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Financial Services Authority and  
Financial Services Ombudsman Scheme:  
a joint consultation paper

## Consumer complaints and the new single ombudsman scheme

November 1999



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The Financial Services Authority and the Financial Services Ombudsman Scheme Limited invite comments on this joint Consultation Paper. Both the FSA and the FSOS (which are currently based at the same address) will receive copies of all responses.

Comments should reach us by 10 February 2000.

Responses should be sent to:

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It is the FSA's policy to make all responses to formal consultation available for public inspection, unless the respondent requests otherwise.

# Executive summary

## Outline of the paper

- 1 This is the second consultation paper on the arrangements which should apply for handling consumer complaints under the new system of financial services regulation. It is issued jointly by the Financial Services Authority (FSA) and the Financial Services Ombudsman Scheme Limited (FSOS), the company which will operate the Scheme, and seeks views on the various rules which the FSA and the FSOS propose to make.
- 2 Part I introduces the paper and sets out the statutory framework and key features of the new Scheme (Chapter 1), together with a summary of progress to date in establishing the new Scheme (Chapter 2).
- 3 Part II sets out the detailed rules which the FSA and the FSOS propose to make in relation to key aspects of the new Scheme's operation. These take account of the responses received to the FSA's earlier consultation paper (CP4) and the relevant provisions of the Financial Services and Markets Bill which was introduced into Parliament in June this year. Part II focuses on three main issues:
  - the scope of the new Scheme (Chapter 3), including proposals for who should have access to the Scheme, which firms and activities the Scheme should cover and what the monetary and territorial limits on the Scheme's scope should be;
  - the Scheme rules (Chapter 4) which will govern the way in which the FSOS will handle complaints; and
  - the funding of the new Scheme (Chapter 5), including proposals for funding the Scheme's operating costs and its establishment costs.
- 4 Part III of this paper (Chapter 6) seeks views on the FSA's proposals for a new, single set of requirements which will apply to FSA authorised firms in handling complaints from consumers.

## Summary of main issues

- 5 The paper seeks views on the following main issues:
- The FSA and the FSOS propose that the new Scheme should be available to all private individuals and certain small businesses, as defined. This would largely mirror the coverage of the existing dispute resolution schemes, but would extend access to small businesses (as complainants) in the insurance sector for the first time.
  - The FSA proposes that all authorised firms which deal with customers who are eligible to use the Scheme (including small businesses as defined) and which are, therefore, capable of giving rise to a complaint which would fall within the Scheme's scope, should be subject to the Compulsory Jurisdiction of the Scheme. However, we propose to consider exempting firms whose permission precludes them from dealing with customers who are eligible to use the Scheme from contributing towards the funding of the Scheme and from having to comply with the complaints-handling rules, as they would not be capable of giving rise to an eligible complaint.
  - The paper discusses the extent to which the different financial services activities of *authorised* firms (including potentially regulated activities) should be covered by the new Scheme's Compulsory Jurisdiction. The FSA proposes that the Compulsory Jurisdiction of the new Scheme should cover all of these firms' regulated activities and, in addition, all of the potentially regulated financial services activities which are currently covered by existing schemes. However, the FSA proposes that the long-term objective should be to extend coverage to all of the financial services activities of authorised firms.
  - The FSOS proposes that the Voluntary Jurisdiction of the new Scheme should, in the first instance, be open to *authorised* firms in respect of any of their financial services activities which are not covered by the Compulsory Jurisdiction and to *unauthorised* firms in respect of mortgage lending (since the majority of mortgage lenders will already be in the Compulsory Jurisdiction by virtue of being authorised firms for their other activities). The FSOS proposes to extend the VJ to cover other financial services activities conducted by *unauthorised* firms in a phased way in order to enable it to manage its workload effectively.
  - The paper outlines the Scheme Rules which the FSOS proposes to make governing the procedures for the handling of complaints under the Scheme (including compliance, where necessary with the requirements of the European Convention on Human Rights). The FSOS does not propose, at this stage, to make rules enabling the Ombudsman to award costs, but will keep this under review in the light of experience.

- The paper seeks views on the funding of the Scheme. The FSA proposes that the Scheme should be funded by an annual levy which would raise 100% of the budgeted operating costs of the Scheme on account at the beginning of the year, with 50% of those costs being reallocated to firms at the end of the year in accordance with their actual usage of the Scheme. The levy would be calculated by reference to a measure of the size of a firm and views are sought on the appropriate measures for different constituencies. The funding mechanism would, however, be kept under close review and refined in the light of the new Scheme's experience and further consultation with the industry.
  - The paper sets out the requirements which the FSA proposes to introduce relating to the way authorised firms handle complaints from consumers. The aim is to give firms flexibility to implement their own procedures within a framework of minimum standards.
- 6 The FSA and the FSOS are seeking views through a number of specific questions which are highlighted in the text. However, we would welcome comments on any aspect of the arrangements set out in this paper.**

# 1 Introduction

- 1.1 This consultation paper sets out detailed proposals relating to key aspects of the Financial Services Ombudsman Scheme, which will replace the eight existing dispute resolution mechanisms in the financial services area.
- 1.2 The statutory framework for the Scheme and the respective responsibilities of the FSA and the Scheme Operator, the separate company which will operate the Scheme, are set out in the Financial Services and Markets Bill. These responsibilities are summarised in paragraphs 1.7 to 1.13 below, but are subject to change during the Bill's passage through Parliament. The proposals set out in this paper are based on the Bill as introduced.
- 1.3 In this paper, references to the 'FSOS' are to the Financial Services Ombudsman Scheme Limited, which has been set up by the FSA to be the Scheme Operator. References to 'the Ombudsman Scheme' or 'the Scheme' are to the legal framework contained in the Bill.
- 1.4 Responsibility for the rules relating to different aspects of the Scheme which will be made under the proposed new legislation is shared between the FSA and the FSOS, and co-ordination is therefore important. The FSA and the FSOS are required to consult on any rules which they propose to make. Where the FSOS has responsibility for making rules, these will require FSA approval. Where the power to make rules rests with the FSA, these are subject both to consultation and to cost benefit analysis.
- 1.5 This paper therefore represents a joint consultation by the FSA and the FSOS on the rules which they propose to make in the respective areas for which they have responsibility. The paper makes it clear who will be responsible for making the rules in each area, but the proposals which it contains are the product of detailed discussions between both bodies.
- 1.6 A further joint consultation paper will be published by the FSA and the FSOS in Spring 2000. This will set out the draft rules which the FSA and the FSOS propose to make in the light of the responses received to this paper and will provide further cost benefit analysis of proposals where appropriate.

