



UK
FINANCE

REVIEW OF STATUTORY DISPUTE- RESOLUTION PROCESSES IN THE BANKING AND FINANCE SECTOR

16 February 2021

WHITE & CASE



1. INTRODUCTION

1. This paper supplements UK Finance's response to HM Treasury's (HMT) phase-II consultation on the financial-services future regulatory-framework (FRF) review. The process for resolving complaints plays an important role in the regulatory framework, and it is vital for both consumers and firms that provide banking and finance services that there exists a fair and effective statutory mechanism for resolving disputes.
2. Central to the current dispute-resolution process is the Financial Ombudsman Service (FOS). The FOS has a valuable role in providing a fair and effective alternative-dispute-resolution (ADR) service. It was established by statute some 20 years ago to provide a quick, informal, low-cost method for resolving low-value complaints from consumers. Its jurisdiction has since been extended to cover many more small and medium-sized enterprises (SMEs). However, since its inception, concerns have been expressed about whether the FOS is the appropriate forum for resolving complaints that have implications extending far beyond the facts of a specific case. These cases can have significant consequences for both individual firms and the sector as a whole.
3. The purpose of this paper is to examine the role played by the FOS and how it performs its statutory function and to assess whether there are areas that require behavioural, operational and/or structural reform. The paper demonstrates a clear case for change and provides some potential solutions, which will require further consideration, impact assessment and consultation.
4. This paper is specific to the FOS as a statutory ADR service to whose jurisdiction regulated firms must compulsorily submit. It does not consider the recently established Business Banking Resolution Service (BBRS), which, by contrast, is a private ADR service voluntarily established by seven participating banks to resolve disputes between those banks and eligible larger SMEs. In this paper, we make no comparisons between the FOS and the BBRS, and no readacross of our commentary and recommendations regarding the FOS should be made to the BBRS.
5. This paper has been drafted on a best-efforts basis. The themes, challenges and recommendations outlined in the paper are all true to the best of our knowledge. While a more-detailed review would be possible, we are confident the recommendations in section 5 would bring about significant improvement to the current process for resolving customer complaints.

APPROACH

6. In drafting this paper, White & Case undertook desk-based research (see annex 1) and engaged with us and our members. In particular, White & Case conducted:
 - one-to-one meetings with some of our members; and
 - two workshops—one internal to us and one with members.
7. These meetings discussed the purpose, structure and operation of the FOS, concerns about the service and potential recommendations for change.
8. The content of this paper was distributed to members for review and feedback. The paper endeavours to capture and reflect the feedback received.

2. EXECUTIVE SUMMARY

9. The FOS was established by statute to provide a valuable service: determining individual, fact-specific complaints between firms and their customers quickly and with minimal formality. In the 20 years since, it has evolved significantly. However, little has been done from a legal, regulatory or operational perspective to combat the impact this evolution has had on the regulatory landscape.
10. Today, the FOS finds itself with the burden of determining complex cases that may also have a significant impact on firms and the market at large. The reasons for this are arguably twofold: first, developments in the regulatory system mean the FOS is having to interpret perceived gaps in regulation; and second, firms are required to ensure lessons learned as a result of FOS determinations are effectively applied in future complaint handling. This means that while the FOS considers each case individually without applying a system of precedent, practically speaking its decisions can set a precedent. This iterative and retrospective rule-making process leaves the FOS in the uncomfortable position of quasi-regulator. This is not what Parliament intended when it established the FOS and, without a robust appeals process in place, leads to considerable uncertainty and unfairness for firms (and possibly customers), potentially stifling innovation in the market and delaying economic recovery from the Covid-19 pandemic.
11. On our behalf, through a combination of desk-based research, interviews and workshops with our members, White & Case has examined the role of the FOS, how it performs its statutory function and whether there are areas that require behavioural, operational and/or structural reform.
12. This report aims to highlight key concerns and potential recommendations for HMT to consider. These are summarised in the table below, with further details set out in sections 4 and 5. A key concern is that while the current FOS process is appropriate for the resolution of individual consumer and SME cases, it does not provide a sufficient, robust or proportionate process for determining cases that have significantly wider implications. Potential solutions include:
 - the adoption by the FOS of a more consultative and collaborative process for complaint decisions that seek to fill in perceived gaps in regulation with policy or precedent implications;
 - the creation of a new decision-making process that can consider cases with wider implications in a way that provides more certainty and efficiency, leaving the FOS to consider those complaints decided on their individual merit that it was established to consider; and
 - the establishment of a new appeals mechanism to provide customers and firms with an effective and robust route for testing FOS decisions.
13. We recommend HMT investigate each of these solutions in detail to ensure the FOS remains a valuable service for consumers, firms and the regulatory regime as a whole.

Concern	Operational	Behavioural	Structural
Basis and quality of decision making	✓ See S.1, S.4, S.9	✓ See S.1, S.9	✓ See S.2, S.3, S.8, S.10, S.12
Inadequate right of appeal			✓ See S.5, S.6, S.7
Jurisdiction	✓ See S.3, S.4		✓ See S.6, S.7, S.11, S.12

Solutions	
Consultation on key issues	S1. Engage with external stakeholders when determining cases with wider implications.
	S2. Amend the memorandum of understanding (MoU) between the FOS and the Financial Conduct Authority (FCA) and make discussions between the two bodies a matter of public record to provide accountability and clarity on when and how they engage on cases with wider implications.
Twin-track decision-making process	S3. Create a new FOS decision-making process, parallel to the existing one but specific to wider-implication cases.
	S4. Create an internal panel within the FOS that can either decide on wider-implication cases or refer them to a court, tribunal or regulator.
New appeals mechanism	S5. Create a new appellate body to sufficiently scrutinise decisions on cases with wider implications.
	S6. Refer decisions with wider implications to a court or tribunal, without having to go through the judicial-review process.
	S7. Create new criteria to ensure only cases with significant wider implications progress to the new appeals process.
Timeliness	S8. Improve the efficiency of the decision-making process while setting a timeframe of eight weeks to resolve complaints.
Consider apparent inconsistencies	S9. Consider apparent inconsistencies where these are raised by either party to a complaint.
Apply lower interest rate on award	S10. Apply a lower interest rate on award than the current 8 per cent, consistent with the current ultra-low interest-rate environment.
Limitation periods	S11. Apply a long-stop date to the limitation period applicable to FOS complaints.
Complaints relating to a firm's commercial judgement	S12. Consider limiting the FOS's discretion to determine complaints relating to the legitimate exercise of a firm's own commercial judgement.

