



Our Profession

Consultation Responses

The Hunt Review

Response to the call for evidence to the independent review of the Financial Ombudsman Service by The Association of Independent Financial Advisers

AIFA is the trade association that represents UK regulated independent financial advisers (IFAs). Membership of AIFA is voluntary and on a corporate basis. AIFA currently represents over 80% of IFA firms in the UK.

IFA firms are the leading distribution channel for retail financial products in the UK. They generate over 65% of business by monetary value and are the major sector advising and arranging on investment products in the UK. As such, IFAs represent a dominant force in the maintenance of a competitive and dynamic retail financial services market.

Despite this high volume of business, complaints against IFA firms are relatively low (see annex 1) and even where they are referred to the Ombudsman, less than one in five are upheld. As IFAs are in the main very small firms, their exposure to and dealing with FOS are very limited and there can be years between cases. **They do not have dedicated complaint handlers and often become emotionally involved with a case as they feel their personal integrity is being questioned. As such, we feel that the Ombudsman service needs to recognise the difference in dealing with small intermediary firms and set up a separate division, replicating the success that FSA has had with its Small Firms Division initiative.**

The FOS works on the principle of what is "fair and reasonable" but in our members' experiences, this does not always appear to reflect a two-way application. Members report that FOS has become more process-driven, legalistic and has lost sight of its "arbitration and resolution" ethos. It must be remembered that Ombudsman schemes should provide a cheaper, more approachable, and less "blame oriented" process than the courts or there is little point in their existence. We have concerns that FOS is drifting away from these ideals.

Specific questions

Are there potential improvements to the FOS's working methods at initial contact and subsequently which would improve its accessibility and help to secure fair outcomes for both businesses and complainants? Can any additional

- could assist such businesses in understanding how the Ombudsman Scheme works,
- provide guidance on how to handle individual cases,
- were transparent about the information, and processes, used internally to train staff (so that firms may also learn from them),
- ensure that policy issues in relation to small firms are properly highlighted and deal with complaints against such firms with a full understanding of how such businesses operate.

The right to a hearing and Article 6(1) ECHR

We are concerned that firms lack proper access to FOS in that the Ombudsman has decided that it has complete discretion as to whether to hold a hearing when one is requested by a firm. FOS has the power to make binding decisions against our members for significant amounts of money. It is a source of concern that they cannot insist on a hearing with proper representation. This is a clear breach of Article 6(1) of the European Convention on Human Rights. It reads:

“In the determination of his civil rights and obligations... everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law. Judgement shall be pronounced publicly but the press and public may be excluded in the interest of morals, public order or national security in a democratic society, where the interest of juveniles or the protection of the private life of the parties so require, or to the extent strictly necessary in the opinion of the court in special circumstances where publicity would prejudice the interests of justice.”

The case law only excludes this right where the party concerned has waived it voluntarily or where there is no arguable point of fact or law: *Bramelid v. Sweden* 5 EHRR 249 at pp. 258-259; *Le Comte, Van Leuven and De Meyer v. Belgium* (1981) 4 EHRR 319; *Lightgow v. United Kingdom* 8 EHRR 329 (1986) & *Allan Jacobsson v. Sweden*, European Court of Human Rights, 16 February 1998 at paras. 46-49. FOS is legally no different from an administrative tribunal or civil court with equivalent powers. For these, the European Court of Human Rights has always granted a right to a public hearing even when the amounts at stake are modest. *Scarth v. United Kingdom* 22 July 1999 [1999] ECHR 59.

The FOS should keep records of when a hearing is requested and either allowed or refused. We would have no objection to the complainants being granted the same rights or for any hearing to take place in public. Either way, we would like proper transparency, and for FOS to publish the number of oral hearings etc. requested and

undertaken.

If FOS is unable to grant a hearing, it must instead provide for an appeal by way of re-hearing including a hearing against decisions of the Ombudsman.

Otherwise, there should be an appeal on a point of law or fairness and reasonableness in the same way as the courts provide one.

