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Financial Conduct Authority
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**By Email**

Dear Sirs

**FCA Smarter Consumer Communications (DP15/5)**

The City of London Law Society ("**CLLS**") represents approximately 14,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

This letter has been prepared by the CLLS Regulatory Law Committee (the "**Committee**"). The Committee not only responds to consultations but also proactively raises concerns where it becomes aware of issues which it considers to be of importance in a regulatory context.

The FCA published its Discussion Paper on Smarter Consumer Communications (the "**DP**") on 25 June 2015 with the intention of encouraging firms to consider innovative ways of engaging with consumers about their products and services.

We welcome the opportunity to comment on the FCA's Discussion Paper on Smarter Consumer Communications (the DP). We do not seek to comment on the proposals as a whole or to focus in detail on specific modes of communication; instead we have limited our response to focusing on legal issues in connection with the use of "smart" formats in the design and delivery of firms' terms and conditions (T&Cs) and potential suggestions for improving accessibility of T&Cs without compromising legal certainty.

In general terms, we support the efforts by the FCA to encourage firms to explore alternative modes of customer communication as a means for increasing understanding and engagement in retail markets. For some retail customers, the types of "smart" content discussed by the FCA may provide a valuable tool in enhancing meaningful transparency around financial products and services.

It is important, however, that the potential benefits offered by innovation in customer communications are not outweighed by an increased risk of financial services contracts being disputed and potentially rendered unenforceable and/or in breach of regulatory requirements.

This risk is particularly relevant where T&Cs are concerned. The binding and heavily regulated legal nature of T&Cs makes them qualitatively different from other forms of customer "communications". Accordingly, the factors to be taken into account in relation to the composition, format and presentation to the customer of T&Cs will necessarily differ from the considerations that may apply to other customer communications whose functions are primarily informative and/or promotional (and which are therefore more amenable to being delivered through innovative formats).

We are concerned that some of the suggestions for firms to "improve" their T&Cs by replacing or supplementing traditional written agreements with "smart" alternative formats could be problematic from a legal perspective, as the alternative formats discussed may not satisfy the fundamental contract law requirements of incorporation and legal certainty. This could increase the potential for legal disputes, with the risk of damaging outcomes for both consumers and firms, including unenforceable rights, increased litigation costs and reputational damage.

In addition, the use of "smart" formats to deliver legal T&Cs may fail to satisfy applicable regulatory requirements for durability and continuous access, which would make this an unfeasible approach for most banking and investment products and services. It is also important to consider the application of pending EU reforms relating to retail disclosures, in particular MiFID II and the PRIIPs regulation.

We would therefore urge the FCA to ensure, in developing any further policy initiatives in this area, that the encouragement of "smart" formats should be primarily focused on communications whose function is informative (rather than legally binding) and that where T&Cs are concerned, the priorities should be regulatory compliance, transparency, legal certainty and enforceability. These priorities should not, however, prevent the development of initiatives to improve customer engagement with T&Cs, provided that any such reforms are designed with due regard to legal and regulatory requirements and in consultation with appropriate stakeholders. We would be very happy to work with the FCA on any further proposals in this area.

We have highlighted below some specific comments on legal issues regarding the use of smart communications in the context of T&Cs.

1. Contract formation

For a contract to be validly formed under UK law, it is necessary to have a binding offer and acceptance of the contract and its terms. For online sales, the practice of requiring the customer to click an acceptance box, after disclosure of the T&Cs, is a recognised form of binding acceptance under UK and EU law and is common practice for web-based sales generally both within and outside the financial services industry.

We do not see anything inherently unfair, unclear or misleading (as the FCA suggests) in inviting a customer to review and accept a set of electronic T&Cs, provided that in each case the customer first, has the option to review the T&Cs before entering into the contract and second, understands that in ticking the box, s/he will be accepting the T&Cs as disclosed.

Customers may also benefit from the flexibility to download and review the T&Cs "offline" or to receive a subsequent email version, particularly as a cancellation period will generally apply. This mechanism for electronic acceptance (assuming that it is not structured improperly) has the advantage of being both legally effective and familiar to consumers as established market practice for electronic trading. We would not support requirements that would prohibit acceptance of T&Cs by the customer until a minimum time period has elapsed (as seems perhaps to be the implicit suggestion in the DP); this would be out of line with market practice for electronic sales, would still not guarantee that the customer will actually read the T&Cs and could instead risk alienating customers.

We appreciate that the length and/or density of T&Cs means that in practice, many customers choose not to read T&Cs. This issue is not specific to the financial services industry. Nor is it particular to electronic T&CS, as customers may (and do) choose equally not to read T&Cs disclosed as part of contracts concluded by post or face-to-face.

We acknowledge that this situation is far from optimal and that there is clear merit in innovative communication strategies that aim to educate and engage customers and to assist them in reviewing and understanding T&Cs before signing a new contract. We agree that (if developed appropriately), the use of "layering" and Q&A formats may be possible avenues for facilitating greater engagement (discussed further in Section 5 and 6 below).