3. THE FOS REGIME

BACKGROUND

14. The FOS is an independent public body established by part XVI and schedule 17 of the Financial Services and Markets Act 2000 (as amended) (FSMA) so that “certain disputes may be resolved quickly and with minimum formality by an independent person.”¹
15. The statute reflects debates in Parliament prior to the enactment of FSMA. The FOS was to provide “easy access for individual retail consumers to a dispute resolution procedure that is speedy and informal.”² It was intended to be an efficient, flexible and informal way to resolve “relatively minor complaints,”³ determined on their individual merit. Parliament never intended the FOS’s remit to extend to writing the rules within which regulated firms operate.
16. The FOS has been described as “the largest Ombudsman scheme in the world.”⁴ It has evolved significantly since its establishment. As succinctly put by Lord Hunt in his 2008 independent review of the service:

*The world in which the FOS operates today is already very different to that at the end of the last century, when it was conceived. The number of cases it considers . . . is far higher than was ever envisaged. Furthermore, its potential clients are more diverse in their backgrounds and levels of financial literacy than anyone foresaw. . . . Regulation is moving away from detailed and prescriptive rulebooks, to high-level principles. The FOS now operates in a world where the presence of aggressive advertising by claims management companies has radically changed the terms of engagement between complainants, firms and the Ombudsman.*⁵

17. Lord Hunt’s observations remain valid today. The number of complaints the FOS receives has continued to increase, from 163,012 in 2010 to 388,392 in 2019—an increase of 138 per cent.⁶ This trend is likely to continue.⁷ The increase in caseload necessarily led to the FOS expanding its resources, and so, in this same period, the FOS has increased the number of its ombudsmen from 42 to 359 and the number of adjudicators from 579 to 1,543.⁸ The FOS’s jurisdiction was expanded in April 2019 to cover many more SMEs, which we welcomed.

1 Section 225(1).

2 Melanie Johnson, Economic Secretary to the Treasury (<https://hansard.parliament.uk/Commons/2000-01-19/debates/0fef08fc-703a-4995-94ba-e42012e61b6b/BankingSector>).

3 Melanie Johnson, Economic Secretary to the Treasury (<https://hansard.parliament.uk/Commons/2000-02-09/debates/25de6eea-1ba1-49d3-8ba8-a5b6d187a1d6/NewClause2>).

4 P. E. Morris, “The intersection of commercial powers and complaints: the Financial Ombudsman Service, consumer protection and the courts” (<https://www.i-law.com/ilaw/doc/view.htm?id=228049>).

5 https://www.financial-ombudsman.org.uk/files/17745/Hunt_report.pdf.

6 It is recognised certain wide-scale matters (e.g. payment-protection insurance—PPI) significantly contributed to this increase. See <https://www.financial-ombudsman.org.uk/who-we-are/governance-funding/annual-reports-accounts/annual-review>.

7 Law360, “Ombudsman Reports 40% Jump In Complaints Over COVID-19” (<https://www.law360.com/insurance-uk/articles/1338703/ombudsman-reports-40-jump-in-complaints-over-covid-19>).

8 <https://www.financial-ombudsman.org.uk/files/2015/ar10.pdf> and <https://www.financial-ombudsman.org.uk/who-we-are/governance-funding/annual-reports-accounts/annual-review>.

18. The evolution of the FOS has not been limited to growth in its physical operations, caseload and jurisdiction. It now finds itself increasingly handling complaints that have wider implications for the industry and the regulatory landscape within which it operates. This has arguably left a service far from that which Parliament intended, potentially stifling competition—a risk Parliament was keen to mitigate.
19. Before considering the implications in further detail, it is important to consider the legislative, regulatory and operational framework within which the FOS works.

LEGISLATIVE, REGULATORY AND OPERATIONAL FRAMEWORK

20. The FOS has broad statutory powers under FSMA. While it is independent from the FCA, any gaps in the regulatory framework governing the FOS are filled by the rules set out by the FCA in the Dispute Resolution: Complaints (DISP) section of its Handbook. DISP determines how the FOS and regulated firms must handle complaints.
21. FSMA also requires the FOS and the FCA to cooperate with each other in the exercise of their respective functions.⁹ An MoU between the two bodies provides a framework for how they exercise this cooperation.¹⁰
22. The FOS must determine complaints within its jurisdiction by reference to what is, in its opinion, “fair and reasonable in all the circumstances of the case.”¹¹ DISP 3.6.4 provides that, in considering what is fair and reasonable in all the circumstances of the case, the FOS will take into account relevant law and regulations, regulators’ rules, guidance and standards, codes of practice and (where appropriate) what it considers to have been good industry practice at the relevant time. However, case law has established that, in practice, it has a wide power of discretion when considering legal principles applicable to a complaint. In essence, it is able to depart from such principles when determining what is fair and reasonable.¹² The extent of the discretion granted to the FOS was noted by Lord Hunt in his review (emphasis added).

*It is important to realise, however, that this jurisdiction does give the Ombudsman unusually wide powers of discretion. I have reviewed the relevant case law on cases raised against the FOS and note, in particular, the judgement in IFG Financial Services v Financial Ombudsman Services Ltd, which makes clear that, although the Ombudsman must have regard to the law, he is not bound to follow it to the exclusion of all other relevant circumstances. **This gives the FOS wider freedom than almost any other public body.***

23. The complaints-handling procedure set out in DISP was summarised in Richard Lloyd’s 2018 report of the independent review of the FOS as follows.¹³

