



*All Party Parliamentary Group on*

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**Insurance &**

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**Financial Services**

**Report into the  
Financial  
Ombudsman  
Service and the  
Hunt Review**

**January 2008**

[www.appgifs.org.uk](http://www.appgifs.org.uk)

## Introduction

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The Financial Ombudsman Service is increasingly used by policyholders and firms alike across the financial services sector as a means of resolving disputes and complaints without recourse to the courts.

In the year ending 31 March 2007 no less than 627,814 cases were referred to the FOS for opinion. Of 111,673 cases accepted as appropriate complaints for FOS to investigate, 94% were resolved informally leaving just 6,482 cases requiring the Ombudsman to make a determination by either upholding or rejecting the complaint.

This number of disputed cases may seem small when set against the many millions of individual policies, investments or banking transactions each year. However, the fact is that but for the FOS the only alternative avenue for rectifying alleged consumer detriment would be through the courts which, on cost grounds alone, is simply not a realistic option for most complaints.

Although there will of course be cases where the nature of an individual case can more appropriately be pursued through legal action, the FOS will increasingly be seen as the better option for the vast majority of consumers seeking a remedy for perceived injustice.

Nevertheless, the FOS is not above criticism and the APPGIFS welcomed the opportunity to review some key aspects of how the FOS currently operates and consider how it might change to make the service more effective.

Having heard from several stakeholders, including the chief ombudsman, Walter Merricks, we set out in this brief report our findings and recommendations for consideration by Lord Hunt and his review team.

The FOS is a vitally important feature of the insurance and financial services market which adds value to policyholders and investors. It's in the interests of both consumers and firms that the FOS functions well and is seen to be fair and independent.

We hope that the ideas in this report will help Lord Hunt's review and lead to a better FOS in the years ahead.



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# Report of an enquiry into the Financial Ombudsman Service and the Hunt Review of the FOS

## November – December 2007

### Key Points and Recommendations

- Maintain and promote a robust independence from the industry and the regulator
- Provide more detailed explanations for decisions
- Raise substantially – or remove altogether – the £100,000 limit on binding awards the FOS can make
- Permit cases to be reopened when new evidence becomes available
- Produce clearer codification and communication of the review process
- Improve the process for raising matters of wider significance
- Access fees: no fees should be imposed for taking cases to the FOS
- Consider establishing an independent appeals tribunal

### Background

The Financial Ombudsman Service (FOS) was created as a single compulsory scheme to bring together six pre-existing schemes under a statutory wrapper within the remit of the Financial Services and Markets Act (FSMA). Its scope has since been expanded to cover activities newly-regulated by the Financial Services Authority (FSA), such as businesses with standard consumer credit licences and National Savings & Investments.

Following its formation, the FOS quickly became engulfed in the mortgage endowment mis-selling crisis, creating a massive workload for the new body. The timing of this episode meant that the FOS had limited opportunity to consider properly and formally how the new scheme should operate and adapt from its predecessor voluntary scheme arrangements, and position itself in the context of the changing regulatory environment and the growing powers of the consumer.

In addition, while not a public body, the FOS wants to assess the implications on its operations of the principles of the Freedom of Information Act.

Accordingly, it has commissioned an independent review of its operation. Lord Hunt of Wirral MBE, who is one of the APPGIFS's deputy chairmen, is carrying out this review, whose remit is centred on two key areas – Openness and Accessibility.

In launching the review, Lord Hunt said "...it [FOS] needs to be readily accessible to all consumers, particularly more vulnerable ones, and to listen and communicate effectively with an ever growing number of businesses. My review will assess how well it is doing this and point to any areas of improvement. So I want the Review to stimulate wide ranging debate amongst industry and consumer groups about the effectiveness of what the FOS does at present, where it should build on current progress and where practices might change."

### The APPGIFS review

The group decided to devote a significant part of its autumn 2007 programme to examining the FOS in the context of the issues raised by the Hunt Review. It received a series of presentations in November covering a wide spectrum of views on the FOS. This paper summarises those views and the group's key conclusions, which are being submitted to Lord Hunt.