## Statutory framework

- 1.7 The Financial Services and Markets Bill provides for the creation of a single Ombudsman scheme (the 'Financial Services Ombudsman Scheme') to handle financial services-related complaints. It requires the FSA to set up a separate company (the 'Scheme Operator') to administer the Scheme, the aim of which is to enable disputes involving consumers to be resolved 'quickly and with minimum formality by an independent person'.
- 1.8 The statutory framework for the new Scheme set out in the Bill recognises the need for the Scheme Operator to be operationally independent of the FSA in the resolution of complaints. However, it also reflects the fact that the FSA will have a strong interest in the effectiveness of the Scheme since the resolution of complaints will form an integral part of its consumer protection objective. The FSOS will therefore be accountable to the FSA in a number of significant respects. The key elements of this balance are as follows.
- 1.9 The FSA will be responsible for:
- appointing the Scheme's Board (with HM Treasury approval in the case of the Chairman);
  - approving the Scheme's budget;
  - determining the scope of the Scheme's Compulsory Jurisdiction (CJ) (and approving the scope of the Voluntary Jurisdiction);
  - defining which complainants should have access to the CJ, the overall monetary limits on awards and the types of loss that may be compensated in the CJ;
  - prescribing time limits for lodging complaints with the Scheme and making rules governing firms' internal complaints procedures;
  - determining fees for authorised firms in the CJ;
  - approving rules to be made by the FSOS;
  - setting rules for formal reporting by the FSOS to the FSA; and
  - ensuring that the FSOS is at all times capable of exercising its statutory functions.
- 1.10 The FSOS Board will be responsible for:
- appointing the Panel of Ombudsmen (including the Chief Ombudsman);
  - determining the scope of the Voluntary Jurisdiction (VJ), (subject to FSA approval);
  - making Scheme Rules relating to the procedures for investigating, considering and determining complaints;

- determining the standard terms and conditions (including award limits, time limits, fees etc) for participation in the VJ;
  - determining case fee rules, if appropriate, in both the CJ and the VJ (subject to FSA approval);
  - recommending an annual budget for approval by the FSA;
  - overseeing the Scheme's overall effectiveness; and
  - reporting to the FSA at least annually on the discharge of its functions (including a separate report by the Chief Ombudsman).
- 1.11 The Chairman and other members of the FSOS Board must be appointed, and are liable to removal from office, by the FSA (acting, in the case of the Chairman, with the approval of HM Treasury). However, the terms of their appointment (and in particular those governing removal from office) must secure their independence from the FSA in the operation of the Scheme. Board members are appointed in the public interest and not as representatives of any particular industry sector or interest group.
- 1.12 The power to appoint the panel of Ombudsmen – including the Chief Ombudsman – rests with the FSOS Board, not the FSA, and, again, their appointments must be on terms (including the duration and termination of the appointments and remuneration) which are consistent with their independence.

### **Accountability**

- 1.13 The FSOS will also be publicly accountable. In particular, the FSOS and the Chief Ombudsman will be required to submit to the FSA, at least annually, reports on the discharge of their respective statutory functions and to publish these reports in an appropriate manner. The FSA proposes to send copies of these reports to HM Treasury and to make them available to Parliament. The FSA will also comment in its own Annual Report on its duty under the Bill to ensure that the Scheme Operator is at all times capable of exercising its statutory functions. In addition, appointment of the Chairman of the FSOS Board requires HM Treasury approval and he may be asked to give evidence to an appropriate Parliamentary Select Committee.

### **FSA's general duties under the Bill**

- 1.14 As well as fulfilling the statutory purpose of the Scheme, the FSA believes that the proposals in this paper will be compatible with its general duties under clause 2 of the Bill. The Scheme will play a key and complementary part in helping the FSA achieve the appropriate degree of protection for retail consumers, and the wide coverage and easy access proposed are regarded as

the best way of achieving this. Although the Scheme will impose a burden on firms, the FSA believes that it will help reduce the need for regulatory intervention and is more than justified by the benefits to consumers and firms which are set out in the relevant sections of this paper. A comprehensive and streamlined service across a wide range of activities is also expected to contribute towards a more level playing field for competition in retail financial services generally.

- 1.15 The FSA does not believe that the Scheme will significantly impact on its remaining regulatory objectives (public awareness, market confidence, and the prevention of financial crime) or other matters to which it must have regard under clause 2(3) of the Bill. However, it believes that its proposals are not inconsistent with these.
- 1.16 **The FSA would welcome comments on the extent to which these proposals achieve the statutory purpose of the Scheme and are compatible with the FSA's general duties.**

## The Financial Services Ombudsman Scheme

- 1.17 The FSOS is expected to be the largest ombudsman scheme in the world, with a budget in the region of £20 million, between 350 – 400 staff and approximately 15 – 20 Ombudsmen. At least 10,000 firms are expected to be subject to the Scheme's Compulsory Jurisdiction, which will apply to FSA authorised firms only. The number of participants who choose to join the Voluntary Jurisdiction (which can include unauthorised firms) will depend on the decisions which the FSOS takes on scope (see Chapter 3).
- 1.18 Based on the experience of the existing schemes, the FSOS can expect to receive each year a minimum of:
- 30,000 written complaints requiring conciliation and/or formal awards;
  - 30,000 written enquiries; and
  - 150,000 telephone enquiries.
- 1.19 The new Scheme will provide a free, simple, informal and accessible alternative to the courts. It will cover similar kinds of disputes to the existing schemes, including, for example, complaints about mis-selling, unsuitable advice, unfair treatment, maladministration, misleading advertising, delay and poor service in relation to products or services provided by financial services firms.
- 1.20 The Scheme will comply with the criteria for Ombudsman schemes set out by the British and Irish Ombudsman Association (BIOA) – independence from the industry; accessibility for complainants; fairness in its decision-making and public accountability.

1.21 Beyond this, the FSOS will aim:

- to provide, as far as possible, a one-stop shop for dealing with disputes about financial services;
- to resolve disputes quickly and with minimum formality;
- to provide a prompt, user-friendly and unbureaucratic service;
- to take decisions which are consistent, fair and reasonable;
- to be cost-effective and efficient;
- to be accessible to all groups in the community, including the vulnerable and the disadvantaged;
- to be regarded as good value by the industry;
- to be forward-looking, adaptable and flexible, making effective use of new technology;
- to be trusted and respected by both consumers, the industry and other interested parties.

1.22 The aim will be for the new Scheme to be more than the sum of its parts – although this is in no way intended to detract from the excellent track record of the existing schemes, on which the FSOS must build. The FSA set up the FSOS, the separate company which will manage the Scheme, earlier this year and is now working closely with the FSOS on detailed planning for the new arrangements. A summary of progress to date is given in the following chapter.

# 2 Progress to date

- 2.1 The FSA published initial proposals for the establishment of a new single Ombudsman Scheme for financial services in December 1997 (CP4 on *Consumer Complaints*). This paper sought views on the arrangements for dispute resolution which should apply once the proposed legislation comes into force.