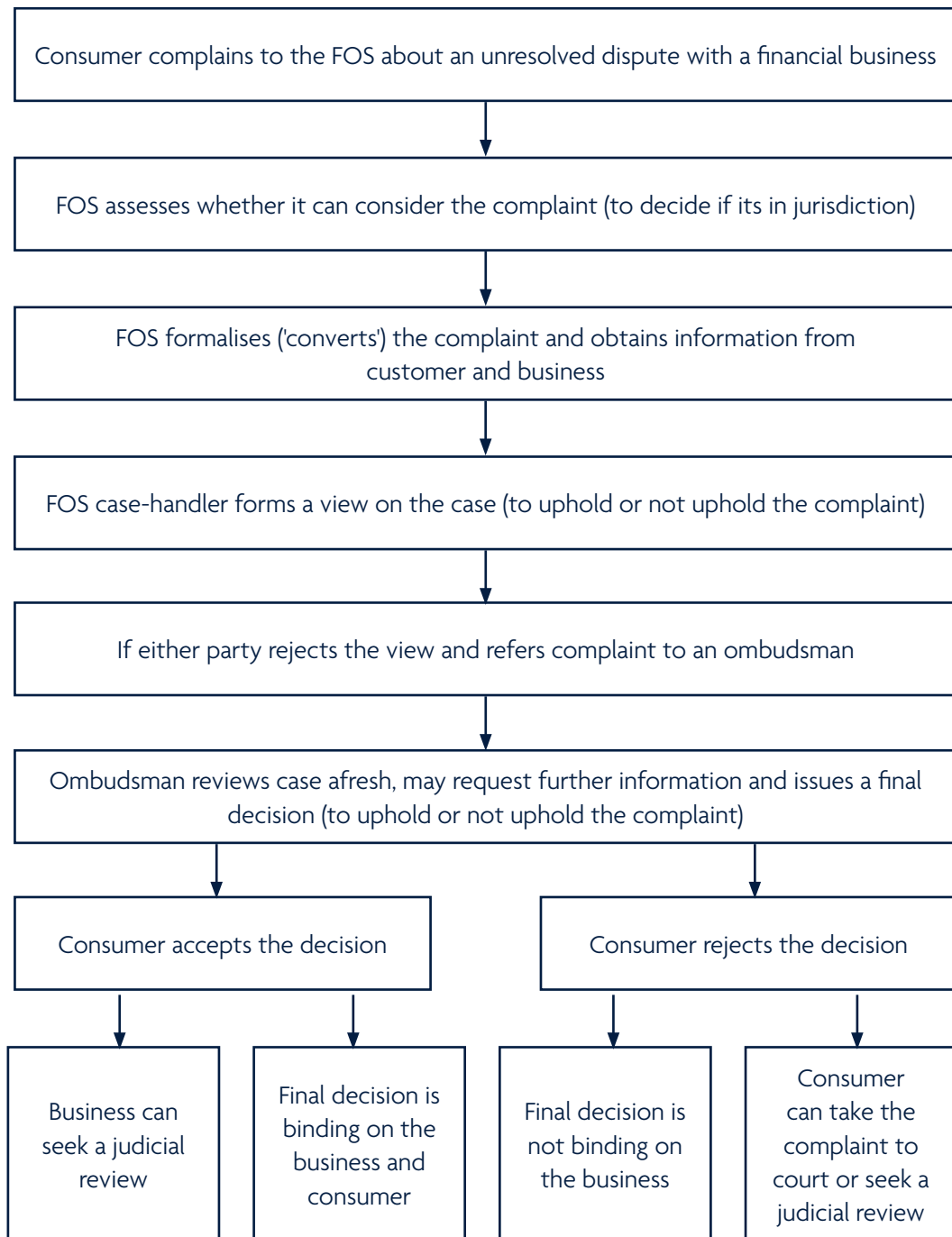
⁹ Paragraph 3A(1) of Schedule 17.

¹⁰ <https://www.fca.org.uk/publication/mou/mou-fos.pdf>.

¹¹ Section 228(2) of FSMA and DISP 3.6.1.

¹² R (on the application of IFG Financial Services v Financial Ombudsman Services [2005] EWHC 1153 (Admin) (<https://www.bailii.org/ew/cases/EWHC/Admin/2005/1153.html>); R (on the application of Aviva Life & Pensions (UK) v Financial Ombudsman Service etc. [2017] EWHC 352 (Admin) (<http://www.bailii.org/ew/cases/EWHC/Admin/2017/352.html>).

¹³ <https://www.financial-ombudsman.org.uk/files/17748/Richard-lloyd-independent-review-2018.pdf>