Are there any particular improvements which would assist potentially vulnerable groups? (para 3.3-3.11)

Case fees in particular where FOS declines jurisdiction

Vulnerable groups include small IFAs and mortgage intermediaries. We support FOS's proposal to institute a system offering 10 free cases. For small firms, the case fee can be a significant burden. FOS was created to provide a less costly alternative to the courts. With a £400 case fee, costs are well in excess of those that apply to the small claims court and procedures are more onerous. Multiple complaints, typically generated by Claims Management Companies (CMCs) with little substance, can cause severe financial hardship to a small firm. *"I should not be forced out of business proving my innocence"* was a statement made by a sole trader member following 11 cases, all rejected by FOS but charged to the firm.

Complaints against such firms constitute a miniscule proportion of the Ombudsman's caseload. According to the FOS Annual Review 2006-2007, only 2.8% of firms have more than 10 cases each. These firms, predominantly banks and insurance companies, have a much worse track record of having their complaints upheld even in the current period of intense mortgage endowment complaints.

One particular area of concern and unfairness for our smaller members concerns the charging of case fees where the Ombudsman declines jurisdiction generally, under DISP 2.3 and 3.3.1. Currently, FOS charges a case fee in these cases if it is not immediately apparent from a cursory examination of the complaint and the final response, that the case should be dismissed without investigation: FEES 5.5.1 and Glossary definition of "chargeable case". This is unfair where the firm has initially and correctly objected to FOS's jurisdiction. It should not have to pay a case fee for the investigation of something that should not have been submitted to the Ombudsman in the first place. This has been a particular problem with mortgage endowments where product providers have been unable to provide copies of red letters to the IFA, FOS has then asked for them, concluded that the case is time-barred and yet still charged the IFA a case fee.

It remains of concern to our members that they have to pay case fees regardless of the result of the case. Since IFAs win a disproportionately high number of cases at FOS, they carry a burden out of all proportion to the unfairness that consumers suffer. This would be partly rectified by a higher number of free cases.

One side of accessibility is that consumers must use it responsibly. Many of our members would like to see complainants put down a small deposit on the lines of the one required by the ABTA travel arbitration scheme. At the very least, the FSA could indicate the need for responsible behaviour by complainants by using the power in the

FSMA to allow FOS to order a complainant to pay the Scheme's costs. That could replace the case fee in an appropriate situation, for example where there is a clear attempt to abuse the service. A few well publicised cases, particularly if driven by CMCs, would deter dishonest and fraudulent complaints.

Summary dismissal of complaints

FOS should in any event publicise its dismissals on the basis of DISP 3.3.1(1-4) and explain in more detail the criteria it uses for this purpose. This would make FOS more accountable and make it easier for our members to judge when they should seek dismissal of a complaint on these grounds. Equally, those assisting complainants could see the types of situation where referring a case to FOS would be pointless.

FOS should also publish information on the number of cases dismissed as frivolous or vexatious (if any). Examples demonstrating the interpretation of these terms would also be helpful.

Time-bars and the absence of a long-stop in DISP 2.3

Small firms are particularly badly affected by the absence of any long-stop in the time-barring rules. They are currently exposed to complaints relating to events 19 years ago. Few can keep records for anything like that long. While the analogy with the Limitation Act is incomplete, it makes sense to have a length of time beyond which complaints cannot be made. It may be appropriate to have a different rule for product providers because they have to keep records relating to an ongoing product. However, for advisers, some form of backstop which should not be more than 15 years and realistically shorter than that, say 10 years. Beyond that time, memories fade and complaints cannot be effectively investigated. Currently, too many complaints are upheld against firms who do not have the records to defend themselves properly.

As the RDR Discussion Papers point out, the continued exposure of firms to ancient claims merely exposes the FSCS to further claims against incorporated firms and clouds the retirement years of those who have not incorporated.

IFAs would not expect a repetition of DISP 2.3.6's extension of the time to complain. The three year limit in DISP 2.3 should run from the date on which a reasonable customer would appreciate that there was a problem with his investment or the purpose for which it was set up.

