policy of compliance and enforcement that is still implemented today.[39] A&L was ordered to pay the biggest fine for serious failings in the selling of PPI pre-crisis.[40] However, A&L also agreed to implement a customer contract programme overseen by third-party accountants. Under

---

[37] *Alliance and Leicester to Pay £7 million Fines for PPI Failings*, FIN. SERVS. AUTH. (Oct. 7, 2008), *available at* http://www.fsa.gov.uk/library/communication/pr/2008/115.shtml; Georgosouli, *supra* note 33, at 415–16.

[38] *TCF Culture*, FIN. CONDUCT AUTH. (Apr. 5, 2013), http://www.fca.org.uk/firms/being-regulated/meeting-your-obligations/fair-treatment-of-customers/Culture; FIN. SERVS. AUTH., TREATING CUSTOMERS FAIRLY – TOWARDS FAIR OUTCOMES FOR CONSUMERS (2006), *available at* http://www.fca.org.uk/static/ fca/documents/fsa-tcf-towards.pdf.

[39] Georgosouli, *supra* note 36, at 416.

[40] A&L was fined £7,000,000. Post crisis, financial firms were made to pay much higher fines. *See* Press Release, Fin. Cond. Auth., FCA Fines Lloyds Banking Group First a Total of £28,038,800 for Serious Sales Incentive Failings (Nov. 12, 2013), *available at* http://www.fca.org.uk/news/press-releases/fca-fines-lloyds-banking-group-firms-for-serious-sales-incentive-failings; Final Notice from Fin. Conduct Auth. to Lloyds TSB Bank plc and Bank of Scotland plc (Dec. 10, 2013), *available at* http://www.fca.org.uk/your-fca/documents/final-notices/2013/lloyds-tsb-bank-and-bank-of-scotland.

this programme, A&L undertook, amongst other things, to contact all customers that purchased PPI in conjunction with an unsecured loan, to review its policy in respect of product information that was sent to these customers, to review any rejected complaints and claims, and to pay redress where appropriate. A&L demonstrates that, at least in theory, the regulator's enforcement strategy goes beyond penalizing unacceptable forms of business conduct. The offender's failure to comply with TCF is seen as an opportunity for the offender to reflect on what went wrong and make things right by taking remedial action, revising processes, practices, and ultimately its corporate culture.[41] This approach survived the upheaval of regulatory reform in the aftermath of the recent financial crisis and it is now crystallised in various dispute resolution provisions of the FCA Handbook. Accordingly, it remains a key element of the regulator's strategy.[42]

---

[41] *See* Howard Becker, *Culture: A Sociological View*, 71 YALE REV. 513 (1982) (describing culture as shared understandings that permit a group of people to act in concert with each other); Roger Cotterrell, *Law and Culture – Inside and Beyond the National State*, 31 NORDIC J.L. & JUST. 23, 23–36 (2008) (Nor.) (identifying four cultural components namely 'beliefs/values', 'traditions', 'instrumental matters' (economic, technological) and 'matters of effect' (emotions)); Justin O'Brien et al., *Culture and the Future of Financial Regulation: How to Embed Restraint in the Interests of Systemic Stability*, 8 L. & FIN. MARKETS REV. 115, 126 (2014) (identifying five sources of cultures); Jasper Sorensen, *The Strength of Corporate Culture and Reliability of Firm Performance*, 47 ADMIN. SCI. Q. 70, 72 (2002) (offering a narrow definition of culture as a system of shared values).

[42] FIN. CONDUCT AUTH., *supra* note 31, at 2, 4 (2014) (reflecting the recommendations made by the FSA in FIN. SERVS. AUTH., THE ASSESSMENT AND REDRESS OF PAYMENT PROTECTION INSURANCE COMPLAINTS (2009)); FIN. SERVS. AUTH., THE ASSESSMENT AND REDRESS OF PAYMENT PROTECTION INSURANCE COMPLAINTS §§ 3.26, 4.7 (2009), *available at* http://www.fsa.gov.uk/pubs/cp/cp09_23.pdf (recommending firms to proactively reassess all complaints and consider whether a wider redress programme would be appropriate, namely one which would include the proactive redress of PPI customers who have not complained); H. Osborne, *PPI Mis-Selling: Banks to Write to up to 12 Million Customers,* GUARDIAN (March 6, 2012), http://www.theguardian.com/money/2012/mar/06/ppi-misselling-banks-write-customers.

In implementing the TCF agenda, the FCA is further assisted by the Financial Ombudsman Service ("FOS").[43] Although it is not the purpose of this Article to examine the powers and role of the FOS as a guardian of best practice in the retail financial sector, it is important to note that its involvement goes beyond dispute resolution and consumer redress. FOS decisions are instrumental in the cultivation of a common understanding of what TCF entails in practice. They inform the interpretation of TCF requirements and, in the long run, they provide guidance on the expected level of performance in delivering fair treatment to customers.