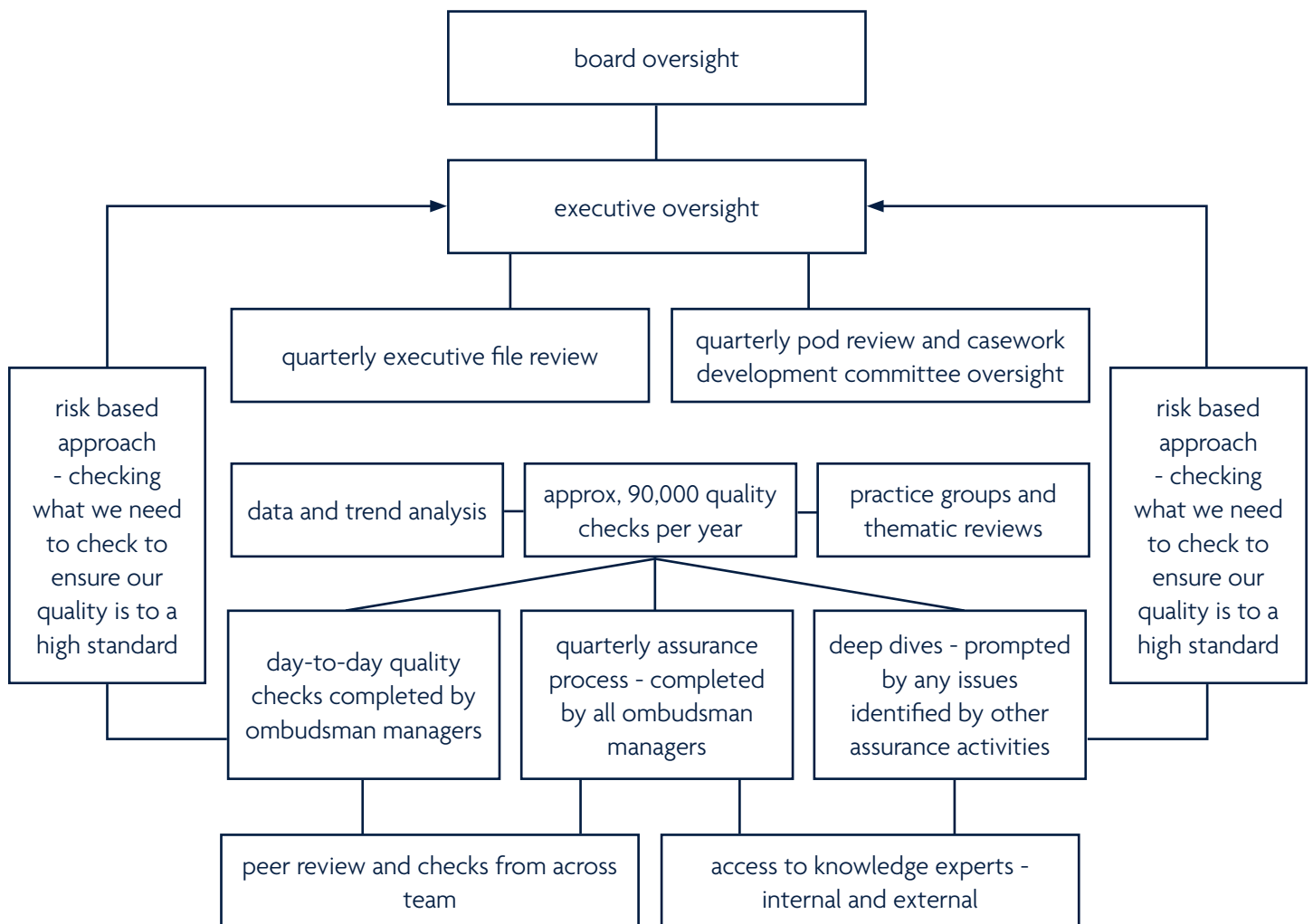


24. According to its principles and approach to quality assurance, the FOS operates three main casework areas:
 - mass claims—where the FOS receives complaints in large volumes (e.g. relating to PPI, packaged bank accounts and short-term lending cases);
 - investigation—complaints relating to banking and credit, insurance, pensions and investment cases; and
 - managed operations—where its flexible contractor workforce handles a mixture of mass claims and other casework.¹⁴
25. While granular information on the FOS's internal operations is not widely published, we understand the exact processes followed in these main areas may differ slightly to reflect the nature of the work.
26. We further understand the FOS implemented a “wider-implications process” in around 2004. This was intended to deal with situations where complaints were indicative of a potential industry-wide issue (e.g. PPI or card-protection plans). Where such issues were identified, the FOS would raise them with the FCA and the industry to consider how best to resolve them. This process was the subject of consideration by Lord Hunt, with recommendations for improvement. However, there is little publicly available information on the operation of the process, and it is not even clear whether it continues to operate.
27. DISP 3.4 also provides the FOS with a mechanism under which, in certain circumstances, it can refer the merits of a complaint to a court to consider as a test case. The complaints to which this test-case rule applies are those that raise an important or novel point of law. The complainant's consent is required for such a referral. It is not clear whether this mechanism has ever been used.
28. The FOS publishes its decisions as well as other guidance in respect of its decision-making. Importantly, under DISP 1.3.2A, regulated firms should ensure lessons learned as a result of all FOS determinations (even those not specifically involving the firm in question) are effectively applied in future complaint handling. In practice, this means that while the FOS does not apply a system of precedent in its decision-making, its decisions can set a precedent.

QUALITY ASSURANCE

29. The FOS states in its principles and approach to quality assurance that its case-handling model puts its ombudsmen “at the heart” of its casework teams. This means its investigators and adjudicators “can access ombudsmen's knowledge and experience of finding fair answers to complaints, to help them reach their own conclusions about individual complaints.” Its ombudsmen work together across its professional subject-matter practice groups “to ensure consistency in their thinking and approach.”
30. While the case-handling processes followed in the FOS's three main casework areas differ, as noted above, its “principles and approach to quality assurance remain the same.” It appears to follow an extensive quality-assurance framework at all levels, from individual case-handlers to the executive.
31. In addition to the FOS's quality-checking activity, it employs a separate team of quality specialists to help identify common themes and coordinate activity so lessons learned are shared across the whole organisation.

¹⁴ <https://www.financial-ombudsman.org.uk/files/3094/our-quality-assurance-principles.pdf>.



MECHANISMS FOR APPEAL

32. As illustrated by the diagram at paragraph 22, complainants are able to challenge a decision made by the FOS at two different stages.
- They can reject the view of the case-handler or adjudicator and refer the complaint to an ombudsman.
 - They can then reject the ombudsman's decision and refer the complaint to a court or seek judicial review.
33. While a respondent firm is also able to reject a case-handler's or adjudicator's decision, the only avenue for it to contest an ombudsman's decision accepted by the complainant is judicial review. As explored further in section 4, there are significant limitations to this appeal mechanism.

COMPARATIVE ARRANGEMENTS

34. Comparing the FOS with other statutory ADR services in the UK demonstrates it is an outlier in three particular ways.
- **Value of compensatory awards.** The maximum award the FOS can make (in the case of complaints referred to it on or after 1 April 2020 about acts or omissions by firms on or after 1 April 2019) is £355,000.¹⁵ This is significantly higher than that of other statutory ADR services. By comparison, the Legal Ombudsman can make a maximum award of £50,000.¹⁶ Most of the Legal Ombudsman's awards are under £1,000.¹⁷
 - **Matters under consideration.** The matters under consideration by the FOS are likely to have wider application (e.g. because they relate to a product commonly used by the consumer population) as opposed to simple complaints about a bill received by a consumer of legal services (as considered by the Legal Ombudsman) or of a water company (as considered by the Water Redress Scheme).
 - **Basis of decision-making.** While the basis of decision making is largely the same across statutory ADR services, the discretion the FOS has been given when considering points of law or regulation is much wider than that of its peers. For example, the FOS can “exclude evidence that would otherwise be admissible in a court or include evidence that would not be admissible in a court.”¹⁸
35. A full comparison of UK-based statutory ADR arrangements can be found in annex 2.

PAST REVIEWS OF THE FOS

36. Since its establishment, the FOS has commissioned six reviews of its operation. Of particular note is Lord's Hunt review and the various submissions made to it in 2008. While conducted some years ago now, this touched on a number of concerns that are equally valid today, in particular:
- the quality of decision making by the FOS;
 - the lack of efficiency in the FOS;
 - the need for improvements and transparency in respect of the FOS's interactions with the FCA;
 - the evolution of the FOS from a decision-making body to a quasi-regulator producing decisions that amount to iterative, retrospective rule-making; and
 - the effectiveness of the mechanisms in place to challenge the FOS's decisions.
37. It is not clear whether or to what extent changes were made by the FOS in response to the various reviews. However, it should be recognised that some of these concerns were also raised by the review of the FOS conducted by Richard Lloyd in 2018, including issues relating to the quality and efficiency of FOS decision making.

¹⁵ <https://www.financial-ombudsman.org.uk/news-events/annual-increase-award-limits>.

¹⁶ Section 138(1) of the Legal Services Act 2007 (as amended).

¹⁷ <https://www.legalombudsman.org.uk/information-centre/factsheets/here-to-help-sort-out-problems-with-your-serviceprovider/>.

¹⁸ <https://www.handbook.fca.org.uk/handbook/DISP/3/5.html>.

4. EVALUATION OF THE FOS

38. The FOS was established to perform a necessary and valuable function. There is a broad consensus that the current process works well for individual complaints. Where a complaint relates to a fact-specific operational or transactional failure, the informality of the FOS process is seen as appropriate. While there are some concerns about consistency, delay and costs, the FOS is generally regarded as fit for purpose in respect of its original remit.
39. However, there have long been concerns that the FOS process is not appropriate for certain types of case.¹⁹ In particular, the requirement for regulated firms to consider the impact of any FOS decision on their operations and treatment of similar complaints means certain decisions are effectively precedent-setting, a power not usually attributed to a statutory ADR service. While a single decision may be valued at £355,000 or less, its economic impact in practice on regulated firms can be significantly more and in extreme cases pose a prudential risk to a firm. Further, in some instances, the value of that impact is unquantifiable, raising legitimate concerns about the basis, quality and proportionality of the FOS's decision-making process.
40. While some of the concerns raised in this paper have been considered in previous reviews of the FOS, they remain entirely valid. Indeed, our members believe them to be even more pronounced now.

WIDER-IMPLICATIONS CASES

41. Although the FOS was established by statute to decide individual complaints, there are cases where its decisions have a wider impact. We recommend HMT consider whether it is appropriate for the FOS to determine complaints with wider impact, particularly given the FOS is not required to apply established legal principles or regulation. The following are just some examples.