## Existing dispute resolution mechanisms

- 2.2 The existing dispute resolution schemes which will be replaced by the new single scheme are:
- The Office of the Banking Ombudsman (OBO);
  - The Office of the Building Societies Ombudsman (OBSO);
  - The Office of the Investment Ombudsman (OIO);
  - The Insurance Ombudsman Bureau (IOB);
  - The Personal Investment Authority Ombudsman Bureau (PIAOB);
  - The Personal Insurance Arbitration Service (PIAS);
  - The Securities and Futures Authority Complaints Bureau and Arbitration Service (SFA CB); and
  - The FSA Complaints Unit and Independent Investigator.

## Results of CP4 consultation

- 2.3 Further decisions about the broad structure of the Scheme were taken by the Government in March 1998 in the light of the FSA's analysis of the 200 responses which it received to CP4 and the FSA subsequently published a Policy Statement,<sup>1</sup> outlining, in broad terms, the results of its consultation. This

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<sup>1</sup> *Consumer Complaints: Policy Statement* (August 1998).

described the policy approach which it proposed to adopt, the further work which had been done since the end of the consultation period and the key milestones ahead.

- 2.4 In taking this work forward, the FSA has been very fortunate in being able to draw on the expertise and experience of the existing schemes whose staff have devoted generous amounts of their time to assisting us. In particular, the principal Ombudsmen from the 5 existing Ombudsman schemes<sup>2</sup> participated with the FSA in an Ombudsman Steering Group, chaired by Laurie Slade,<sup>3</sup> which produced a report setting out recommendations on the detailed design of the new Scheme and on the process of bringing the existing schemes together. This drew on the valuable groundwork carried out by 'task forces', made up of representatives from each of the existing schemes and from the FSA, which carried out a detailed 'current state' audit of the schemes in a range of key areas (IT, terms of reference, funding, premises etc.). The FSA has also liaised closely with HM Treasury and has had regular contact with the Boards and Councils of the existing schemes, consumer bodies and trade associations.

## Financial Services and Markets Bill

- 2.5 The Financial Services and Markets Bill, which sets out the statutory framework for the new Scheme, was published by HM Treasury in draft for consultation in July last year. It was also subject earlier this year to scrutiny by a special Parliamentary Joint Committee of the Lords and the Commons, which reported on its conclusions at the end of April this year. As a result of these processes, a number of changes were made to the draft Bill prior to its introduction into Parliament on 17 June 1999. The Bill had its second reading on 28 June and is currently undergoing clause by clause scrutiny by a Standing Committee of the House of Commons. For planning purposes, we are assuming that the Bill will receive Royal Assent around Easter 2000 and that 'commencement' will be in the second half of next year.

## Financial Services Ombudsman Scheme Limited

- 2.6 The FSOS was set up by the FSA in February 1999, in accordance with the current provisions in the Bill.
- 2.7 The new FSOS Board is chaired by Andreas Whittam Smith. A full list of Board members is given at Annex A. All Board members are non-executive and appointed on the grounds of public interest. They were appointed following a Nolan-style selection process on terms designed to secure their independence.

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2 Peter Dean (Investment Ombudsman); Tony Holland (Principal PIA Ombudsman); Walter Merricks (then Insurance Ombudsman); Brian Murphy (then Building Societies Ombudsman); and David Thomas (Banking Ombudsman).

3 Laurie Slade, a former Insurance Ombudsman, who has since resumed the role of Insurance Ombudsman on Walter Merricks' appointment as Chief Ombudsman of the new Scheme.

- 2.8 The FSOS Board (which met for the first time on 1 March this year) will not receive its statutory powers or duties until the Bill has been enacted and Part XV commenced. It currently has no direct operational responsibilities, and complaints continue to be handled by the existing schemes. The FSOS Board is currently working with the FSA on the design of the new Scheme and hopes to bring the eight existing schemes together in advance of the legislation in order to secure the benefits to consumers of a 'one stop shop' at the earliest opportunity. However, until N2, the Scheme will act under the existing legislation or the contractual powers of the current schemes.
- 2.9 A number of senior appointments has already been made. Walter Merricks, the former Insurance Ombudsman, was appointed by the FSOS Board as Chief Ombudsman on 15 June 1999 and formally took up his post on 2 August 1999, and Ian Marshall joined the FSOS as Chief Operating Officer in early October. The FSOS is currently in the process of interviewing candidates for a range of further senior management posts. In the meantime, interim HR and Finance Directors have been taking forward the practical work involved in setting up the new Scheme and the FSOS Board is receiving general policy support from FSA staff.

## Next steps

- 2.10 A significant amount of work remains to be done by both the FSA and the FSOS before the new Scheme becomes operational. Most of this work is already in train, but the responses to this consultation will enable us to take forward some of the more detailed issues relating to the design of the new Scheme.
- 2.11 Co-location of the current schemes is a high priority and work on this front is well advanced. The FSOS has recently announced that it will be based at South Quay Plaza in London's Docklands and the FSOS Board hopes, with the agreement of the current schemes, to be able to bring all the existing schemes together in its new building in April 2000. Other major priorities for the FSOS Board include further senior management appointments; the transfer of staff in the existing schemes to the new Scheme; and finalisation of the Scheme's rules and casework procedures.
- 2.12 The FSA is working closely with the FSOS on the policy framework for the new Scheme. This includes the determination of the scope and funding of the Scheme, the Scheme Rules and the complaints-handling requirements which will apply to FSA- authorised firms. This consultation paper sets out proposals and seeks views on all of these issues.
- 2.13 HM Treasury and the FSA are working together and with the FSOS and the existing schemes, to establish transitional arrangements. The aim is that these should be easy for consumers to understand and that they should impose minimum possible costs on the industry. Proposals will be announced in due course.

# 3 Scope of the Financial Services Ombudsman Scheme

3.1 This chapter sets out the FSA's and the FSOS's proposals for the scope of the new Scheme, which will be contained in the FSA's Compulsory Jurisdiction Rules and the FSOS's Voluntary Jurisdiction Rules. These proposals take account of the responses received to CP4.

3.2 The Bill provides that the Scheme will have two jurisdictions:

**The Compulsory Jurisdiction (CJ)** will cover *authorised* firms only. The CJ can cover not only complaints about regulated activities, but also complaints about the financial services activities of authorised firms which are *potentially* regulated under the Bill. The Rules determining the scope of the CJ will be made by the FSA; and

**The Voluntary Jurisdiction (VJ)** will be open to *unauthorised* as well as *authorised* firms. The VJ can cover any of the potentially regulated financial services activities of *authorised* firms which are not brought into the CJ and specified financial services activities of *unauthorised* firms. The Rules determining the scope of the VJ will be made by the FSOS.