Several considerations informed the decision of the UK regulator to implement TCF.[44] As with any other typical scheme of management-based regulation, TCF embraces self-regulation. This makes it morally appealing because it subscribes to a vision of the regulatory community, the members of which are assumed to be capable of working out for themselves the public standards that ought to govern their relationships. Self-regulation also tends to create a sense of legitimacy, as it bears out standards of conduct that are made by the industry and for the industry, albeit under the watchful eye and quasi-approval of the regulator.

The management-based and performance-oriented elements in TCF also have the potential to tackle a series of persistent problems that are associated with the old-school 'command and control' regulation. Examples include those of creative compliance, the cost of rulemaking and enforcement, lack of flexibility, and problems of over and under inclusiveness.[45] As the argument goes, the articulation of a specific set of outcomes helps firms concentrate on what matters, namely performance in delivering certain goals rather than sticking to the letter of the law. The informal means of communicating the regulator's TCF expectations are

---

[43] In the past, FOS alerted the UK regulator about emerging trends concerning poor standards of conduct of business practices and the case for regulatory action. *See* FIN. CONDUCT AUTH., COMPLAINT HANDLING PROCEDURES OF THE FINANCIAL OMBUDSMAN SERVICE (2014), *available at* http://fshandbook.info/FS/html/FCA/DISP/3.

[44] See Georgosouli, *supra* note 36, at 417–420, for a more detailed discussion.

[45] On the limitations of rules as instruments of social organisation and control see generally JULIA BLACK, RULES AND REGULATORS ch. 1 (1997); Colin Diver, *The Optimal Precision of Administrative* Rules, 93 YALE L.J. 65 (1983) (approaching the matter from a law and economics perspective); Doug McBarnet & Christopher Whelan, *The Elusive Spirit of the Law: Formalism and the Struggle for Legal Control*, 54 M.L.R. 848 (1991).

also thought to be more flexible and less time consuming. Moreover, they arguably place the regulator in a better position to obtain crucial and timely information that is essential for the formation of judgments with respect to compliance, the expediency of enforcement action, and even the case for reform.

TCF also affords a more participatory and discursive approach to regulation. The latter carries with it the promise of being more effective in aligning the industry's perceptions with the goals and views of the regulator.[46] As the argument goes, long-term cultural change is more likely to happen with industry engagement, not least because in this manner, the regulatees are expected to become more cognizant of their responsibilities in delivering TCF outcomes and also more sophisticated in sensing what TCF requires even in the presence of new or unforeseen circumstances. Moreover, regulatees who are given the chance to decide how best to proceed in their attempt to incorporate TCF into their business culture are more likely to view it as reasonable and thus worthy of compliance. Finally, by granting firms the flexibility to develop their own strategies, TCF enables firms to experiment and seek out better and more innovative solutions.

Finally, there are several advantages to note in relation to the FCA's policy of reactive intervention in the context of the TCF initiative. The desirability of enforcement action is assessed in light of its likely impact on the industry's capacity to develop patterns of self-regulation. It is forward-looking in the sense that it aims to educate the regulated industry and to encourage a change of culture.[47] Being partly premised on negotiation, the enforcement procedure itself creates opportunities for the alleged offender to deliberate with the regulator, become cognizant of its failure to comply, remedy any wrongdoing, and revise its business practice where appropriate.

---

[46] See Black, *supra* note 45, at 37–44, for a classic exposition of the nature of conversational regulation. See also Andromachi Georgosouli, *Regulatory Interpretation: Conversational or Constructive?*, 30 O.J.L.S. 361, 361–84 (2010), for a critical evaluation of the view of regulation as conversational.

[47] *See* Sorensen, *supra* note 41, at 15.

IV. TRACING THE CAUSES OF THE TCF FAILURE TO DETER PPI MIS-SELLING

A. THE RULIFICATION OF TCF

In its original inception, TCF departs from the traditional rulebook approach. It seems to be based on the belief that, in the absence of rules, problems like, for example, that of legal uncertainty – vanish automatically. However, the reality is different. Legal certainty may no longer be a function of the design of rules, but it is certainly contingent to the informal means through which regulatory expectations are communicated. Judging from past experience, the text of these informal means of communication is no less authoritative than the content of the FCA Handbook. In the case of TCF, informal communication failed to convey with clarity the regulator's expectations.[48]

One would expect that the informal and flexible nature of TCF would compensate for the perceived legal uncertainty surrounding its implementation, but this is not what happened. By and large, firms have been reluctant to take initiative and exercise the level of discretion that was delegated to them. They preferred more detailed regulatory guidance. Conversely, when they did exercise discretion, the outcomes were not to the regulator's satisfaction. In view of this, TCF soon evolved into a rulified regime.[49] The response of the UK regulator was a conspicuous proliferation of detailed and legally binding rules and guidance. In 2007, in particular, and after repeated failings to combat misconduct, the UK regulator introduced more detailed ICOBS rules[50] in the name of clarity and certainty.[51] At the same time though, it continued to communicate its expectations regarding TCF through informal guidance.