INTERPRETATION AND APPLICATION OF REGULATORY REQUIREMENTS

42. As the concept of principles-based regulation has evolved over the past decade or more, firms have been granted some discretion in achieving the right regulatory outcome. Firms use their knowledge and experience to determine how best to deliver compliant products to their customers. This often involves liaising with the FCA as well as lawyers and other advisers. Indeed, a firm's approach to delivering its products and services may well have been reviewed and effectively sanctioned by the FCA.
43. There are many instances of the FOS determining a complaint based on its interpretation of the relevant regulatory requirements. In some cases, this will be limited to the specific facts of the case. In others, where there is a degree of ambiguity about the application of the relevant requirement, this can lead the FOS to make decisions that amount to retrospective rulemaking or guidance on rules, something Parliament specifically sought to avoid. For example, the FOS is often asked to determine complaints relating to affordability. The regulatory requirement for unsecured lending in the Consumer Credit (CONC) section of the FCA Handbook is for firms to take reasonable steps to determine

¹⁹ See, for example, <https://www.bba.org.uk/policy/retail/complaint-handling/fca-thematic-review-on-complaints-handling/thehunt-review/>.

a customer's current income and nondiscretionary expenditure.²⁰ As the FCA intended, this can lead to a variety of approaches to the issue. However, the FOS may decide that where a loan is of a specific term or size, the firm should have obtained bank statements to establish the customer's income and expenditure. Such a decision effectively seeks to define the application of the relevant regulatory requirements. It is an interpretation that applies not just in the specific case but in all similar cases and therefore affects not just the relevant firm but every lender that makes unsecured loans of a certain size or duration. This arguably places the FOS in the role of quasi-regulator, establishing rules across an industry sector without a requirement to consider or consult on the impact of implementing them. This is something the FCA is required to undertake when proposing new rules. First, it is perverse for the FOS to find itself in the position of quasi-regulator without the same due process the FCA is required to follow. Second, the FOS's (unintended) role of quasi-regulator arguably strips away the FCA's role, which cannot be what was intended on the establishment of the FOS. Where the FOS finds itself in this position of quasi-regulator, it should refer such decisions or related trends to the FCA for consideration.

DEFINING RIGHTS AND RESPONSIBILITIES

44. In some cases, the FOS will be called on to determine the respective rights and responsibilities of a firm and its customer. Again, this can lead to decisions that effectively set a precedent for other firms facing similar situations. An example of this is in respect of fraud and scams. In the absence of applicable regulatory requirements, the FOS has made decisions that defined what was expected of the bank and the customer in relation to the particular fraud. While the respective duties may be well defined at law, the FOS is not required to follow those principles. In determining what is a fair and reasonable approach to a particular fraud or type of fraud, the FOS often has recourse to available industry guidance. Again, such interpretation and definition of the obligations of firms is retrospective, sometimes applying today's lens to old complaints, and without any of the rigour adopted by the courts in determining such important issues. Further, in respect of good industry practice, the FOS is only required to take account of what it "considers" to be good industry practice "where appropriate." This subjective approach to considering the law and industry practice can lead to significant deviation from longestablished legal principles and the established workings of the industry in the pursuit of returning monies that were taken from customers, notwithstanding any lack of fault on the part of their bank.
45. These decisions can have potentially far-reaching implications for both the banking and finance sector and society as a whole. In addition, the potential for misinterpretation or misapplication of industry guidance makes firms reluctant to subscribe to such standard-setting initiatives, potentially leading to a lack of cooperation between firms and an increase in the prevalence of fraud. This is undoubtedly a risk to consumers.

²⁰ CONC 5.2A.15 and 5.2A.17.

CONTRACTUAL INTERPRETATION

46. A complaint often involves a question about the correct application or interpretation of a contractual provision. Indeed, the nature of the FOS test is such that the FOS can make decisions about the fairness or reasonableness of a particular contractual term. While this may seem inoffensive, such decisions often run contrary to established legal principles or relevant legislation. A firm may have taken all necessary steps to ensure its customer contracts are compliant with consumer-protection legislation—indeed, a court might well rule the contractual term perfectly legal—but this does not stop the FOS from reaching a different view and holding the clause to be ineffective. While such deviation from legal principles may seem appropriate in a particular case, it is clearly not appropriate where the contract is used for thousands or millions of customers.

THE CASE FOR LEGAL CERTAINTY

47. A central pillar of the UK economy and its attraction for new businesses is the concept of legal certainty. Firms are able to launch new products or services without the fear of retrospective redefinition of their legal rights and obligations. When considering the risks associated with a product or service, firms will undertake a detailed assessment and put in place mitigating measures. The one risk factor that cannot be accurately assessed is the potential for the FOS to undermine, many years after the product or service is sold, the fundamental assumptions in the decisions a firm makes.
48. As illustrated above, decisions of the FOS that are not consistent with preexisting law and regulatory standards create significant uncertainty and the risk of retrospective assessment of conduct. Our members advise us this uncertainty has a chilling effect on innovation and leads to reluctance to consider new products or services.
49. This position is exacerbated by the limited avenues available to challenge the FOS's decisions. This effectively allows the FOS to create its own jurisprudence without sufficient checks and balances or the need for consistency with established law and regulation.
50. As noted in section 3, there are mechanisms in place to address the wider implications of a specific case or cohort of cases. However, these have not proven to be effective in addressing the need for legal certainty.
51. The wider-implications process was established to identify potential mass-consumer detriment. It is clear the FOS is well placed to identify the emergence of industry-wide issues. For example, if it begins to receive a large number of complaints relating to a particular product or service (e.g. PPI), this may be indicative of a thematic issue. It does not address the issue of the FOS's own decisions giving rise to wider implications. It is also rarely called on, appearing not to have been used in more than a decade.
52. While the test-case rule is a clear recognition that some issues are better decided by the courts, the process is dependent on the FOS recognising the issue and the customer consenting to a referral to the courts. This perhaps explains why it is used so infrequently, if ever.

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53. As noted above, the courts have a role to play in overseeing final FOS decisions, principally through judicial review. However, it is widely accepted that the use of judicial review is an ineffective method of challenging the FOS. In practice, it is extremely difficult to bring a successful application for judicial review. The threshold for judicial review is very high, and the court rarely grants permission to challenge the FOS's decisions. Indeed, 73 per cent of judicial-review cases brought against the FOS since 2010 have been dismissed.²¹
54. Even if successful, the practical application of judicial review as an appeals mechanism is limited. The process cannot be used to recast a decision that has been challenged or (except where the purpose of the review is to consider its legality) to enquire into the merits of the decision. It can only review the process by which the decision was reached in order to assess whether that decision was flawed. The best a firm can hope for, if successful, is for the court to direct the FOS to reconsider the original decision reached in relation to the particular complaint. Further, any judicial review of a FOS decision is likely to be limited to the individual facts of the particular matter and is therefore not a useful method for ensuring robust precedent in respect of cases that have wider implications.
55. Moreover, the importance of maintaining effective engagement with the FOS means larger firms in particular are loathe to pursue a judicial challenge. A consequence of this and the limited value that judicial review provides means this appeal mechanism is seldom used in practice and wholly inadequate to deal with the array of potential wide-implication scenarios.²²

²¹ This figure is based on the analysis of the outcomes of judicial-review case law against the FOS between 2010 and 2020

²² See also <https://www.ukfinance.org.uk/policy-and-guidance/consultation-responses/uk-finance-response-independent-review-administrative-law-call-evidence>.