Retrospection

Finally, small firms are particularly vulnerable to FOS making decisions on the basis of retrospective standards. The objective of AIFA's Stakes in the Ground initiative was to address this concern and we would appreciate contributions from all sectors, including consumers, in developing this initiative further. In particular, firms are concerned that the failure of consumers to react to offers of subsequent advice is exposing them inappropriately to liability, or greater liability, than would otherwise be the case. Clear

guidelines on capping liability would help greatly to protect smaller firms.

FOS's refusal to do the calculations

One final problem is FOS's continued refusal to do the calculations when it makes an award. Sir Michael Barnes in the 2006-2007 Annual Review at p. 75 drew attention to this problem and had been re-assured that it would not recur. It is still going on, placing great strain on small IFAs who do not have the resources to do the calculations themselves. Consumers are also in no position to check the calculations. As Sir Michael said:

"In my annual report last year, I drew attention to the problems that can arise for consumers, when ombudsmen make "formulaic" awards which require firms themselves to calculate the actual amount of compensation due to the consumer. I very much welcome the board's response to my concerns. I understand that steps are being taken in this area. In particular, the ombudsmen are now making greater effort to specify the exact amount of compensation awarded – wherever they have the specific detailed information needed for this calculation.

However, I am still receiving a number of complaints about redress calculations carried out following final decisions by ombudsmen. One pension case graphically illustrated the wide variations that can exist between the level of compensation that the parties understand the ombudsman to have awarded – and the actual amount payable when the final calculations have been made.

In the case in question, the consumer's financial advisers considered that the redress due was in the region of £130,000. The firm must have taken the same view, because shortly after the ombudsman issued the final decision, it offered the consumer £100,000 (the maximum amount binding on the firm). The consumer did not accept the firm's offer and instead held out for the higher amount estimated by her advisers. When the final (admittedly complicated) calculations were complete, the actual amount of compensation due was found to be only £25,700."

We share Sir Michael's concerns not only for consumers but for the firms that have to make the calculations.

How far is a material - or perceived - barrier to accessibility created by the eight-week period businesses are granted to resolve complaints before they can be considered by the FOS? (para 3.3-3.11)

We do not see this as a particular problem.

What evidence do you have on the current effectiveness of the FOS in reaching individual consumers directly and/or through trusted third parties? (para 3.12-3.18)

Our only concern is that sometimes so much effort is made that this has an impact on the FOS's budget for resolving cases. The cost-effectiveness of some of the efforts needs

to be monitored to ensure that it provides value for money.

Are you aware of good practice on accessibility within your own organisation or elsewhere that the FOS should consider adopting? (para 3.12-3.18)

We suggest that FOS discuss this matter with FSA's Financial Capability team as there may be lessons that can be shared across both organisations. This will also help to minimise work and costs that may otherwise be duplicated.

How should the FOS approach the identification and targeting of under-represented groups? (para 3.12-3.18)

Again, we feel there could be lessons from FSA's Financial Capability work that FOS could learn from. Our only concern is to make sure that the efforts are proportionate and cost-effective.

We query the notion of the meaning of "under represented groups" and wonder why FOS would encourage complaints from people who may well be satisfied with the products or service they have bought. We feel strongly that it is not the role of an arbitration and dispute resolution service to entice consumers to complain.

How far do the FOS's practices enable or limit the ability of businesses (in particular small businesses) to understand how they can best participate in and contribute to a satisfactory resolution of complaints made against them? (para 3.19-3.22)

A Small Firms Division could increase the effectiveness of the assistance provided to businesses. It would also ensure that staff have the necessary awareness of how small firms work. It would also be a good idea if Ombudsman News and other FOS technical papers devoted more attention to difficulties encountered by small firms. Currently, the relevant material is far more directed at insurers and banks. We suggest that FOS considers better targeted communications, perhaps with different branding, more clearly aimed at smaller firms and their particular concerns.

Another concern we have is the way in which FOS effectively operates as a regulator when resolving disputes and then publicising outcomes in Ombudsman News. We appreciate that the Ombudsman cannot consult the industry every time it decides a case. However, the tone of its publications should be more consultative than they are at present and should invite comment. If one had the feeling that FOS were open to changing its mind and had done so in response to reaction to their publications, firms would be more inclined to contribute to the relevant discussions. In its early days, FOS did conduct some consultations in relation to the failure to collect insurance premiums and mortgage payments. We would encourage this practice and like to see more of its publications being framed in more "minded to" terms and inviting a response and seeing that the responses are taken into account in changing policy for future cases.