Indeed, the UK regulator did not give up the idea of self-regulation as the main conduit of change in the business culture of retail firms. In this spirit, it reassured the industry that the changes in the ICOBS did not amount to a 'command and control' approach and that informal communications and non-legally binding guidance would continue to be

---

[48] *See* FIN. SERVS. AUTH., *supra* note 32.

[49] See Frederick Schauer, *The Tyranny of Choice and the Rulification of Standards,* 14 J. CONTEMP. LEGAL ISSUES 803 (2004), for a general discussion.

[50] *See supra* pp. 7-8 (discussing new ICOB rules).

[51] *See infra* pp. 20–24 where formal enforcement is discussed in the context of credible deterrence.

relied upon. This was thought appropriate to allow for a degree of flexibility that would make possible for firms to develop patterns of self-regulation, however, legal uncertainty remained an issue.[52] So did the firms' reluctance to commit to the ideal of self-regulation.[53]

B. TCF AND THE CRUCIAL ROLE OF 'BIG DATA'

The implementation of TCF requires increasing capacity to collect and process data, as, for example, for the purposes of managing emerging risks as a preventive measure, or for the purposes of effective enforcement. The UK regulator recommends the Management Information ("MI") framework as a tool for the management and processing of data.[54] Essentially, MI standardises the process of collecting information during a period of business activity with respect to key issues that are of relevance to TCF. It makes it easier for managers to put information in perspective and align it with the regulator's expectations. Furthermore, the data collected serves as evidence of the firm's capacity to meet performance targets.

The data that is produced and accumulated at the level of each regulated firm is then fed into the regulatory system via GABRIEL (Gathering Better Regulatory Information Electronically).[55] The latter is an online reporting platform for the collection, validation and storage of data. The nature of the data that a firm is expected to report to the FCA via GABRIEL varies. In any case, it depends on the regulated activities that the firm undertakes and the prudential category into which the firm is classified. GABRIEL makes a special reporting provision for PPI related data. This signifies the importance of data collection and processing as a necessary precondition for the timely identification of TCF-related risks and, where appropriate, for the taking of disciplinary action.

Although, both the MI and the special PPI reporting through GABRIEL are welcome developments, they are subject to limitations. There is no doubt that MI makes it easier for firms to deal with a tangible problem, that of information management and the associated cost of

---

[52] *See* Andromachi Georgosouli, *Judgment-led Regulation: Reflections on Data and Discretion*, 14 J.B.R. 209, 210 (2013).

[53] *See infra* p. 24.

[54] The FSA introduced the MI framework. FIN. SERVS AUTH., *supra* note 32, 4.

[55] *See generally GABRIEL*, FIN. CONDUCT AUTH. (Aug. 26, 2014), http://www.fca.org.uk/firms/systems-reporting/gabriel.

processing an ever-growing volume of information.[56] However, this is as far as it goes. MI cannot guarantee the reliability of the data that is made available to the regulator. The data that is eventually channelled through the regulator's system of decision-making is as good as the data produced at regulated firm level.

As we learn from empirical studies on the use of big data by the medical professions in the US, there are several pitfalls and shortcomings in the process of electronic reporting.[57] Apart from errors due to software failures, problems may occur as a result of typing quickly, ticking the wrong boxes, or copying and pasting out-dated or otherwise wrong information.[58] To the extent that the reporting forms allow for the addition of free text, contradictions may also occur between the content of the free text and the content of the standard text. There is no reason to think that the electronic reporting systems that are currently deployed by the industry and the FCA are immune from shortcomings like those reported in the medical profession.

The accumulated data is the product of self-assessment exercises, which are riddled with human bias. For example, firm employees are unlikely to disclose non-favourable information, especially when there is a little chance that the regulator will ever find out about this.[59] Similarly, they are unlikely to pass on information that is harmful to them or their fellows. Human judgement is also subject to "automation" bias namely the tendency to disregard information which contradicts information that is generally accepted as correct.[60] Last but not least, the reward and incentive structure

---

[56] *See*, however, PRICEWATERHOUSECOOPERS, INTELLIGENT MANAGEMENT AND COMPLIANCE COST REDUCTION 10–12 (2008) (demonstrating that management-based regulation is expensive in its implementation).

[57] *See, e.g.*, Sharona Hoffman & Andy Podgorski, *The Use of Biomedical Data: Is Bigger Really Better?* 39 AM. J.L. & MED. 497, 499–502 (2013). Nevertheless, the authors point out that digitalization can prevent some data quality problems, such as those associated with illegible handwriting.

[58] *Id*. at 515–16, 519–20.