5. OPTIONS FOR IMPROVEMENT OR REFORM

56. While the current statutory FOS process is appropriate for the resolution of individual cases, it does not provide a sufficient, robust or proportionate process for determining cases that have significantly wider implications.
57. There are a number of potential solutions. These include:
- the adoption by the FOS of a more consultative and collaborative process for complaint decisions that seek to fill in perceived gaps in regulation with policy or precedent implications. Openly collaborating with the FCA and others on the approach to deciding such complaints is important, with each body fulfilling its intended role and providing more rigour and accountability in respect of such complaints;
 - the creation of a new decision-making process that can consider cases with wider implications in a way that provides more certainty and efficiency, leaving the FOS to consider those relatively minor complaints, whether from consumers or SMEs, decided on their individual merit that it was established to consider. This could involve the establishment of a decision-making panel, able to provide a more proportionate degree of analysis and consideration of applicable law and regulation, that can make decisions on complaints itself or make recommendations to the FOS. As explained further below, the application of a new decision-making process will likely provide more certainty in decision making and efficiency to the FOS; and
 - the establishment of a new appeals mechanism to provide customers and firms with an effective and robust route for testing FOS decisions.
58. Any change to the current process would need to be the subject of a detailed assessment and consultation exercise that goes beyond the scope of this report. We have, however, provided some further analysis of the above options.

CONSULTATION ON KEY CASES

59. There will be some cases whose wider implications are not immediately apparent. However, the significance of many cases will be apparent to the FOS. For example, it is clear the FOS often identifies the need to make a policy determination in respect of certain cohorts of case. It will often see a large number of particular complaints in respect of an emergent issue (e.g. affordability or authorised-push-payment fraud). It is evident there is some degree of internal debate within the FOS about the appropriate treatment of such cases. However, there is no apparent evidence of engagement with any external stakeholders such as the FCA, firms or consumer bodies. Rather, the FOS reaches an internal “policy” view on the issues, which may be only partially explained in its published decision.
60. The MoU between the FOS and the FCA could be amended at least to the extent that the FCA is engaged in relevant issues. Its provisions already require the two bodies to “seek to achieve a complementary and consistent approach, so far as that is consistent with their independent roles” and “consult one another at an early stage on any issues that might have significant implications for the other organisation.”

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61. While these cooperation provisions are helpful, they provide no detail on how they are implemented in practice and, more importantly, what discussions the FCA and the FOS have in respect of those decisions that fill in interpretative gaps in regulation. To ensure greater rigour and accountability in relation to such discussions, it would be helpful if these were made a matter of public record. Further, the MoU should establish clear guidelines to determine the types of case that will be a matter of discussion between the FCA and the FOS.

A TWIN-TRACK DECISION-MAKING PROCESS

62. As noted, the current FOS process is appropriate for resolving individual, fact-specific complaints. It may, however, be better if cases with wider implications are processed in a different way, either by an expert panel within the FOS or by a different administrative decision-making body. The important point is that the relevant cases would be subject to a more proportionate degree of analysis and consideration of applicable law and regulation. This process would represent a more formal encapsulation of the more collaborative and consultative decision-making process described above, possibly with a panel of relevant stakeholders either deciding cases or making recommendations to the FOS.
63. This twin-track process might alleviate some of the pressures on the FOS. A well-designed and bespoke process for resolving cases with wider implications would allow it to focus its attention on dealing with routine individual cases. This might allow for a more efficient allocation of resource and lead to faster resolution of complaints.

A NEW APPEAL PROCESS

64. A new appeal body would allow for sufficient scrutiny of decisions that have wider implications. Further consideration is required to determine the types of case that would fall to be considered by this body, but any appeal process would clearly need to be limited to certain types of case or risk defeating the purpose of the FOS. In addition to meeting certain threshold criteria, there would also need to be a funding mechanism and processes to ensure consumers were equally able to avail themselves of the right of appeal. The appeal could either be to a court of tribunal, such as the Upper Tribunal (a division of the High Court), or to a new appellate body established for this purpose.
65. It is important to note this right of appeal would only be available in a very small minority of cases, but it should be given to the FOS, firms and the customer. As such, the additional delay to the process would only arise in a few cases and would be fully justified in the interests of ensuring a robust and proportionate process was applied to all cases.

6. OTHER ISSUES IDENTIFIED

66. Inevitably, while looking at the operation of the FOS, further issues were raised that we believe are also important for HMT to consider as part of the FRF review.

DELAY

67. The issue of timeliness has become increasingly problematic as the demands on the FOS have grown. The FOS is now very far from achieving a “quick” resolution of complaints. It is clear the volume and changing nature of the caseload have placed significant pressure on the FOS. While some improvements have been made in this regard, a significant proportion of complaints still take at least 12 months to reach a final decision, and some can take as long as two years to resolve. The FOS does not appear to be held accountable for these delays, which, with the exception of highly complex disputes, fall foul of the 90- day complaint period required by the ADR Regulations.²³ This is a source of frustration for consumers and firms alike. One of the particular problems for firms is the impact this has on their ability to adjust their processes to address the FOS’s findings. For example, if the FOS determines that a firm’s product or service is deficient in some way, the firm needs to know this as soon as possible. In the two years it can take to get a FOS outcome, the firm will incur further and unnecessary liabilities to its customers and deal with complaints in a manner that it will transpire is not in accordance with the FOS’s expectation. This point is linked to some of the issues raised in section 5.
68. We recognise the issue of delay is one of concern for Parliament. Questions were asked of the FOS’s chief ombudsman and chief executive at a November 2020 hearing of the Treasury Committee²⁴ and in a subsequent letter from its Chair.²⁵
69. While delay may be solved by increasing the number of adjudicators, it is clear the FOS must look to improve the efficiency of its processes. It should also set service-level agreements. Firms are required to determine complaints within eight weeks, and the FOS should be aiming for a similar response time. Applying this rule to the FOS will ensure its processes are reflective of the quick ADR service Parliament intended, which can only be of benefit to consumers as well as firms.

CONSISTENCY

70. It is clearly not incumbent on the FOS to ensure its decisions are entirely consistent. Indeed, it would be very difficult to ensure absolute consistency. However, the FOS should at least endeavour to achieve a reasonable degree of consistency to its decisions. As noted, firms are obliged to learn from and apply FOS decisions. This is made difficult when decisions set out conflicting approaches to the same or similar facts. The FOS should at least be prepared to consider apparent inconsistencies where these are raised by either party to a complaint.

23 Paragraph 6(d) of Schedule 3 to the Alternative Dispute Resolution for Consumer Disputes (Competent Authorities and Information) Regulations (SI 2015/542) provides that an ADR service will notify the parties of the outcome of a dispute “within a period of 90 days” from the date on which it notifies the parties that it has received the complete complaint file, except in highly complex disputes where it may extend this period.