### The Main Topics

#### Openness and accessibility

In the first session, the chief ombudsman, Walter Merricks, briefed the group on the background to the Review and the remit for Lord Hunt.

Regarding Openness, he indicated that the FOS was experiencing increasing pressures from consumers for information about market participants and their complaints records. He also recognised the appetite of the financial services sector for more information from the FOS regarding the FOS's accumulated knowledge of cases and its experience of opining on them.

On Accessibility, Mr Merricks recognised that the FOS operates from a single office in London and deals with an increasing number of smaller firms. He is looking for comment on the appropriateness of the FOS's accessibility to both consumers and firms, the mechanisms by which interested parties can access the FOS and the way in which it communicates with them.

#### Changing consumer habits and claims culture

Generally, there is widespread support for the FOS, its scope and its funding (which incurs no direct cost to the consumer). However, there is strong support for the current review which many see as an ideal opportunity to assess the effectiveness of the FOS's existing processes and protocols and take stock of the impact of external factors.

Key among these issues are matters such as the growth in internet sales, the growth in claims management companies and the use of their automated complaint letters.

### **Role of the FOS in the context of the Financial Services Authority's move to principles based regulation**

There is clearly a concern as to the role of the FOS in context of the FSA's move towards a principles based regime, particularly regarding the Treating Customers Fairly principle. The key concern stems from differing interpretations – management's interpretation of TCF within the business, the FSA view of TCF around its specified outcomes and the FOS's view of what is fair and reasonable in all the circumstances of an individual case.

The industry says retrospective judgements regarding what is deemed by the FOS as unfair have the ability to undermine significantly the financial services industry as a whole and management's ability to operate with confidence under a principles based regime.

### **Perceptions of the independence of FOS**

There is a recognition that FOS needs to be funded by the financial services sector: other options have greater disadvantages. However, it was felt that more could be done to improve the perceptions of the independence of the FOS in the eyes of consumers and consumer groups.

It was discussed whether there should be greater transparency of the ability of complainants and companies to refer an initial decision by an adjudicator to an ombudsman, who could consider the issues afresh. In addition, the question of whether there should be a separate appeals tribunal to act as a check and balance to the FOS decision-making process was raised.

At the two year review of the FSMA, the FOS and the FSA consulted publicly and found little industry appetite for an appeal. It was also pointed out that in 2004 the Treasury Select Committee expressed concern that creating a general right of appeal could risk undermining confidence in the current system.

### **Complementarity between the FOS and the FSA**

A view exists that there is a gap emerging between the roles and relationships of the FSA and the FOS. Specifically, it seems that adherence to regulatory requirements is not necessarily a safe haven when it comes to FOS decisions. Where the FOS upholds decisions in the customer's favour, despite the firm believing there has been regulatory adherence, there is reputational damage for the financial services sector. According to the FOS, many cases turn on disputes of fact and firms' staffs do not necessarily follow the procedures established for regulatory adherence.

It is felt that this gap is not intentional, but a consequence of existing processes. Generally, it is felt that more should be done to increase the extent to which the FSA and the FOS work together to avoid unnecessary market disruption. An example quoted related to the payment protection market, where it is felt that the expected alleged mis-selling claims could have been avoided if the FOS had been more vocal.

The FOS argued that, had it been more vocal, it could have been usurping the role of the regulator and could have been accused of advertising for complaints.

### **Promotion of good practice**

It was noted that the FOS is well positioned to publish and promote good practice in order to help to close the gap between the FOS and the FSA, based on its own knowledge and experience of dealing with consumers and firms.

### **The wider implications process**

The wider implications process exists to enable the FOS, FSA and the Office of Fair Trading communicate matters of systemic interest to the industry.

A view exists among both industry and consumers that the wider implications process has been very disappointing in practice. Many market participants feel that the FOS does not currently share information regarding the reasons for key case decisions or raise concerns about potential widespread product failure or mis-selling early enough to prevent significant consumer detriment.