[59] *See* John C. Coffee Jr., *Beyond the Shut-Eyed Sentry: Toward a Theoretical View of Corporate Misconduct and an Effective Legal Response*, 63 VA. L. REV. 1099, 1146, 1242 (1977).

[60] *See generally* Steven T. Schwarcz & David E. Wallin, *Behavioural Implications of Information Systems on Disclosure Fraud*, 14 BEHAV. RES. IN ACCT. 197 (2002) (arguing that the use of computer data increases the likelihood of this pattern of behaviour).

of firms gives rise to another type of bias namely, the "self-serving bias".[61] This describes the tendency to interpret ambiguous information in a manner that is favourable to one's self.

The quality of information may be further compromised due to certain structural features of the electronic reporting system – most notably that of data fragmentation. In the case under examination, it is interesting to note, for example, that the special PPI reporting requirement applies only to those firms that have been asked to provide monthly data on specific PPI management information.[62] The rest must follow the usual path and submit electronically information that is classified as data pertaining to product sales, complaints handling, etc. This differential treatment that is reflected in terms of 'who' is to submit PPI-related data makes sense especially when seeing through the lens of risk-based regulation, according to which resources should be directed in priority to the monitoring of those firms that pose a higher risk to the delivery of TCF outcomes. However, this approach can be problematic.

Data that is submitted for the purposes of reporting on product sales and complaints handling can also be PPI-sensitive despite the fact that it is not earmarked as such at the time of its submission to GABRIEL. Accordingly, a danger here is that its PPI-relevance will escape the regulator's attention. There is an additional issue of concern here. Due to its structural features, GABRIEL is bound to produce more data for those firms that are already put under the spotlight because they present a higher risk of failure to meet TCF targets. Conversely, GABRIEL is expected to produce less data for the purposes of proactive intervention and in particular with respect to lower risk retail financial services providers whose business culture may nevertheless call for attention as it may not be compatible with TCF goals in the long run. The suboptimal production of data for the purposes of proactive intervention is not a trivial matter. It is liable to undermine the regulator's attempt to map out the prevailing business culture of the firm in question accurately and to decide appropriate course of action in a timely fashion.

---

[61] *See generally* Jeffrey Rachlinski, *The Uncertain Psychological Case for Paternalism*, 97 NW. U. L. REV. 1165, 1172–73 (2003) (offering a classification of various types of self-serving bias).

[62] FIN. CONDUCT AUTH., PAYMENT PROTECTION INSURANCE (PPI) REPORTING FORM (2014), *available at* http://www.fca.org.uk/firms/systems-reporting/ppi-reporting-forms.

The UK regulator has not done enough to put in place inter-operable data systems and take steps to ensure that collected data is integrated into a single data. This could ameliorate the difficulties that are associated with data fragmentation.[63] For example, the so-called Integrated Regulatory Reporting ("IRR") does not serve as a universally integrated system of data resource management.[64] It does harmonize inconsistent reporting formats, but its scope of application is very limited. On the one hand, it is calibrated to comply with the transparency requirements of the Capital Requirements Directive ("CRD") and the Markets in Financial Instruments Directive ("MiFID").[65] On the other hand, it applies to a very specific group of regulated firms, namely investment management firms, securities and futures firms, and firms that enter into regulated mortgage contracts or administer regulated mortgage contracts.[66]

The problem of data fragmentation is further exacerbated by the fact that the FCA and the PRA collect data separately.[67] Although the two regulators are expected to share information along the lines of a Memorandum of Understanding, delays and turf wars cannot be precluded over sensitive information.[68] Furthermore, the two regulators may not necessarily share the same view when they assess whether a piece of information should be brought to the attention of the other regulator in the first place or as a matter of priority.

---

[63] *See generally* Hoffman & Podgorski, *supra* note 57, at 517–518 (discussing the harms and causes of incomplete or fragmented data).

[64] FIN. CONDUCT AUTH., FCA-PRA COMBINED HANDBOOK § 16.12 (2014), *available at* http://fshandbook.info/FS/html/handbook/SUP/16/12 (making IRR mandatory); *see also* CPAAUDIT LLP, GUIDE TO INTEGRATED REGULATORY REPORTING (RII) AND MANDATORY ELECTRONIC REPORTING (MER) FOR INVESTMENT FIRMS (2008), *available at* http://www.cpaaudit.co.uk/pdfs/IRRandMERGuide.pdf.

[65] *See* Rebecca Atkinson, *FSA Issues Integrated Regulatory Reporting Paper*, MORTGAGE STRATEGY (June 1, 2006), http://www.mortgagestrategy. co.uk/isa-issues-integrated-regulatory-reporting-paper/123106.article.

[66] *See* CPA AUDIT LLP, *supra* note 64, at 1.

[67] HM TREASURY, MEMORANDUM OF UNDERSTANDING (MOU): BETWEEN THE FINANCIAL CONDUCT AUTHORITY (FCA) AND THE PRUDENTIAL REGULATION AUTHORITY (PRA) (Apr. 22, 2013), *available at* https://www.gov.uk/government/publications/memorandum-of-understanding-between-the-financial-conduct-authority-and-the-bank-of-england-including-the-prudential-regulation-authority.