24 <https://committees.parliament.uk/event/2666/formal-meeting-oral-evidence-session/>.

25 <https://committees.parliament.uk/publications/3608/documents/35093/default/>.

71. Ensuring a reasonable degree of consistency to FOS decisions will benefit not only firms but also customers and the FOS itself. With greater consistency across decisions, firms can be certain of the FOS's position, ensuring its policies and procedures are in alignment, which may lead to customers avoiding the need to refer complaints to the FOS in the first place.

APPLICATION OF INTEREST ON AWARDS

72. DISP 3.7.1 allows FOS determinations to include an interest award against the respondent. The statutory rate of interest of 8 per cent applied to judgement debts was set back in 1984.²⁶ In an ultra-low interest-rate environment, the application of such a high level of interest makes less sense. It is particularly inappropriate when seen against the backdrop of delays in the FOS deciding complaints.

RETROSPECTIVE APPLICATION OF REGULATORY STANDARDS

73. A number of members reported cases where the FOS has applied standards applicable at the present time but not in force at the time the customer received a product or service. For example, we understand the FOS has chosen to extend the limitation period for complaints in cases where the right to refer a matter to the FOS was not explained to the customer, even in cases where the rules at the time did not require such information to be given. The effect of this retrospective application of regulatory standards (i.e. the effective reopening of already-closed cases) creates a level of uncertainty and is in direct conflict with the rules themselves, including DISP 3.3.4 (6).

LIMITATION PERIODS

74. Subject to certain exceptions, customers are able to refer complaints to the FOS up to three years from the date on which they became aware (or ought reasonably to have become aware) there was a cause for complaint (see DISP 2.8.2 (2)(b)). There are similar such latent limitation periods applied in law. However, such rules are subject to a long-stop date, which provides certainty and recognises a person's recollection fades with time and documentary evidence is destroyed as part of companies' usual data-retention policies. An unintended lacuna in the legal position on limitation periods clearly arises in respect of FOS complaints where no long-stop date is applied, leaving the FOS in the unsatisfactory position of potentially determining complaints without the necessary evidence available and firms with open-ended liability for complaints relating to incidents occurring many years earlier.

DETERMINING COMPLAINTS RELATING TO A FIRM'S COMMERCIAL JUDGEMENTS

75. Since 9 July 2015, the FOS has had the ability to determine a complaint relating to the legitimate exercise of a firm's commercial judgement.²⁷ Certain members are of the view that this limits their ability to exercise their own commercial judgement (e.g. in respect of whether to lend to a customer) and arguably extends the FOS's remit from determining complaints to involving itself in matters more appropriately dealt with by firms themselves.

²⁶ <https://www.lexisnexis.co.uk/legal/guidance/interest-on-judgment-debts>.

²⁷ This arose following an amendment to DISP 3.3.4 that removed the FOS's right to dismiss a complaint without reviewing its merits if it concerned the legitimate exercise of a respondent's commercial judgement.

ANNEX 1. READING LIST

Title	Link
Financial Services and Markets Act 2000	https://www.legislation.gov.uk/ukpga/2000/8/contents
Financial Conduct Authority handbook	https://www.handbook.fca.org.uk/handbook
R (on the application of IFG Financial Services v Financial Ombudsman Services [2005] EWHC 1153 (Admin)	https://www.bailii.org/ew/cases/EWHC/Admin/2005/1153.html
R (on the application of Aviva Life and Pensions (UK)) v Financial Ombudsman Service [2017] EWHC 352 (Admin)	http://www.bailii.org/ew/cases/EWHC/Admin/2017/352.html
Hansard	https://hansard.parliament.uk/
Legal Ombudsman: annual report and accounts for the year ending 31 March 2020	https://www.legalombudsman.org.uk/media/h2np2cv4/olc-annual-report-and-accounts-2019-20-web-version.pdf
Legal Ombudsman: overview of annual complaints data 2019/20	https://www.legalombudsman.org.uk/media/bzsl5q2i/200924-overview-of-complaint-summary-final.pdf
Legal Ombudsman: our approach to investigations	https://www.legalombudsman.org.uk/information-centre/factsheets/our-approach-to-investigations/
Legal Ombudsman: quality-assurance update	https://www.legalombudsman.org.uk/media/nmuf04n/101-7-20-quality-assurance-update.pdf
Local Government & Social Care Ombudsman: annual reviews of complaints	https://www.lgo.org.uk/information-centre/reports/annual-review-reports
Local Government and Social Care Ombudsman (LG&SCO): role, duties and powers	https://uk.practicallaw.thomsonreuters.com/4-501-1874
Local Government & Social Care Ombudsman: guidance on jurisdiction	https://www.lgo.org.uk/information-centre/staff-guidance/guidance-on-jurisdiction
Local Government & Social Care Ombudsman: how we deal with your complaint	https://www.lgo.org.uk/make-a-complaint/how-we-deal-with-your-complaint

Title	Link
Lexis Nexis Practice Note: Interest in Judgement Debts	https://www.lexisnexis.co.uk/legal/guidance/interest-on-judgment-debts
Parliamentary and Health Service Ombudsman: annual report and accounts 2019-2020	https://www.ombudsman.org.uk/sites/default/files/The%20Ombudsman%E2%80%99s%20Annual%20Report%20and%20Accounts%202019-2020_Website.pdf
Parliamentary and Health Service Ombudsman: governance statement	https://www.ombudsman.org.uk/about-us/who-we-are/board/governance-statement
Parliamentary and Health Service Ombudsman: how we look into complaints	https://www.ombudsman.org.uk/sites/default/files/PHSO_Stage_Three_Information_leaflet_2019.pdf
Parliamentary and Health Service Ombudsman: ombudsman casework assurance process—oversight and handling arrangements	https://www.ombudsman.org.uk/sites/default/files/page/Ombudsman%20Casework%20Assurance%20process_0.pdf
Pensions Ombudsman: annual report and accounts 2019/20	https://www.pensions-ombudsman.org.uk/sites/default/files/publication/files/TPO-AnnualReport-WEB.pdf
Financial Ombudsman Service: annual reports and accounts	https://www.financial-ombudsman.org.uk/who-we-are/governance-funding/annual-reports-accounts
Financial Ombudsman Service: strategic plans and budget	https://www.financial-ombudsman.org.uk/who-we-are/governance-funding/strategic-plans-budget
Financial Ombudsman Service: board-meeting minutes	https://www.financial-ombudsman.org.uk/who-we-are/governance-funding/board-meetings
Financial Ombudsman Service: quality assurance—our principles and approach	https://www.financial-ombudsman.org.uk/files/3094/our-quality-assurance-principles.pdf
Financial Ombudsman Service: our customer service	https://www.financial-ombudsman.org.uk/who-we-are/service-standards
Water UK: resolving disputes	https://www.water.org.uk/advice-for-customers/resolving-disputes/
Water Redress Scheme: key performance indicators	https://www.cedr.com/consumer/watrs/reports/
Updated Water Redress Scheme case process from 1 September 2020	https://www.cedr.com/wp-content/uploads/2020/08/WATRS-process-flowchart-Aug20.pdf
Memorandum of understanding between the Financial Conduct Authority and the Financial Ombudsman Service	https://www.fca.org.uk/publication/mou/mou-fos.pdf