3.3 The CJ and VJ Rules will determine:

- which complainants should have access to the Scheme;
- which firms should be subject to the Scheme;
- which activities should be covered by the Scheme; and
- the territorial coverage of the Scheme.

3.4 In the interests of consistency, the CJ and VJ need to be carefully co-ordinated. In some areas, (eg access to the Scheme, limits on awards and time limits etc), it is clearly desirable for both jurisdictions to have the same requirements. In other areas, (eg those defining the activities to be covered) the rules will be specific to one particular jurisdiction but co-ordination will be necessary to ensure that they are complementary and to avoid gaps and

overlap. The FSA and the FSOS have, therefore, worked closely together in formulating these proposals. The overall aim is that there should be no difference, from a consumer's perspective, between the CJ and VJ in terms of the way a complaint is handled.

- 3.5 The rest of this chapter distinguishes between those proposals which relate to both jurisdictions, and those which relate only to one, and indicates in each case under whose authority the relevant rules will be made.

## Which complainants should have access to the Scheme?

- 3.6 The Bill enables the FSA to define which consumers are eligible to complain to the Scheme under the CJ. It provides the FSOS (with the approval of the FSA) with similar powers in relation to the VJ. The FSA and the FSOS believe that access criteria should be the same across the whole Scheme, and the following proposals therefore relate to both jurisdictions.
- 3.7 Most respondents to CP4 agreed with the FSA that the Scheme should be available to private individuals and some small businesses up to a certain level (see below).
- 3.8 **Private individuals.** The FSA and the FSOS therefore propose that the Scheme should be available to all private individuals.
- 3.9 **Small businesses.** We also propose that the Scheme should be made available to certain kinds of small businesses. As the Government's response to the Parliamentary Joint Committee's report on the draft Bill pointed out,<sup>1</sup> small family firms may be, in practice, in a position which is no different from that of the private consumer. Furthermore, all of the existing schemes, except the Insurance Ombudsman Bureau, currently accept complaints from small businesses. Although in practice, it is only in the banking sector that anything approaching a significant number of complaints is received from small businesses,<sup>2</sup> excluding small businesses from the scope of the new Scheme would represent a reduction in the protection available under the existing schemes.
- 3.10 The key issues are how 'small businesses' should be defined and whether a common definition is appropriate for all sectors of the industry. A common definition of an eligible complainant would seem preferable to one which varies from sector to sector or product to product, both in the interests of consistency and simplicity, and also for practical reasons. Complaints under the new Scheme might, for example, cross previous boundaries – for example,

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1 Paragraph 7.3, page 21.

2 Current data from The Office of the Banking Ombudsman indicates that 6% of total cases received and 17% of cases requiring investigation are from small businesses.

a small business might complain about its treatment under the terms of a commercial loan and a linked insurance policy.

- 3.11 The current schemes' definitions of 'small business' vary. For example, The Office of the Banking Ombudsman places a limit of £1 million turnover on small companies, but puts no limit on partnerships or unincorporated bodies, whilst the Office of the Building Societies Ombudsman places a £1 million turnover limit on *all* small businesses.
- 3.12 In defining a 'small business' for the purpose of access to the new Scheme, the aim, as noted above, is to limit access to the Scheme to those small firms which are in a similar position to private individuals. However, a turnover limit of less than £1 million would not significantly affect the number of UK businesses which would be eligible to complain. DTI figures show little difference between the number of firms with a turnover of £500,000 compared with £1 million. We therefore propose to impose a £1 million turnover limit on firms which can use the Scheme, and to combine this with an additional 'employees' test (see below).
- 3.13 In view of the policy objective described in paragraph 3.9, the FSA considers that an '*under 5 employees*' test would be appropriate. Figures obtained from the DTI<sup>3</sup> indicate that a significant number of firms would meet such a test. Out of 3.7 million active businesses in the UK in 1998, 3.2 million had fewer than 5 employees, of which 2.3 million were made up of sole traders or partners without employees. However, firms would have to meet *both* tests (ie turnover and employees limits) in order to be eligible to use the Scheme. Figures for the number of firms which would meet both tests are not available, but we believe that the combination of a turnover test and an 'employees' test would make possible a more sensitive definition of a 'small business' than could be achieved by simply cutting down the turnover limit alone.
- 3.14 The Bill makes clear that authorised persons will not be eligible to use the Scheme, except as specified by the FSA in its CJ Rules. The FSA proposes to give authorised firms access to the Scheme only where they meet the eligibility test proposed above and where their complaint relates to an activity which they are not themselves authorised to conduct. This will enable small authorised firms to use the Scheme where they are in a similar position to a private individual, but will prevent authorised firms from using the Scheme to complain about other authorised firms conducting similar business. Complaints from market counterparties will also be excluded.

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3 *Small and Medium Enterprise (SME) Statistics for the UK, 1998*, published by the DTI on 5 August 1999.

3.15 The main change from the current schemes' arrangements arising from this proposal would be that small business customers of insurers would be eligible to bring a complaint to the Scheme for the first time. We recognise that this will be a new departure for the insurance sector, but believe that the case for adopting a common definition for all industry sectors is compelling.

3.16 **It is therefore proposed to make the Scheme available to small businesses which have a turnover of less than £1 million and fewer than 5 employees. This would include small companies, unincorporated bodies and partnerships and, in the interests of consistency, would apply across all sectors of industry. However, we recognise that some flexibility may be needed where charities and non-profit-making bodies are concerned and we are giving thought to how this can best be achieved.**

Q3.1 Do respondents agree with the proposal:

- (i) to give access to the Scheme to private individuals and small businesses with a turnover of £1 million or less and under 5 employees (except where the latter are market counterparties or authorised to conduct the type of business about which they are complaining); and
- (ii) to apply this definition across all industry sectors, including insurance?

#### Complainants who are not contracting parties

3.17 Another issue for consideration is the extent to which third parties should be eligible to complain to the Scheme. Current schemes vary in their coverage of third parties, reflecting the different nature of their business. Generally speaking, third party complaints are currently covered where the firm owes a duty of care and it is proposed to continue to include these third parties in the definition of eligible complainant, *provided that they satisfy the primary criteria for eligibility described above.*

3.18 This would mean that the Scheme would accept complaints from the following third parties:

- insured persons (even where they were not the policyholder) where the policy was taken out for their benefit (eg named drivers on a car insurance policy and those covered under, for example, group travel policies);
- persons giving a guarantee or security for a loan or mortgage;
- traders who rely on a cheque guarantee card;
- beneficiaries where the firm is executor/trustee of an estate/trust, provided that the complaint is made jointly by all of the people concerned;

- the true owner of a cheque, or the funds it represents, collected for someone else's account;
- recipients of bank references;
- holders of units or similar interests in unit trusts and other collective investment schemes;
- personal representatives of complainants with the complainant's authority; and
- holders of shares in investment trust companies.