What should the priority areas be for business outreach? (para 3.19-3.22)

See our answers to the previous questions: especially the creation of a Small Firms Division which would be empowered to act in the ways we have set out.

What priority for investment should improving accessibility have within the FOS's broader agenda? (para 3.23-3.26)

The creation of a Small Firms Division should be FOS' top priority as 90% of regulated firms are labelled as "small" (by FSA) and yet have no clearly identified resource allocated to their needs.

The cost-effectiveness of other efforts should not come at the expense of proper fair procedures handled by well-qualified and trained staff. We think FOS should work in conjunction with FSA on financial capability – and also discuss these matters with Otto Thoresen's team working on Generic Financial Advice.

What should its accessibility priorities be – should they differ between different elements of its work? (para 3.23-3.26)

Again, we believe FOS's priority should be to create a Small firms Division. 90% of regulated forms are classified by FSA as small yet they are generally treated by FOS in the same way as the large financial institutions who attract the vast majority of complaints and whose corporate structures and governance bear no resemblance to small intermediary firms.

Can FOS information make the market work better?

Should the FOS publish all or some adjudication and/or formal ombudsman decisions? What reasons are there for or against publication? What practical issues (e.g. on selection criteria, anonymity, approach to summarising, regularity and form of publication) would arise and how should they be resolved? (para 4.4-4.11)

We think that FOS should publish on a no-names basis any "lead" case which is likely to set an informal precedent as to how a particular type of complaint or issue will be handled. The same applies to any case that is decided using the wider implications procedure. This should invite comment from readers and leave it open as to whether FOS will not change its mind in the future in response to such comments.

Given FSA's move towards a more principle based regulatory regime, firms will have to improve their "regulatory scan" to observe what is accepted custom and practice. AIFA's Stakes in the Ground will be an important part of this "scan" and we are pursuing this through the RDR to make it an industry-wide project.

However, firms will also pay even closer attention to FOS' decisions. This risks FOS becoming a second-tier regulator so it is essential that ombudsman decisions are transparent and that new trends are identified quickly so that the industry may respond.

How can the FOS best develop and communicate its policies and practices in a manner consistent with principle-based regulation? (para 4.12-4.18)

FOS should be more transparent about the processes and criteria it uses in determining cases. Any internal guidance on assessing particular complaints should be available to the relevant sector.

The points made earlier about the need for publications to take the form of effective consultations apply here. It becomes more important than ever that FOS does not make significant numbers of decisions on points not covered by the rulebook without being open to public persuasion that it is mistaken.

We are concerned that FOS needs to research properly what is regarded and what was, at the time of the events complained about, good practice through considering the literature published at that time in specialised journals and books and industry guidance such as the AIFA "Stakes" work on With Profits.

See our answer to the next question in relation to the problem of joint-liability and the relationship between distributors and providers and their respective responsibilities to the client. The FSA has developed guidance on a principles-basis which cannot be effectively enforced without the changes set out in the next section.

Within the broad remit of current FSMA and DISP rules, to what extent should the FOS align its practices with those of the legal system? (para 4.12-4.18)

We have already made the point about the need for a backstop to protect firms from having to retain files for ever. This could be the 15 years in the Limitation Act or another period ideally shorter than that after which recollections become stale and record-keeping obligations create real problems for small firms. We recommend 10 years at most.

A major problem concerns the formal absence at present of any joint-liability process. We appreciate that the proposed new DISP 3.5.3G would encourage the Ombudsman to decide which firm should be responsible for what in such cases. However, it is important that respondents at FOS should be able to join other firms in complaints even in the absence of the complainant's consent.

More generally, in a joint liability case, FOS should not be dealing with the complaint against one firm separately from the other. Currently, FOS has no effective means of dealing with these multiple responsibility cases in a fair way, leaving product providers able to argue in court and FOS that they owe no duty of care to customers that they have never met face-to-face with respect to deficit marketing literature: *Seymour v. Ockwell*.