[68] See generally Georgosouli, *supra* note 14, 63–66, for a critical evaluation of the FCA and PRA coordination arrangements under the Financial Services Act 2012.

An integral aspect of the creation of computer software is the reduction of regulatory commands into code. The latter poses a range of challenges. The code is bound to reflect the professional programmers' beliefs about how TCF should be interpreted in practice. When these beliefs are not consistent with those of the regulator, there is a risk that firms end up using computer software (e.g. computer software that supports a firm's system of data resource management pertaining to TCF) whose code encapsulates an understanding of TCF that may actually be words apart from that which was originally envisaged by the regulator. As a result of this incompatibility, important risks are unlikely to be detected or indeed properly identified and responded to.

In view of this problem, one would expect that at least some form of quasi-monitoring be in place at the production stage of computer software so that a minimum calibration and compatibility is secured. This would also keep at bay several inconsistencies and unnecessary discrepancies in the design of the code, however, at the moment, the FCA goes as far as to provide a list of Independent Software Vendors ("ISVs") for the purpose of assisting the industry in finding software suppliers. Moreover, and in order to avoid any misconception to the contrary, this list is followed with a disclaimer that the "FCA does not endorse or recommend any ISV listed."[69]

C. TCF AND THE DESIDERATUM OF CREDIBLE DETERRENCE

Credible deterrence requires enforcement action that is visible enough so that wrongdoers realise that they face a real risk of being held accountable and of bearing the tangible consequences of disciplinary action.[70] The UK regulator did not always give emphasis to formal enforcement as a tool for credible deterrence.[71]

Pre-crisis, the motto was "prevention is better than cure." Initially, the FSA relied on a combination of principles and rules in order to regulate

---

[69] *Independent Software Vendors*, FIN. SERVS. AUTH. (Jul. 11, 2014), http://www.fca.org.uk/firms/systems-reporting/gabriel/tech-publications/list-of-isvs.

[70] Howard Rockness & Joanne Rockness, *Legislated Ethics: from Enron to Sarbanes-Oxley, the Impact of Corporate America*, 57 J. BUS. ETHICS 21, 50–51 (2005) (highlighting the need for meaningful sanctions and fines that exceed gains).

[71] Ferran, *supra* note 6, at 260–61.

the sale of PPI ranging from the Eleven High Level Principles for Business ("PRIN") to rules on systems and controls ("SYSC"), training and competence ("TC"), and rules on how to handle customer complaints ("DISP"). Eventually, these were further supplemented by a more detailed version of the ICOBS. The legal enforcement of these rules was not at the top of the priorities of the UK regulator. The emphasis was on persuasion and the industry was expected to voluntarily adhere to Handbook provisions. The industry's enrolment was viewed as key to proactive regulation and self-regulation was relied upon as the main conduit of cultural change. The fact that the FSA's policy of deterrence was not enforcement-led does not mean that enforcement was missing. Even in the early years, enforcement –for example, through the imposition of administrative fines- had a role to play in sending the message that non-compliance would not be tolerated, but it was clearly employed as a last resort.[72]

Post-crisis, and after an increasing number of instances of financial misselling, the FSA became concerned that its enforcement strategy was neither preventive nor visible enough to change industry attitudes.[73] The probability of enforcement was not considered a credible threat as much as a consideration that it would make firms think twice before breaking the rules.[74] Scepticism also started to grow about the extent to which it is

---

[72] *See generally* Margaret Cole, Dir. of Enforcement, Fin. Servs. Auth., Annual Financial Crimes Conference: Delivering Credible Deterrence (Apr. 27, 2009), *available at* http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2009/0427_mc.shtml; Margaret Cole, Dir. of Enforcement, Fin. Servs. Auth., Enforcement Law Conference: How Enforcement Makes a Difference (June 18, 2008), *available at* http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2008/0618_mc.shtml.

[73] *See* Letter from Andrew Tyrie, Member of Parliament, U.K., to Fin. Ombudsman Serv. (Dec. 19, 2012), *available at* http://www.parliament.uk/documents/commons-committees/treasury/121 219-FOS-PPI-capacity-planning.pdf; *see also* NICK WAUGH & CHRISTIE SILK, THE COST OF REDRESS: THE LESSONS TO BE LEARNED FROM THE PPI MIS-SELLING SCANDAL 8 (2014), *available at* http://www.citizensadvice.org.uk/index/policy/policy_publications/er_consumertravelandtransport/the_cost_of_redress.htm.