All of the above, with the exception of the last bullet point, are currently covered by one or more of the existing schemes.

3.19 Complaints from other third parties involved in an insurance dispute (eg a motor accident where the other driver's insurer is disputing the claim) would *generally* be excluded. These complaints are not currently covered and to do so would confer wider rights on third parties than those which currently exist under insurance contract law. However, certain new legal rights will be conferred under the Contracts (Rights of Third Parties) Bill when that legislation is in force.<sup>4</sup> We therefore propose that third party disputes should continue to fall outside the Scheme's jurisdiction except where legal rights are conferred on them by the Third Party (Rights Against Insurers) Act 1930<sup>5</sup> or the new legislation.

Q3.2 Do respondents agree with the proposal to give access to the Scheme to insured persons only where they have legal rights to enforce a contract and to the other third parties outlined above?

## Which firms will be subject to the Scheme?

### Compulsory Jurisdiction

3.20 The CJ will cover FSA-authorized firms only. The FSA believes it is reasonable to require all authorised firms which are capable of giving rise to an eligible complaint to be subject to the Scheme and to contribute to its funding. This would apply irrespective of whether or not they actually give rise to a complaint, since they will all derive a general benefit from the existence of the new Ombudsman Scheme. In particular, the existence of the Scheme will enhance the general image of the industry and increase consumer confidence. It will also provide firms with a valuable backstop mechanism for dealing

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4 Under the new legislation, a third party will have the right to enforce a contract if all three of the following requirements are satisfied: (1) the contract expressly provides that the third party can enforce it or it purports to confer a benefit on the third party; (2) the third party is identified in the contract by name, class or description; and (3) the contract does not expressly exclude the right of third parties to enforce the contract.

5 This legislation currently gives enforceable rights to third parties only where the policyholder is insolvent.

with complaints which they are unable to resolve themselves (including, for example, those where the consumer is unwilling to accept a reasonable offer).

- 3.21 This would cover the vast majority of FSA-authorized firms including:
- firms currently conducting investment business under the Financial Services Act 1986 (including any appointed representatives for which they have responsibility);
  - deposit-taking firms (ie banks and building societies);
  - insurance companies; and
  - friendly societies.
- 3.22 However, some authorised firms (eg listed money market institutions) will not be permitted to conduct relevant business with customers eligible to use the Scheme and will therefore be incapable of giving rise to an eligible complaint. The FSA proposes to exempt such firms from the obligation to fund the Scheme and to comply with the FSA's complaints-handling rules, but only where the terms of their permission prevent them from doing business which could give rise to an eligible complaint.
- 3.23 The FSA does not expect this exemption to have wide application. It will not, for example, apply to firms which have permission to deal with customers eligible to use the Scheme, but do not actually do so. Nor will it extend to smaller authorised firms solely on the grounds that the sums at issue and/or the expected number of complaints are likely to be very small. The FSA proposes instead to introduce appropriately structured funding proposals where charges might otherwise be disproportionate (see Chapter 5).
- 3.24 The FSA has concluded that it is not possible to identify specific categories of firms which should benefit from this exemption on a blanket basis. It will, however, be willing to consider, on a case by case basis, applications for exemption from individual firms which are not permitted to conduct business with any customers who would be eligible to use the Scheme. Such firms are likely to include trade credit insurers, reinsurance companies and some listed money market institutions.
- 3.25 The arrangements proposed above would not, however, prevent the Scheme from dealing with a complaint about such a firm if it breached the terms of its permission and gave rise to an eligible complaint. The firm would be charged accordingly and the FSA would also have an interest from a regulatory perspective.

## Professional firms

- 3.26 Firms of solicitors, accountants or actuaries which will require authorisation by the FSA<sup>6</sup> when the new legislation comes into force will, like all other authorised firms, be subject to the CJ of the Scheme. However, complaints about such firms which relate only to their professional services activities will continue to be handled by the relevant professional body.
- 3.27 Complaints which would fall into the Scheme's CJ might relate solely to a firm's financial services activities, or they might relate to both its financial services activities and to its professional activities. The FSA is concerned to provide consumers with a single point of entry and therefore proposes that, in either case, the complainant should be directed to the FSOS in the first instance. Where appropriate, the Scheme Operator will pass the complaint to the relevant professional body. Working arrangements will therefore need to be agreed between the FSOS and each of the professional bodies for handling complaints against these firms.

## EEA firms

- 3.28 Under Schedule 3 to the Bill, an EEA firm automatically qualifies for authorisation if it seeks to conduct business in the UK by virtue of having obtained a passport under one of the relevant EC directives.<sup>7</sup> Such firms will derive their authorisation to conduct business from the authorities in their home state. However, we propose that where such firms qualify for authorisation and their activities fall within the CJ, they should also be required to participate in the Ombudsman Scheme.
- 3.29 These EEA firms will, like FSA authorised firms, be required to comply with the FSA's rules for handling complaints (see Chapter 6). Where appropriate, they will also be required to comply with the FSA's conduct of business rules and the Ombudsman will be able to take these into account when reaching decisions on complaints. For those EEA firms whose business will not be subject to conduct of business regulation, such as banks and general insurance companies, the FSA proposes that the Ombudsman should be able to take into account relevant UK industry codes of conduct when considering complaints (as he will be able to do with UK firms).

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6 The Government recently announced that, subject to certain conditions, professional firms which do not carry on mainstream investment business will not need to be authorised or regulated by the FSA. These firms will therefore fall outside the Ombudsman Scheme. However, the Government has said that it also intends the FSA to have a duty to keep generally under review the way regulated activities are carried out by these firms, the primary purpose of which will be to consider whether, in order to protect consumers, the FSA should exercise proposed powers to cut back the classes of excluded firms or activities. The FSA will finalise its approach to the exercise of this new duty once the full terms are clear. However, on current expectations, the FSA will be likely to want to consider, amongst other things, the nature and scale of complaints about the relevant activities of these firms and review the adequacy of the professional bodies' arrangements for handling such complaints.

7 *Second Banking Co-ordination Directive; Third Life Directive; Investment Services Directive; Third Insurance Directive.*

- 3.30 We do not propose, at this stage, to require inwardly passporting EEA firms which are transacting business into the UK on a *services* basis only (ie firms which have not established a permanent place of business in the UK) to participate in the Ombudsman Scheme. These proposals are in line with the current position in the existing schemes.