We have already indicated that FOS is breaking Article 6(1) of the European Convention on Human Rights by making awards without hearings when these are requested in arguable cases by the firm.

Equally, a court would not leave a decision up to the firm to calculate damages. That

needs to be changed.

How effective in enabling you to understand and inform the policy and practice of the FOS do you find the FOS publications; telephone helplines, website; and industry/consumer liaison arrangements? How are these sources used within your organisation? (para 4.19-4.22)

We have found these helpful. The most popular sources of information have been presentations by FOS personnel at AIFA conferences and events. We would hope that a Small Firms Division would undertake far more public appearances with staff specifically trained on dealing with smaller firms' concerns.

Do you use any others? What else would you value? (para 4.19 – 4.22)

FSA website and others relevant to this industry.

Why has the IWI procedure been relatively little used? What additional changes are needed? (para 4.19 – 4.22)

People do not understand the definition of a wider implications case. The process is introduced too late in the case. For firms, it can be a huge gamble, creating the risk of a general obligation to compensate customers where none previously existed. The process needs to be more transparent on all these points.

FOS should be quicker to identify a potential IWI case. An example is Single Premium Payment Protection Insurance, where, with regulatory oversight, the product has been sold in a certain manner for many years. FOS is currently finding against advisory firms on a range of criteria, many of which relate to product features and are outside the control of the adviser. It is a complex matter and one that should have been identified as a case with wider implications and debated with FSA and industry experts prior to any adjudications.

There is some concern expressed by firms that FOS disallows too many cases from entering the IWI process. More transparency on this issue is needed.

What is the appropriate balance for the FOS between reasonable claims for confidentiality and modern expectations of openness? What are the lessons from other sectors? (para 4.23-4.29)

What level of information should the FOS put into the public domain about outcomes of cases by individual businesses? What would be the consequences? What should be withheld and why? (para 4.23-4.29)

Firms with particularly high levels of complaints upheld and received, considering the nature of their firms, should be named and shamed with the relevant numbers publicised. FOS can always seek submissions from the firm as to whether publication

would be appropriate and as to any commentary that should accompany publication. FOS should not be put off publishing data just because the FSA is not interested in taking action against the firm or is in fact taking action.

There is an example in Sharon Gilad's 2006 doctorate, An Intra-Organisational Perspective on the Role of Consumer Complaint Handling in the UK Retail Investment Regulatory Regime (1981-2004), PhD thesis, Oxford University 2006 at pp. 306-310 of a firm whose identity she hides with a significant precipice bond problem that lost a great number of cases without the FSA revealing its identity. This company may have persisted in fighting cases because it knew that the risk of publicity was modest.

If more data were to be made publicly available, what practical issues would need to be overcome in relation to: data quality and timeliness; fair presentation; and accessibility for the needs of different audiences? What sort of qualifications, or "health warnings", if any, would need to be attached to them? (para 4.23-4.29)

FOS can be relied upon to add commentary as required after consultation with the firm.

What level of transparency should there be in communication between the FOS and the FSA and OFT? (para 4.30-4.34)

Exchanges should be publicised to the extent that they relate to policy or principles to be adopted by FOS in deciding cases. Where a firm is referred to the FSA by FOS for disciplinary purposes, it would help to know this on a no-names basis.

AIFA

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Annex 1

IFA Complaints 2006/2007

Complaints about banks and general insurers in 2006/2007 rose by 4% on previous year. This compares with disputes involving IFAs which fell by 2%.

Financial services firms complained about by sector	
IFA firms	12%
Life insurance & product providers	37%
Banks	30%

Complaints about mortgage endowments	
IFA firms	21%
Life insurance & product providers	54%
Banks	19%

Complaints about Personal Pensions	
IFA firms	16%
Life insurance & product providers	72%
Banks	8%

Complaints about other investment products	
IFA firms	12%
Life insurance & product providers	63%
Banks	17%

1. *Annual Review Financial Year 2006/07*, Financial Ombudsman Service