[74] *See* Tracey McDermott, Dir. of Enforcement & Fin. Crime, Fin. Conduct Auth., Enforcement and Credible Deterrence in the FCA, Address at the Thompson Reuters Compliance and Risk Summit, at 3–5, 7–8 (clarifying that the regulator's role is to test and challenge assertions about what the culture of an institution is)

feasible to attune business culture to the delivery of public policy goals and to foster patterns of self-governance in an industry that was demonstrably hostile to self-regulation. In view of this, the FSA introduced a new strategy. This made its first appearance in the FSA 2007/8 Annual Report and was labelled "credible deterrence" to mark a toughening up of the regulator's enforcement action.[75]

The FCA continues this approach, but also enjoys more powers to become a credible enforcer of TCF.[76] As pointed out above, the parent legislation now entrusts the FCA with enhanced powers to use transparency as an enforcement tool in the sense that it is now possible for the regulator to publish information about a disciplinary action at an earlier stage than in the past provided that certain conditions are met.[77] Product intervention is another key element of the new strategy. At least on paper the FCA has more interventionist powers at its disposal under new sections 137C to 137D and 137M to 137N of the FSMA 2000 as recently amended by the FSA 2012.[78] These are further complemented by new sections 137P to 137Q, which set out more powers to intervene in respect of financial promotions.[79]

(June 18, 2013) (transcript *available at* http://www.fca.org.uk/static/documents/enforcement-credible-deterrence-speech.pdf).

[75] FIN. SERVS. AUTH., ANNUAL REPORT, 2007-8, H.C., at 6 (U.K.).

[76] FIN. SERVS. AUTH., THE FINANCIAL CONDUCT AUTHORITY: APPROACH TO REGULATION 25 (2011).

[77] Financial Services and Markets Act, 2000, c. 8, § 391 (U.K.) (amended 2010). Section 391 incorporates further extension of transparency-enhancing changes made by the Financial Services Act 2010. *Id.* The FSA's use of these powers has already been challenged by way of judicial review and in the Upper Tribunal. *See* R *ex rel.* S v. X, [2011] EWHC (Admin) 1645, [4]–[10] (Eng.) (addressing the claimant's appeal of the FSA's decision notice to the Upper Tribunal and granting an interim injunction to restrain the FSA from publishing the notice); R *ex rel.* Can. Inc. v. Fin. Servs. Auth., [2011] EHWC (Admin) 2766 (Eng.).

[78] Financial Services Act, 2012, c. 21, § 137C–137D, 137M–137N (U.K).

[79] Some of the FCA's key priorities in respect to consumer credit reveal the intention of the UK regulator to make use of its new powers. These priorities include (a) the review of financial promotions, (b) the improvement of debt management standards, (c) considering the introduction of price caps on what payday lenders can actually charge, (d) assessing regularly how the industry treats financial difficulties, and (e) getting a better understanding of the economic behavior of consumers. FIN. CONDUCT AUTH., BUSINESS PLAN 2014/15 (2014),

Firms are still required to demonstrate an ongoing commitment, right up to the board level, in securing right outcomes for their customers, particularly consumers.[80] Furthermore, senior managers that repeatedly fail to deliver now face greater chances of becoming the target of the FCA's enforcement action.[81] Last but not least, there is now the possibility of mass consumer redress, the aim of which is to ensure consistent redress outcomes for consumers in a timelier fashion.[82]

There is no doubt that these amendments to the TCF legal framework bear the potential of cementing the FCA's enforcement action if indeed the FCA decides to move from simply expressing intentions to the taking of action. Nevertheless, the fact remains that post-crisis, visibility of enforcement action of the UK regulator is still lacking. Although it is true that we witnessed a peak in formal enforcement between 2006 and 2008, it is equally true that enforcement action regarding PPI tailed off more recently, given that the regulator's priority remains that of securing redress for the numerous victims of PPI misselling rather than to punish wrongdoers for their misconduct.[83] Formal enforcement is still considered a measure of last resort while dialogue and persuasion continue to be the preferred course of action for behaviour modification.[84] There is a good reason for this. Formal enforcement takes time to bring fruits let alone secure large-scale consumer redress. In a similar fashion, early settlement is thought to be in the public interest because it secures redress for the victims of PPI misselling, and it is speedier and less expensive relative to other alternatives.

---

available at http://www.fca.org.uk/static/documents/ corporate/business-plan-2014-2015.pdf.

[80] FIN. SERVS. AUTH., TREATING CUSTOMERS FAIRLY: PROGRESS UPDATE 15 (2008), *available at* http://www.fsa.gov.uk/pubs/other/ tcf_progress.pdf.

[81] McDermott, *supra* note 74, at 5–7.

[82] Financial Services and Markets Act, 2000, c. 8, §§ 404-404G (U.K.) (amended 2010); Richard Peat et al., *Imposing Consumer Redress Schemes*, 32 COMPANY LAW. 183 (2011).