The FOS argued that the process is transparent and pointed out that there are dedicated webpages reviewing the issues that have been raised under the process and the outcomes ([www.wider-implications.info](http://www.wider-implications.info)).

### **Transparency of communications**

It was felt that the FOS could increase and improve its communications of complaints data. However, great care is needed in communicating absolute complaints numbers so as to avoid any potential misunderstanding of relative numbers, especially for larger firms.

Similarly, there is a clear industry view that better communication of reasons for decisions reached would be beneficial to both consumers and market participants alike. From the industry's perspective, it is felt that its ability to respond to decisions is thwarted as a result of this failure to communicate the reasons supporting decisions.

It was noted that, because the reasons for case decisions are communicated only to the relevant parties and not published, market rumours of FOS rulings and the reasons for them attract widespread media coverage and that this is not always helpful.

### **Impact of changes to insurance law following the Law Commission review**

The FOS does not expect any significant impact on its approach if insurance law is more clearly defined following the Law Commission's review, since it believes that the Law Commission's proposals would effectively place in statute much of the FOS's current practice. However, it expects fewer non-disclosure related complaints to arise if the law is changed to reflect modern interpretation and practice (albeit the volumes are modest in overall terms).

### **Non advised sales**

Generally, there is a concern that as a consequence of regulatory uncertainty (including both the FSA's move to principles based regulation and the FOS's restrictions on publicising individual decisions), there is a trend towards non-advised selling, reducing the scope for consumers to obtain advice and redress, although FOS will still consider cases where consumers have been misled by information and documentation.

### **Oral hearings**

It was noted that oral hearings are often declined, although they do take place in a very limited number of cases.

There was a proposal that either party should be allowed to request an oral hearing on payment of a suitable fee, refundable if their case was subsequently upheld.

### **Fees**

Industry representatives felt that consumers should be required to pay a refundable fee, repayable in the event of a successful case, to help to dampen the increasing number of vexatious complaints, particularly arising through the activities of claims management companies.

Consumer representatives did not support this and also felt that claims management firms had an important role to play in representing complainants. The 24 page form consumers complaining of mortgage endowment mis-selling are required to complete was cited as an example of the complexity of the process which can be intimidating to many consumers.

### **Small firms division**

Given the massively increased number of small firms now subject to the compulsory regime, it was felt that the FOS should establish a distinct small firms division to facilitate the handling of cases arising from this sub-sector.

### **Access to the FOS through the internet**

It was noted that the FOS's processes tend to be substantially paper based, and both industry and consumer representatives said consideration must be given to increasing access through the internet. Similarly, better use of the internet for outbound communications might be appropriate.

### **Record keeping by firms**

It was noted that at present there is inconsistency between the FSA's record keeping requirements and the need to hold records to assist in resolution of complaints and FOS cases arising at a later date.

## **Conclusions and recommendations**

### **Accessibility**

#### **Physical access to the FOS**

The group believes that the FOS should consider the benefits of additional access mechanisms, such as the internet, as a means by which complaints can be submitted, logged and tracked, to widen the accessibility for consumers to the ombudsman scheme.

The group sees no merit in seeking to establish one or more satellite offices, as local presence will always be restricted to a relatively small number of locations. However, the group believes that more could be achieved by the FOS in promoting itself directly to consumer networks and groups such as Trading Standards Officers and Citizens Advice.

#### **Consumer awareness**

The group believes that the principal responsibility for improving consumer awareness of the role of the FOS lies (under the regulatory system) with the financial services sector and the FSA. Both should do more to inform consumer of the existence of the FOS and how to access it.

It is, however, essential that the FOS is seen as independent of both regulator and industry. This cannot be achieved by relying solely on both those parties to promote it. It should adopt a more pro-active stance in promoting itself, especially among key consumer groups.

#### **FOS limits**

The group challenges the merit of the existing formal FOS redress limits (eg the limit of £100,000 on binding awards) and recommends a fuller review to determine whether any limit is appropriate anymore. The group would prefer to see the limit abolished altogether, although it accepts that some ceiling may need to be imposed. This would need to be at a level that would prevent the overwhelming majority of complainants contemplating the courts as a viable alternative to the FOS.