2. Content of T&CS: legal certainty and comprehensiveness

The function of T&Cs is to formalise the binding legal agreement between a firm and the customer and to specify and record the rights, duties and liabilities of both parties, together with any associated limitations. In order for the rights of either party to be legally enforceable, these various contractual components must be specified clearly and comprehensively, as applicable both in a "business as usual" context and in the "just in case" eventuality of various potential future scenarios (including termination, variation, default, and dispute).

The contract must also contain all disclosures or other terms required by regulation; for financial products and services, the requirements under FCA conduct of business rules translate into a considerable list. T&Cs also include non-sectoral mandatory disclosures such as those required under data protection law and must comply with the transparency requirements under the Consumer Rights Act 2015. In overall terms, it is essential from a legal perspective that T&Cs form a "complete", binding and certain agreement, taking into account all of the relevant contractual and regulatory requirements. This has been highlighted by the FOS in a number of judgements on retail financial services contracts.

We are therefore concerned by the FCA's suggestions that firms limit their T&Cs to those that are "necessary or relevant" and exclude terms that are "relevant primarily in case of conflict" or are otherwise included "just in case". It is not clear exactly what the FCA has in mind here; we would agree that it is unhelpful for firms to include genuinely irrelevant material in retail contracts (such as T&Cs governing products or services not purchased by the relevant consumer). It is not appropriate, however, to equate terms that are "relevant primarily in case of conflict" with those that are not "necessary or relevant", as to omit such terms would expose both firms and consumers to significant risks. An absence of (or insufficiently specific) provisions in this area will potentially increase the likelihood of formal legal disputes and of unpredictable outcomes arising from such disputes. At worst, some or all terms may be unenforceable (including against the customer), which would be damaging not only for individual consumers and firms, but could also have a destabilising impact on retail financial services markets overall.

Ensuring that contracts contain sufficient detail and clarity on the respective rights of the parties in different scenarios helps to minimise industry wide risks. It is also an important risk management tool for individual firms, as it enables firms to measure and price risks associated with particular products, services or customers and to reduce litigation and enforcement costs, which may otherwise be passed on to consumers.

3. Format of T&Cs: incorporation of terms

In addition to ensuring that all elements of a contract are sufficiently certain and that the contract overall is complete enough to be certain, it is also necessary for firms (and customers) to be confident that all relevant terms have been validly incorporated into the contract.

As noted above, the accepted market practice for web-based sales of directing a customer to an online printed display of the supplier's T&Cs, with an invitation to tick the appropriate box to indicate acceptance, is in principle generally effective under English law to incorporate the relevant T&Cs.

In contrast, the legal status and of information provided via "smart" formats would potentially be uncertain. If a firm chooses to deliver all or part of its T&CS through dynamic formats such as pop-ups, videos, audio clips and/or pictures, it seems questionable as a matter of contract law whether these pieces of information could be said to be "terms" at all, and if so, whether and in what circumstances they could be regarded as having been incorporated and how they would function in the event of any inconsistency with related written T&Cs. Moreover, In practical terms, not all customers will necessarily be able or willing to view smart content, due to technical barriers (such as browser or audio functionality), environmental factors (public/open plan settings, for example), or personal choice.

Firms will therefore need to continue to maintain and disclose their T&CS in conventional, written format (in addition to any "smart" alternatives adopted) in order to avoid discriminating against and/or losing customers on the basis of technical or environmental barriers.

Legal issues would still remain, however, where T&Cs are delivered in partial or alternative (as opposed to exclusively) "smart" formats, particularly if a customer is able to rely purely on the "smart" content as an alternative (rather than a supplement) to the conventional written T&Cs. This would raise legal questions over whether either or both versions have been validly incorporated into the overall contract and how any apparent inconsistencies in interpretation should be reconciled (a question that would be challenging for the FOS and/or the courts to resolve). Firms would also need to have the means to track and record which version(s) have been viewed and accepted by customers (and query how "acceptance" of a non-permanent smart format T&Cs would be executed).

These legal and practical questions indicate that while "smart" communications may be highly effective as tools for presenting customer information and generating interest, they be less effective as vehicle for establishing and recording binding legal obligations, which is best achieved through static written formats for reasons of certainty.

Firms carrying out designated investment business and/or certain retail banking and other services within the scope of the Distance Marketing Directive are also subject to regulatory constraints that create effective barriers to departing from the conventional format of static, written T&Cs. For example, Chapter 8 of COBS (which implements MiFID requirements but applies to most designated investment business), requires a firm, to: "enter into a written basic agreement, on paper or other durable medium, with the client setting out the essential

rights and obligations of the firm and the client. The agreement may be provided initially via a website, but only provided that the "Website Conditions" are satisfied, including a requirement that the information is "accessible continuously by means of that website for such period of time as the client may reasonably need to inspect it." (Similar requirements apply under BCOBS to retail banking contracts concluded electronically and/or on a distance basis.) The difficulty of satisfying these requirements through dynamic content, which is generally neither durable nor continuously viewable indicates that the traditional written T&Cs model would therefore have to be preserved for regulatory as well as contractual reasons.