Title	Link
Memorandum of understanding between the Pensions Ombudsman and the Financial Ombudsman Service	https://www.financial-ombudsman.org.uk/files/2629/memorandum_of_understanding-with-Pensions-Ombudsman-December-2017.pdf
Pensions Ombudsman: overview	https://uk.practicallaw.thomsonreuters.com/5-203-2515
Pensions Ombudsman: procedure for complaint, response and determination	https://uk.practicallaw.thomsonreuters.com/7-203-2802
Pensions Ombudsman: what stages are involved in the complaint process?	https://www.pensions-ombudsman.org.uk/investigation-process
The intersection of commercial powers and complaints: the Financial Ombudsman Service, consumer protection and the courts	https://dialnet.unirioja.es/servlet/articulo?codigo=3036627
Ombudsman Association: service standards framework	https://www.lgo.org.uk/assets/attach/4409/OA17-Service-Standards-2017_Final.pdf
Ombudsman Association service standards framework: Local Government & Social Care Ombudsman	https://www.lgo.org.uk/assets/attach/4349/How-we-assess-and-report-against-OA-SS-Framework-v2.pdf
Report of the independent review of the Financial Ombudsman Service	https://www.financial-ombudsman.org.uk/publications/pdf/independent-review-2018.pdf

ANNEX 2. COMPARISON OF ADR SERVICES

Criteria	Financial Ombudsman Service	Legal Ombudsman (Office for Legal Complaints)	Pensions Ombudsman	Parliamentary and Health Service Ombudsman	Local Government & Social Care Ombudsman	Water Redress Scheme
Source of statutory power	Financial Services and Markets Act 2000	Legal Services Act 2007	Pension Schemes Act 1993; Pensions Act 2004	Parliamentary Commissioner Act 1967; Health Service Commissioners Act 1993	The Local Government Act 1974; The Local Government and Public Involvement in Health Act 2007	N/A
Additional regulatory powers	DISP; Alternative Dispute Resolution (Competent Authorities and Information) Regulations 2015; Online Dispute Resolution (Regulation on consumer ODR) Regulation 2013	Scheme Rules 2019	The Personal and Occupational Pension Schemes (Pensions Ombudsman) Regulations 1996 (SI 1996/2475); The Personal and Occupational Pension Schemes (Pensions Ombudsman) (Procedure) Rules 1995 (SI 1995/1053)	The Regulatory Reform (Collaboration etc. between Ombudsmen) Order 2007 (SI 2007/1889); The Parliamentary Commissioner Order 2007 (SI 2007/3470)	The Regulatory Reform (Collaboration etc. between Ombudsmen) Order 2007 (SI 2007/1889)	Water Scheme Rules 2019
Type of complaint within the ombudsman's jurisdiction	Financial loss; material distress; material inconvenience; the marketing or provision of financial services or products within the FOS's jurisdiction; mortgage endowments	Professional negligence; costs for the firm's services; delayed or unclear communication; loss of documents.	Injustice as a result of maladministration by occupational and personal pension schemes; disputes of facts and law in relation to the said schemes; scheme administrators	Poor service by the NHS, dentists, GPs, private hospitals, DVLA, HMRC, Jobcentre Plus and the Passport Office	Sustained injustice in relation to debt enforcement; transport and highways; housing and council-tax benefits claims; housing-allocation schemes; school admissions; commercial and contractual matters	Inconvenience and stress as a result of the services of water and sewerage companies.
Basis of decision making	Fair and reasonable test, taking into account laws and regulations, codes of practice and what the FOS considers to have been good industry practice	Fair and reasonable in all the circumstances, having regard to such generally accepted principles of good corporate governance as it is reasonable to regard as applicable to it	Disputes of fact and law are decided in accordance with established legal principles; complaints of maladministration are based on the Ombudsman's assessment of the evidence and the fair outcome to the complaint	Whether the public body has acted fairly and properly in accordance with the principles of good administration, good complaint handling and remedy	Whether the action or inaction of an organisation was reasonable, fair and appropriate in all the circumstances	On a balance of probabilities, whether the company has failed to provide its services to the standard one would reasonably expect and, if so, whether the customer has suffered some loss or detriment
Application of legal principles	Y	Y	Y	Y	Y	Y

Criteria	Financial Ombudsman Service	Legal Ombudsman (Office for Legal Complaints)	Pensions Ombudsman	Parliamentary and Health Service Ombudsman	Local Government & Social Care Ombudsman	Water Redress Scheme
Links to internal processes	Not available. Only DISP 3 is available: https://www.handbook.fca.org.uk/handbook/DISP/3.pdf	https://www.legalombudsman.org.uk/information-centre/factsheets/our-approach-to-investigations/	https://www.pensions-ombudsman.org.uk/investigation-process	https://www.ombudsman.org.uk/sites/default/files/PHSO_Stage_Three_Information_leaflet_2019.pdf	https://www.lgo.org.uk/make-a-complaint/how-we-deal-with-your-complaint	https://www.cedr.com/wp-content/uploads/2020/08/WATRS-process-flowchart-Aug20.pdf
Potential case outcome	Money awards up to £355,000; an interest award; costs award or a direction to the firm as the FOS considers just and appropriate	Statutory limit of £50,000; most money awards made are lower than £1,000; refund or waiver of a service provider's costs; an apology from the service provider; completing or correcting work; processing matter within a specific timeframe and return of documents	Direction to the firm; money award for distress and inconvenience (generally no more than £500 but may go up to £2,500-£3,000 for severe distress); costs award (although this is rare)	Request an organisation take action; an apology; money awards	Recommend how an organisation put things right (including money awards); request an apology	Recommend the best way to resolve the dispute; money awards up to £25,000 per customer per household
Where available, detail of internal process for the review of case outcome	N/A	N/A	https://www.pensions-ombudsman.org.uk/sites/default/files/publication/files/Determination%20factsheet.pdf	https://www.ombudsman.org.uk/sites/default/files/Review_and_Feedback_What_to_do_if_you_think_our_decision_is_wrong_form_May_2019_20190503.docx	https://www.lgo.org.uk/assets/attach/2825/Your-complaint-our-decision-leaflet-revised.pdf	N/A
Forum for appeal	Judicial review	Judicial review	High Court but only on a point of law	Ombudsman will consider a review only when there is an error; judicial review	Ombudsman; judicial review.	N/A
Number of judicial-review cases since 2010	24	13	3	11	4	N/A
Number of successful judicial-review challenges	6	4	1	2	3	N/A