[83] *See* Financial Services and Markets Act § 2(2) (providing that the primary regulatory objectives include the protection of consumers); *see* Patrick Collinson, *Ombudsman Still Receiving 1,000 Complaints a Day on PPI Mis-Selling*, GUARDIAN (Mar. 4, 2014), http://www.theguardian.com/money/ 2014/mar/04/ombudsman-receives-1000-ppi-misselling-complaints (indicating a steep drop in number of enforcement cases for PPI misselling).

[84] *See generally* Financial Services and Markets Act §§ 225–34 (providing a mechanism for adjudication of certain disputes with "minimum formality").

The credibility of enforcement also calls for consistent policy. Otherwise it is difficult for the regulator to convey the seriousness of its intention. Experience in the UK suggests that the intensity of enforcement action varies and that it is by and large driven by the prevailing political climate. For example, the FSA's willingness to proceed to formal enforcement gained momentum during the recent financial turmoil, that is to say, at a time when there has been great political pressure to bring cases to court. As collective memory of the financial crisis of 2008 fades away, the regulator's commitment to formal enforcement is expected to recede.

The possibility of early settlement and the tendency to resort to private warnings at the supervisory stage and in exclusion from any further enforcement action are two further features of the UK regulator's approach that undermine the visibility of disciplinary action. Specifically, under the current regime, the industry is given several incentives to opt for early settlement, such as discounts and the reduction of financial penalties.[85] The downside of this is that nobody takes notice given that these early stages of disciplinary action are carried out away from the public eye. Private warnings at the supervisory stage are arguably the most serious form of reprimand during ongoing supervisory correspondence. They communicate the regulator's concerns about the firm's conduct and that disciplinary action may follow as a result of this, but again this correspondence is kept confidential and may never materialise into a widely publicized formal enforcement action.

The credibility of deterrence practices of the UK regulators has been further eroded by the industry's reluctance to genuinely engage with the regulator to secure fair treatment for customers.[86] This is evident, for example, (a) in the large number of PPI complaints being referred to the FOS, (b) in the discrepancy in outcomes between PPI complaints that were referred to the FOS and those that were handled by firms[87] and (c) more recently, in the industry's attempt to challenge the FSA's decision to take

---

[85] FIN. CONDUCT AUTH., DECISION PROCEDURE AND PENALTIES MANUAL § 6.7 (2014), *available at* http://media.fshandbook.info/content/FCA/ DEPP.pdf. For information on the discount rates, see *id*.

[86] *See* Final Notice from the Fin. Servs. Auth. to the Co-operative Bank PLC (Jan. 4, 2013), *available at* http://www.fca.org.uk/static/ fca/documents/final-notices/co-op.pdf; Lloyds TSB Bank Plc, *supra* note 6. *See also* McDermott, *supra* note 74 (discussing this erosion).

[87] *See* Collinson, *supra* note 83 (noting the increased flow of PPI complaints that was referred to the FOS); Ferran, *supra* note 6 at pages 252 and 255 (discussing the dismissiveness of the industry).

enforcement action following the industry's failure to take into account FOS decisions in handling customer complaints, contrary to the regulator's expectations, as these were communicated informally in a Policy Statement ("PS").[88]

In its judicial review action the industry argued that PRIN are not actionable by suit by a private person in view of the wording of old section 150 of the FSMA 2000.[89] Accordingly, they could not give rise to redress obligations. In addition, the industry claimed that regulatory principles could not conflict with or augment specific rules.[90] Finally, it contended that the existence of an alternative statutory collective redress scheme precluded the FSA from taking the action that was set out in the Policy Statement.[91] The industry eventually lost its case on all three grounds.[92] In the course of bringing the action, several firms put on hold the handling of nearly all PPI complaints. This caused significant delays in the system, eventually leading to the large pay-outs in the second term of 2011.[93] Most importantly though, it aggravated the situation in the eyes of the UK regulator and undermined past attempts to build trust.

V. CONCLUSION

The principle that customers must be treated fairly has a long history in the UK. So does the problem of PPI misselling, which the Treating Customers Fairly initiative aims to tackle. I tried to demonstrate in this Article that TCF looks good on paper. It intends to be flexible enough to let firms adapt regulatory mandates according to their individual circumstances and it encourages firms to develop their self-regulatory capacities in a manner that bolsters TCF targets, namely tangible public policy outcomes. However, in practice, the recurring instances of PP misselling indicate that TCF has, thus far, made little difference.

---

[88] R *ex rel.* British Bankers Ass'n v. Fin. Servs. Auth., [2011] EWHC (Admin) 999.

[89] *Id.* at [60].

[90] *Id.* at [95].

[91] *Id.* at [210]–[211].

[92] *Id.* at [264].

[93] FIN. SERVS. AUTH., *supra* note 42; Press Release, Fin. Servs. Auth., Lloyds Banking Grp. Fined £4.3 Million for Delayed PPI Redress Payments (Feb. 19, 2013), *available at* http://www.fsa.gov.uk/library/communication/pr/2013/017.shtml.