4. Layering of T&Cs

A further suggestion put forward by the FCA as an example of alternative best practice where T&Cs are concerned is the use by firms of a "layered" approach to delivering T&Cs content. We agree that this may in principle be a useful approach, although it would need to be implemented carefully with appropriate regard for the legal implications of appearing to classify terms into "tiers" of relative importance.

We would suggest that the best approach in this respect would be for the FCA and others to work to develop best practice standards for the form and content of layered disclosures or similar "signposting" strategies for improving customer engagement with specific terms. We would also agree that content delivered in Q&A format could also be a useful tool for providing information to customers more clearly, provided that the Q&A are appropriately designed and that their legal status and relationship to the remainder of the contractual terms can be made adequately clear to consumers.

With respect to the FCA's specific questions on this point, we are not aware of any legislation that would specifically prohibit a layered approach (though care would be needed to ensure that the "durable medium" or "continuous access" requirements prescribed by MiFID, etc. are properly met for each "layer"). Indeed, it is possible to point to EU legislative requirements that specifically mandate a "layered" approach to disclosure of key terms in relation to retail financial products. Examples would be the UCITS Directive, Prospectus Directive and PRIIPs Regulation (which prescribe the provision and content of a short-form summary/abbreviated T&Cs document, which supplements the remainder of the contractual documents). The FCA's packaged product rules in COBS 13-14 offer another example at UK domestic level.

The challenge is rather that any new short-form or other "layered" disclosure standards developed at UK level for retail products generally will need to be consistent with pending EU reforms in this area, most notably the PRIIPS KID requirements and the various new retail disclosure standards under MiFID II (due in both cases to take effect on 1 January 2017). In light of these reforms, it essential that any retail communication standards or guidance developed in the meantime is produced with the PRIPS and MIFID II standards in mind, to avoid over-burdening either firms or confusing customers with repeated changes to T&Cs and to work towards clear and consistent best practice standards.

While we would see some merit in exploring strategies in the meantime for optimising clarity and accessibility of T&Cs (including, possibly, through use of layering), we would caution against mandating or recommending a layered approach that leaves it up to firms to determine the appropriate content requirements for each layer.

One important feature of regimes such as the PRIIPS Regulation and UCITS and Prospectus Directives is that (in contrast to a more generic "layered" approach), the relevant law prescribes clear parameters and content specifications and (at least ostensibly, for the relevant EU regimes) imposes clear standards of liability with respect to the "first tier"

summary disclosure. These prescriptive content standards not only aid comparability for customers, but also substantially eliminate the risk for firms of making subjective judgement over which terms are important enough to be highlighted at the first layer or tier.

If, on the other hand, firms were expected to exercise discretion over which terms are sufficiently important or relevant to warrant "first layer" status, this would expose firms to the risk of being regarded by the FCA, FOS and/or a court of making the "wrong" judgement: for example, applying a "misleading" or "unfairly" selective approach to disclosure in relation to those terms that are not highlighted in the first "layer".

A particular risk in the context of the Consumer Rights Act 2015 would be the possibility of second-tier terms being struck out by the courts as unenforceable due to failure to meet the necessary transparency and fairness standards for consumer contracts. For example, if a firm takes the view that (as is implied by the FCA) terms relating to possible contractual disputes or changes in law may relegated to second-tier status, this would increase the risk for the firm of such terms being deemed unenforceable due to insufficient prominence, particularly where they have the potential to operate to the detriment of the consumer. The converse risk, from a consumer perspective, is that relegation of these terms to second-tier status (due to having less immediate "relevance") would make a customer even less likely to read them and to be aware of any associated risks.

5. Recommendations

We would therefore suggest that the FCA works with stakeholders from industry, consumer groups, other public bodies such as the Competition and Markets Authority and FOS, as well as legal experts to develop common best practice standards for layering and/or better signposting of retail financial services T&Cs. We would be happy to work with the FCA on developing any further initiatives in this area, although we would recommend that appropriate consideration is given to pending EU-level reforms, which may substantially achieve the FCA's objectives in this area (at least for some products and services) and will also impose overlapping requirements in relation to retail disclosure standards and associated pre-sale behaviour.

If you would find it helpful to discuss any of these comments then we would be happy to do so. Please contact either Karen Anderson by telephone on +44 (0) 20 7466 2404 or by email at karen.anderson@hsf.com, or Peter Richards Carpenter by telephone on +44 (0) 20 3400 4178 or by email at peter.richards-carpenter@blplaw.com, in the first instance.

Yours sincerely

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Its contents should not be taken as legal advice in relation to a particular situation or transaction.

**THE CITY OF LONDON LAW SOCIETY**
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