#### Lloyd's

- 3.31 In November 1998, the FSA consulted on the future regulation of Lloyd's, including the complaints arrangements which should apply. A Response Paper summarising the results of that consultation was published by the FSA in June. We intend that the Society of Lloyd's (which is currently a member of the IOB) will be subject to the new Scheme, in respect of complaints from personal policyholders and to the FSA's complaints-handling rules. As now, complaints from Lloyd's personal policyholders will continue to be handled, in the first instance, by the Lloyd's Complaints Department. Lloyd's personal policyholders will then have access to the new Ombudsman Scheme if the Lloyd's Complaints Department is unable to resolve their complaint. This will essentially replicate the current position.
- 3.32 Lloyd's Members will not have access to the Scheme. The FSA intends instead to include in the Handbook a requirement for Lloyd's to maintain adequate dispute resolution arrangements for dealing with complaints from Lloyd's Members.

### Which activities should be covered by the Scheme?

- 3.33 The Bill gives the FSA and the FSOS considerable flexibility in determining the *activities* to be covered by the Scheme. This section addresses the question of which activities should be covered by each jurisdiction.

#### Compulsory Jurisdiction

- 3.34 The Bill gives the FSA discretion to specify in the CJ Rules any of the financial services activities of an authorised firm which are either *regulated or potentially regulated* under the Bill, subject to appropriate cost benefit analysis and consultation.
- 3.35 The Scheme will be able to deal with a dispute if it relates to an act or omission of an authorised firm *in carrying on* an activity to which the CJ Rules apply. In other words, disputes will fall within the CJ if they relate to or arise from a service which forms part of an activity which has been specified in the CJ rules. For example, if deposit-taking were specified as a relevant activity, the Scheme staff would be able to look at any disputes arising from the operation of a bank account (eg withdrawal of money from a cash

machine or the operation of a cheque account even if the account were overdrawn at the time).

#### Options

- 3.36 There are three main options for determining the scope of the CJ of the Scheme. It could cover:
- (1) regulated activities only; or
  - (2) regulated activities plus those potentially regulated activities which are currently covered by the existing schemes; or
  - (3) all financial services activities conducted by FSA authorised firms, whether regulated or potentially regulated.
- 3.37 Option (1) would mirror the scope of the Regulated Activities Order. However, it would remove from the scope of the CJ complaints about some activities which are currently covered by the existing arrangements but which will not constitute regulated activities (for example, the lending activities of banks). This could mean that consumers who are currently able to bring a complaint about a particular activity to one of the existing schemes, would no longer be able to do so under the new arrangements. The FSA does not believe that this is acceptable. Most CP4 respondents felt that the Scheme's compulsory remit should go beyond regulated activities and the draft Bill was amended before its introduction into Parliament specifically to enable the CJ to cover, as far as possible, all of the activities which currently fall within the scope of the existing schemes.
- 3.38 Option (2) is therefore effectively the 'baseline option'. It would mean that any activity currently covered by any of the existing schemes would be covered by the new Scheme on a *compulsory* basis for all authorised firms, irrespective of whether or not that activity required authorisation by the FSA. (A list of the types of dispute which the new Scheme would cover if Option (2) were adopted is set out at Annex B, together with an indication of which of the existing schemes currently covers them.) Other financial services activities would fall outside the scope of the CJ, but could be covered by the VJ, provided that the FSOS decided to do so and the firms concerned agreed to participate (see paragraphs 3.49 to 3.59 below).
- 3.39 Option (3) is more comprehensive and therefore has clear advantages from a consumer perspective. It would mean that a consumer could complain to the Scheme about any of the regulated or potentially regulated financial services activities of an authorised firm. It would also be simpler for consumers to understand. The FSA therefore sees this as a desirable longer term objective.
- 3.40 However, moving straight to Option (3) could create difficulties for the FSOS in its early days of operating the new Scheme. In particular, it would bring

into the CJ at N2 complaints about certain types of unregulated business which are not currently covered by the existing arrangements (eg general insurance broking<sup>8</sup>/advice and independent mortgage broking/advice). However, it would do so *only where these types of business happened to be conducted by an authorised firm*.

- 3.41 For example, an independent financial adviser who was authorised to conduct investment business, but also arranged general insurance, would be required to participate in the CJ for all of these activities, whereas an adviser whose business concerned only general insurance could remain outside the CJ altogether.
- 3.42 This could create an unlevel playing field between authorised and unauthorised firms in respect of activities which are not currently covered by any of the existing schemes and it might lead to some firms setting up subsidiaries to carve business out of the Scheme's CJ. It could also result in a significant and unpredictable increase in the volume of complaints which would fall to be handled under the Scheme at N2.
- 3.43 **Against this background, the FSA proposes to adopt the approach outlined in Option (2) (the 'baseline option'), but sees Option (3) as the longer term objective.**
- 3.44 Option (2) would ensure that no consumer who is currently able to complain would lose the ability to do so. Equally important, however, it would give the FSOS greater certainty about the volume of complaints which it would have to handle at N2 and more flexibility to manage the merger process and start up its service in a phased way. It would leave the way open for other trade or regulatory organisations to encourage (or require) their members to join the VJ of the Scheme, for example where those sectors of the industry are not currently subject to such a scheme, on a level playing field basis. It would also leave open the option to extend the scope of the CJ at some future point, if appropriate, in the light of experience.

Cost benefit analysis

- 3.45 Option (1) would have the least impact in terms of costs. It might even be less expensive than existing arrangements since some activities which are currently covered would no longer be covered, although costs to both consumers and firms might increase as a result of increased court action. However, the FSA considers that the reduction in consumer protection which this option would entail, in terms of disenfranchising existing consumers, makes this option unacceptable.

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<sup>8</sup> Although the Insurance Ombudsman Bureau opened its membership to insurance brokers last year, very few insurance brokers have joined. In these circumstances, it is difficult to justify (on cost-benefit grounds) bringing general insurance broking into the scope of the Compulsory Jurisdiction for authorised firms and it is more appropriate for this to be covered under the Scheme's Voluntary Jurisdiction. This would also be consistent with Government policy that general insurance intermediation should be subject to self-regulation.

- 3.46 Option (2) should not result in material increases in costs since it replicates the combined scopes of the existing schemes and virtually all of the firms which would be affected are already members of those schemes. In the longer term, there may even be a reduction in costs for some firms, (eg group companies), since all relevant activities will be covered by a single scheme, whereas, currently, their activities may require membership of two or more schemes. It should not, therefore, have a significant impact on either the quantity or variety of products available to consumers.
- 3.47 The main benefit of Option (2) is that the Scheme would be more comprehensive, with easy access making the process of complaining simpler for consumers. The Scheme will also be able to deal more effectively with complaints involving more than one activity (which previously would have been subject to more than one scheme) and this will be of benefit both to consumers and to firms.
- 3.48 The costs and benefits of a possible move, at a later stage, from Option (2) to Option (3) would be subject to detailed analysis and consultation before any further extensions to the CJ were made.