This Article traced the causes of this shortcoming, focusing in particular on the rulification of TCF, some difficulties associated with the system of data resource management that is currently in use, and the absence of a system of credible deterrence to back up the regulator's attempt to inflict long-term cultural change in the interests of consumers. Several lessons may be drawn from the UK experience with TCF. All of them illustrate that the focus on "outcomes" rather than "principles" does not necessary guarantee better performance in attaining public policy objectives.

For a start, the implementation of TCF in the UK demonstrates that the choice to depart from the traditional rulebook approach does not necessarily offer a better solution to the pervasive problem of striking the proper balance between, on the one hand, certainty and predictability and, on the other hand, flexibility and adaptability. TCF was informal in its inception, but eventually it became rulified and sclerotic, in view of the measures that were taken to respond to the industry's constant pressure for more detailed guidance.

Further, the regime of intensive supervision that has been associated with the implementation of the rulified TCF is likely to have contributed to the regulatees' general reluctance to exercise judgement and discretion and to adopt an attitude of reflective compliance with rules and guidance. Instead of being "enabling" and "engaging," in all probability the regulator's near omnipresence in the internal affairs of the regulated firms left hardly any scope for reflection and healthy experimentation and made the regulatees either more complacent or less confident in their expertise and judgement.

The UK experience with the implementation of TCF also highlights the relevance of big data in making the whole initiative a success. Specifically, it reveals how the computer software that supports data resource management can actually hinder regulators from making sound judgments. This occurs when the software is not properly designed or when errors, undermining the reliability and accuracy of the data produced, are not identified and properly addressed at an early stage. Who develops computer software for data resource management is also of practical importance. Professional programmers do not necessarily understand what TCF requires in practice in the same way as the regulator does. To the extent in which the articulation of TCF outcomes may turn out to be different from what was originally intended, computer software that is specifically calibrated to ensure compliance with TCF may in reality be at odds with the intended TCF goals.

In view of the fact that technology shapes the meaning of TCF goals and may even translate TCF goals into a course of action that is worlds apart from what the regulator would recommend, some further issues that require immediate attention include, but are not limited to, the following: (a) The determination of the respective roles of the State and the market in developing the software that would support the operationalization of a consolidated system of data resource management; (b) whether some sort of a licensing regime would be appropriate as a mechanism that would ensure consistency between the regulator's understanding of TCF and that of software developers'; (c) how to make sure that the relevant software is constantly updated so that it keeps pace with market developments; (d) whether it is desirable to have in place inter-operable data systems with means for monitoring and correcting data errors built into them (e.g., automatic alerts regarding the entry of anomalous values); and (e) whether it is expedient to standardize terms and industry jargon.

Finally, the lack of credible deterrence brings to the surface an inevitable trade off between two conflicting policy considerations that cannot be ignored: on the one hand, the need to secure timely and cost-efficient consumer redress and, on the other, the need to ensure that law enforcement is visible enough to deter. The UK experience highlights that it is not possible to have both. While securing financial redress in a timely fashion justifies early settlement, credible deterrence pulls in the opposite direction because it calls for a course of action that is more time consuming (typically this would involve bringing a case to the courts) and a gamble to retail customers.

The increasing emphasis on business culture suggests that the FCA is cognisant of this trade off and that it has made a deliberate choice to boost market discipline by challenging the business culture that prevails in the industry. This is a welcome development, but it will take time to bring fruits. In any case, the potency of culture as a regulatory tool should not be blown out of proportion.

At least in part, the efficacy of the regulator to instigate cultural change depends on the willingness of the firms to genuinely engage with the regulator and – when challenged – to reflect on the soundness of their respective culture in order to amend business practices where appropriate. Persistent industry regression leaves little scope for optimism. In this regard, it is interesting to note that in the past the policy of the FSA was to offer firms a "regulatory dividend" in the form of less scrutiny, as an incentive to make them behave well demonstrating essentially that customer interests were central to the corporate culture of the business in question. This policy reflected an assumption that the vast majority of

firms had the intention to treat their customers fairly and that the majority were willing to engage openly and positively with the regulator. Both assumptions proved to be naïve in reality.

Retail financial firms are not charities working in the interests of customers. They are profit-driven institutions. A business culture that ends up reflecting both the profit-driven character of the business and the firm's perceived commitment to public policy goals, like fair treatment for customers, is bound to be self-defeating because it constitutes a contradiction in terms. One must take priority, and quite intuitively this will have to be profit. Otherwise, the business will not be able to survive. This is not to say that no good can come out of business culture as a tool for improving the effectiveness of TCF. It can, but in all probability, it is going to be less than we are inclined to think. Profit-making considerations confine how far TCF can go in aligning the goals and priorities of the industry with those of the regulator and, by implication, to what extent it is possible to rely on business culture. Accordingly, when designing and implementing TCF, a healthy dose of pragmatism is called for to make it a credible policy in the first place.