The existing limits were established some time ago and have not increased in line with the quantum of financial transactions effected by retail and small business customers. The £100,000 limit was originally adopted by the voluntary Insurance Ombudsman Bureau when it was established in 1981 and was subsequently incorporated into other ombudsman schemes as they were established in the 1980s and 1990s. It is not appropriate over a quarter of a century later.

#### **Small firms division**

The group supports the view that there may be benefit to the financial services sector through the creation of a distinct small firms division within the FOS, not only aimed at dealing with cases from this sub-sector but also aimed at promoting good practice messages to it.

#### **New evidence**

The group believes that further consideration should be given to instances where new evidence is identified after a case is decided which challenges the basis upon which that decision was reached by the FOS initially. This is particularly important to consumers who sign away rights to go to court if they accept the FOS's judgement.

In addition, there would be a need for transparency of the mechanism by which such new evidence would be allowed.

#### **Openness**

#### **Commonality of interpretation**

The group believes that there is a case for greater commonality of interpretation between the FOS and the FSA and believes further work is needed to increase the effectiveness of the gateway between these organisations to the benefit of both consumers and industry participants. This must, however, be done without blurring the important distinctions between the two organisations.

This is increasingly important as principles such as TCF, which are inherently prone to judgement as to the definition of fairness, take hold. This is a significant challenge as the FSA promotes key outcomes while the FOS looks at the actual outcomes for individuals, having regard to all the circumstances. There is potential for conflict and confusion which must be avoided.

### **Communication of data sets**

The group believes there is a case for improved communication of data regarding complaint volumes, but recognises that care is needed as regards both categorisation and relativity.

### **Communication of reasons for decisions**

The group believes there is benefit for both consumers and the financial services sector as a whole in improved communication of the reasons for individual case decisions. It recognises that this is one of the main reasons quoted for dissatisfaction with the FOS by industry participants as, currently, the industry is often perplexed as regards the basis of decision-making by the FOS. Consumers similarly complain that they do not always understand the reasons for adjudications.

It is felt that this will be increasingly important as the FSA's principles based regime gains momentum. There will be a need for greater transparency of FOS decision-making in an environment where firms operate without the safe haven of detailed rules, and as a consequence there is less predictability.

In making the reasons for its decisions known more widely, the FOS must not allow them to become fixed precedents. Industry has to accept that there will be variations depending on the consumer's circumstances and other factors.

The group also believes that the FOS might have a role in promulgating good practices where these are identified to help industry participants improve their standards, although it must guard against allowing itself to become a quasi-regulator.

### **Communication of good practice**

The group supports the view that publication of good practices by the FOS would be beneficial to both consumers and the industry.

### **Reporting wider implications**

The group believes there should be a more effective wider implications process. As well a more pro-active approach by the FOS, industry and other organisations need confidence that when they raise concerns with the FOS, OFT and FSA they will receive appropriate feedback that will lead to proportionate action.

It hopes that recent changes initiated by the FSA will help achieve this but believes there is a need for better transparency of the definition of a wider implications issue and the protocol for its communication in a timely manner.

### **Appeals process**

The group believes there is a need for much better communication of the option to refer an initial decision by an adjudicator to an ombudsman. In addition, there should be a separate, independent appeals tribunal.

## **Other key recommendations**

### **Retrospective judgements**

The group is concerned that FOS judgements which have significant retrospective implications can potentially create reputational damage for the entire marketplace, even though current industry practice may have evolved significantly from that which originally caused concern and gave rise to the complaint(s).

It is also concerned that such judgements create regulatory uncertainty which may lead to a trend towards non advised sales to avoid regulatory uncertainty.

The group urges the FOS to be extremely cautious in the issuing of retrospective judgements and to enter into a dialogue with the relevant industry sectors to avoid unnecessary reputational damage.

### **Cases involving suspected fraud**

The group believes there is a need for an improved mechanism for dealing with complaint cases where there is a suggestion of fraud, which requires investigation beyond the remit of the FOS. In such cases, a protocol for working with the FSA and the police might be appropriate.