Q3.3 Do respondents agree that the FSA should adopt the approach outlined in Option (2) in the first instance, but aim to move, in due course, to Option (3)?

### Voluntary Jurisdiction

- 3.49 The Bill gives the FSOS the same discretion to determine the activities covered by the VJ as it gives the FSA in relation to the CJ, although, unlike the CJ, the VJ will be open to *unauthorised* firms as well as *authorised* firms.
- 3.50 The VJ could therefore cover:
- any of the potentially regulated financial services activities of *authorised* firms which are not brought into the CJ; and
  - any of the potentially regulated financial services activities of *unauthorised* firms, if specified by the FSOS for this purpose.
- 3.51 The potential scope of the VJ in terms of the breadth of activities and the number of firms which it could cover is therefore extremely wide. As noted above, there is a tension between the desire to offer consumers as comprehensive a service as possible and the need to guard against the danger that the Scheme Operator could be overwhelmed by an unpredictable and unmanageable volume of complaints which might prejudice the quality of service which it could provide. A key consideration for the FSOS is the potential size of the VJ and the need to ensure that its VJ services are made available in a controlled way which is consistent with its ability to handle the complaints generated.

#### Authorised firms

- 3.52 Whilst decisions on the scope of the VJ are a matter for the FSOS, the FSA's decision on the scope of the CJ will inevitably have an impact on the extent to which the VJ is made available to authorised firms. If Option 2 were adopted in relation to the CJ, it would be desirable, from a consumer perspective, for the VJ to be made available to *authorised firms* in respect of any of their financial services which were not subject to the CJ. If, however, Option 3 above were to be adopted, all of an authorised firm's financial services activities would be subject to the CJ.
- 3.53 The FSOS proposes to make the VJ available to authorised firms in respect of any potentially regulated activities which are not brought into the CJ. However, it will want to obtain more information about the volume and nature of these activities before it does so and therefore proposes to bring these activities into the VJ over a phased period and in the light of experience of the operation of the CJ.

#### Unauthorised firms

- 3.54 Decisions on the extent to which the VJ should be made available to unauthorised firms are particularly difficult because of the absence of hard information on both the number of firms which are conducting particular activities and the number of complaints which they are likely to generate. This is particularly the case where unauthorised firms are conducting financial services activities which are not currently subject to any kind of complaints arrangements (eg general insurance intermediaries ). It is essential that the FSOS should not overstretch itself, particularly in the early stages. It is also essential that unauthorised firms should have appropriate complaints-handling arrangements (similar to those proposed in Chapter 6 for authorised firms) before they are allowed to participate in the VJ.
- 3.55 As a first step, therefore, the FSOS aims to bring unauthorised firms into the VJ in respect of unregulated financial services activities which are covered by the CJ and conducted, for the most part, by authorised firms (eg mortgage lending). This would mean, for example, that direct mortgage lenders which are not conducting any authorisable activities and which therefore will not be subject to the Scheme's CJ would be able to join the Scheme. This will be of obvious benefit to consumers and will enable authorised and unauthorised firms to compete on a level playing field in respect of these activities.
- 3.56 The General Insurance Standards Council (GISC) (the new self-regulatory body covering general insurance) has indicated that it would like to make it compulsory for members of GISC to join the Scheme's VJ (insofar as they will not be within the CJ) and similar arrangements could be made with other trade bodies if they considered it appropriate.

- 3.57 However, a phased approach is necessary in order to enable the FSOS to manage the process effectively. Although the selling of general insurance (as distinct from the underwriting or broking) and the provision of unsecured loans (consumer credit) by banks and building societies will be covered by the CJ, the FSOS could not open its door at N2 to *all* independent general insurance brokers or consumer credit firms for the reasons mentioned above. In these sectors a more cautious approach is called for. The same applies to mortgage broking, unless HM Treasury were to decide that advice on mortgages should be regulated, in which case this activity would come into the CJ.
- 3.58 The FSOS therefore proposes to bring these activities into the VJ over a period of time, as and when the relevant sectors of the industry are able to give it a realistic idea of the volume of firms and complaints which this is likely to involve. In particular, it is keen to ensure that it is fully informed of the implications which the inclusion of these activities would have for its workload. It will also want to be satisfied that the firms concerned have in place effective complaints-handling policies and procedures for the activities concerned. The FSOS is seeking further information from the relevant organisations.
- 3.59 **In summary, the FSOS proposes, once it is satisfied that the firms concerned have in place effective complaints-handling policies and procedures, to make the VJ available to:**
- **authorised firms in respect of any of their potentially regulated activities which are not brought into the CJ; and**
  - **unauthorised firms in respect of advice on mortgage lending, since the majority of this sector will be covered by the CJ.**

**Other potentially regulated activities will be brought into the VJ as and when the FSOS considers this to be appropriate. This approach will, in time, create a level playing field between authorised and unauthorised firms in terms of the Scheme's coverage.**

Q3.4 Do respondents agree with the phased approach which the FSOS proposes to adopt in relation to the VJ?

### **What should the territorial coverage of the Scheme be?**

- 3.60 The FSA proposes that the territorial coverage of the CJ of the Scheme should mirror the FSA's authorisation requirement, as currently framed in the Bill, and the FSOS proposes, in the first instance at least, to define the territorial jurisdiction of the VJ in the same way.

- 3.61 On this basis, the Scheme would cover complaints about:
- UK firms conducting business domestically with UK consumers;
  - UK-based firms conducting business from the UK with consumers resident in other countries;
  - European firms passporting into the UK under one of the EC Directives which have a permanent place of business in the UK.
- 3.62 We do not propose to apply a residence qualification to consumers, provided they fall within the definition of eligible complainant as outlined above. This would be in line with the coverage of most of the existing schemes.
- Q3.5 Do respondents agree with the proposed territorial coverage of the Scheme?

### **What should the limits on awards be?**

- 3.63 Ombudsman awards will be based on what is ‘fair and reasonable in all the circumstances’, rather than on strict legal liability. The Bill gives the FSA the power, in relation to the CJ, to specify maximum limits on the amounts which the Ombudsman can order firms to pay for particular kinds of loss or damage. The FSOS has similar powers in relation to the VJ as part of the standard terms which it will set for VJ participants. This enables us to ensure that the Scheme is not available for use by those with disputes involving very large sums of money which should more properly be decided in the courts. Both the FSA and the FSOS believe that this is an area where it is desirable for the two jurisdictions to mirror each other and the proposals contained in the next two paragraphs therefore relate to both jurisdictions.
- 3.64 In CP4, the FSA consulted on the basis that the maximum limit should be £100,000, which is the limit in most of the existing schemes. This received widespread support from respondents and we propose to retain this limit for money awards for all industry sectors, although it will be subject to review by the FSA, in consultation with the FSOS, in the light of experience, every three years. The Bill allows the Ombudsman to recommend payments in excess of this limit, although the firm will not be bound to pay the balance.
- 3.65 We do not propose, at this stage, to place any separate limits on awards within that overall total (such as those for distress and inconvenience). The Chief Ombudsman has indicated that he will put arrangements in place within the Scheme to ensure that such awards are made on a consistent basis. However, the need for any separate limit will be kept under review by the FSA in the light of experience.
- Q3.6 Views are invited on the limits on awards outlined above.