There is already a *Memorandum of Understanding* between the FSA and the Association of Chief Police Officers (ACPO). This could be extended.

### **Access fees chargeable to complainants**

The group is not in favour of introducing fees whereby the consumer pays to get access to FOS (even where such fee is refunded where a case is upheld), as it is felt that this might deter some consumers with genuine grievances. The group understands the industry's concerns about mischievous complaints but considers the danger that even one genuine complaint might not be submitted because of the imposition of a fee to be too much of a risk.

However, the group does think that there is a need for greater transparency regarding the FOS's filter processes in place to sift out mischievous complaints.

### **Statutory and non statutory regulation**

The group is concerned by the view that there is a perception of a weaker regulatory regime for retail banking products (current and savings accounts, overdrafts, loans and cards etc) than for other products regulated by the FSA. In light of the increasing emphasis on TCF, while recognising that the concept forms part of the Banking Code, it sees a need for a review of the way in which banking is regulated.

It is recognised that this is clearly beyond the remit of the current review. Accordingly, the group will recommend to the Law Commission that it carries out a review of banking law when it has concluded its current work on insurance.

### **Record retention**

The group recognises the inherent difficulty of record retention (in the context of specific FSA record retention requirements and the need to maintain records to respond to subsequent complaints and FOS cases), but also believes this is a matter for individual firms to determine.

Firms need to acknowledge that consumers have an expectation that full records will be available.

## List of those who made presentations

14 November 2007

Walter Merricks CBE, Chief Ombudsman, Financial Ombudsman Service

21 November 2007

Alison Blackmore, Head of Customer Care, AXA Insurance  
Kevin Carr, Head of Protection Strategy, LifeSearch  
Angela Knight, Chief Executive, British Bankers' Association

28 November 2007

John Howard, Chair, Financial Services Consumer Panel  
Robert Owen, Struggle Against Financial Exploitation (SAFE)



*All Party Parliamentary Group on*

## Insurance & Financial Services

### The group: officers, contacts and background

#### Chairman:

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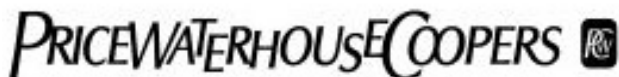
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The group was formed in January 1991 following an initiative by *Post Magazine*, the leading weekly magazine for the insurance industry.

Over the previous three or four years there had been much legislation that had adversely impacted on the insurance industry and it was frequently the target of unjustified criticism by MPs and ministers.

Consultation with interested MPs led to the proposal to form an All Party Group and potential members from both the House of Commons and House of Lords were approached during the autumn of 1990 and sufficient numbers had signed up by the end of November for the formation of the group to be announced at *Post Magazine's* 2nd Parliamentary Reception. It held its inaugural meeting in January 1991.

The late Sir Robert McCrindle, who was the British Insurance Brokers' Association's Parliamentary advisor at the time, was the first chairman of the group. When he stood down from Parliament in 1992, another of the group's founder members, John Greenway, was elected chairman. Labour Peer Baroness Turner of Camden was elected as deputy chairman at the inaugural meeting, a post she still holds today.

In 1992 the group appointed Price Waterhouse as its technical advisers to provide briefings for its meetings and additional technical support, especially when representations have been made to the Treasury or other Government departments.

The group has tackled a wide range of issues over the years and has played a significant part in the formation of Pool Re, the introduction of equalisation reserves, securing compensation for people mis-sold home reversion plans and getting tougher action on uninsured driving. In 2005 it submitted a comprehensive report on the compensation culture which helped shape the 2006 Compensation Act. It meets frequently with the Financial Services Authority and a wide range of organisations representing interests in the insurance and wider financial services sector.

Its brief now ranges across the entire financial services sector, although the administrative and secretarial support is still provided by *Post Magazine's* publishers, Incisive Media.

All full list of members can be found on the group's website [www.appgifs.org.uk](http://www.appgifs.org.uk).

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