## When is a complaint an 'eligible complaint'?

- 3.66 The Bill sets certain conditions on the circumstances in which complaints can be dealt with under the CJ and VJ as follows:
- the complaint must relate to an act or omission in carrying on an activity which was subject either to CJ or VJ rules at the relevant time;
  - the firm concerned must have been authorised or participating in the VJ at the time of the relevant act or omission and, in the case of the VJ, must still be participating when the complaint is referred to the Scheme (but the FSOS intends to impose a notice period on firms wishing to withdraw from the VJ to enable outstanding complaints to be handled); and
  - the complainant must meet the relevant criteria for access to the Scheme.
- 3.67 We anticipate, however, that the Bill will, in due course, provide for transitional arrangements where appropriate in relation to work in progress in the existing schemes at N2 to provide continuity of coverage.
- 3.68 The Bill also allows the FSA and the FSOS to set certain conditions on the circumstances in which a complaint will be eligible to be handled under the Scheme. The FSA will have the power to make 'procedural rules' stipulating that a complaint will not be eligible to be referred to the Scheme under the CJ unless the firm has had a reasonable opportunity to consider the complaint and the complaint is referred to the Scheme within time-scales prescribed by the FSA, although the Ombudsman may extend these in certain circumstances. (The FSA's proposals are set out in Chapter 6.)
- 3.69 The FSOS will have the power to make Scheme Rules relating to the CJ, which amongst other things, could allow the Ombudsman, in specified circumstances, to dismiss a complaint without consideration of its merits. (The circumstances in which the FSOS proposes to do this are set out in Chapter 4.)

# 4 Scheme rules, standard terms and costs rules

- 4.1 This chapter deals with the following rules and standard terms to be established by the FSOS under powers contained in the Bill:
- *Scheme rules* – for the CJ, the FSOS *must* make scheme rules governing the procedures for considering and determining complaints.
  - *Standard terms* – in the VJ, complaints are to be dealt with in accordance with standard terms fixed by the FSOS.
  - *Costs rules* – for both jurisdictions, the FSOS *may* make costs rules setting out the circumstances in which an ombudsman may award costs.
- 4.2 The responsibility to establish the scheme rules, standard terms and (if appropriate) costs rules rests with the Board of the FSOS, but the written approval of the FSA is also required. To put the proposals in context, the way in which the FSOS proposes to handle complaints in the CJ is outlined below.

## Outline of procedures

- 4.3 It is proposed to follow the successful pattern established by existing ombudsman schemes. First, the Scheme staff will check that the firm has been given a reasonable opportunity to consider the complaint and that the matter remains unresolved. Next it will check that the complaint is within the Scheme's jurisdiction – eg that the complainant is eligible and that the firm and activity involved are covered. Any questions about whether or not a complaint falls within the Scheme's jurisdiction will be settled by an Ombudsman's determination and, as such, will be subject to the requirements of the European Convention on Human Rights (ECHR) described below.
- 4.4 After that, the Scheme staff will consider the information supplied by complainant and firm. In doing so, they will explore any reasonable prospect of resolving the complaint by a conciliated settlement acceptable to both complainant and firm. Based on the experience of existing schemes, it is

expected that a substantial proportion of complaints can be resolved speedily by conciliation, once the Scheme Operator becomes involved as honest broker.

- 4.5 Otherwise, the Scheme staff will investigate the circumstances. They will call for any information which is needed from either party in order to do so. To assist the Scheme Operator in considering complaints, the Bill gives it power to require information from complainant and firm – enforceable in court if necessary. Then the Scheme staff will issue an initial decision, setting out a recommended outcome and the reasons for it. If both complainant and firm accept the initial decision, the complaint is resolved.
- 4.6 If either party does not accept the initial decision, the case will be reviewed by one of the Ombudsmen, who will issue a final decision (which the Bill refers to as a ‘determination’). The procedures relating to an ombudsman’s final decision will take into account the ‘fair trial’ requirements in Article 6 of the European Convention on Human Rights (ECHR), applied in the UK by the Human Rights Act 1998, which will be drawn to the parties’ attention.
- 4.7 The FSOS aims to incorporate ECHR safeguards into its procedures in a way which does not undermine the essential informality and speed of the ombudsman process. In some circumstances, either party is entitled to request a public oral hearing before the final decision is made. In such cases, the hearing will be conducted informally, in the way the Ombudsman concerned considers best suited to the circumstances. The hearing does not have to be confrontational. What is necessary is that each party can hear and comment on the other’s evidence.
- 4.8 In accordance with ECHR requirements, a party may choose to be legally represented at an oral hearing. However, the FSOS does not believe that this will be necessary. The Ombudsman will conduct any hearing in such a way that a party who is represented will not have any advantage over a party who is not represented. The Ombudsman may ask questions of either party, set appropriate time limits, where necessary, and ensure that the hearing is confined to matters which are material.
- 4.9 The Bill requires complaints to be determined by reference to what the Ombudsman considers to be fair and reasonable in the circumstances of the case. The final decision must give the Ombudsman’s reasons. It must also state a time limit within which the complainant must indicate acceptance or rejection. In accordance with ECHR requirements, the decision will be published (though the published version will not have to reveal the identity of the parties).
- 4.10 If the final decision is accepted by the complainant within the time limit, the Bill requires that it will be final and will bind both complainant and firm. It can be enforced by the complainant in court if necessary. If the final decision is not accepted by the complainant within the time limit, it will not bind either

party and the complainant will be free to pursue the matter by court proceedings against the firm. But there will be no further appeal stage within the Scheme.

## FSOS Scheme Rules

### Fair and reasonable

- 4.11 The Bill allows the FSOS's Scheme Rules to specify matters which an Ombudsman may take into account in deciding what is fair and reasonable. It is proposed that relevant law and regulations (including FSA rules and regulatory guidance) and relevant codes of practice should be taken into account. It is also proposed that, where appropriate, what the Ombudsman considers to be good industry practice should also be taken into consideration.

### Early termination

- 4.12 The Scheme will be free to complainants. Accordingly, it is important to ensure that it is not overwhelmed by cases which should not be handled under the Scheme. The Bill allows the FSOS to specify in its Scheme Rules the circumstances in which a complaint which is being handled under the CJ could be dismissed without consideration of its merits. Similar conditions can be imposed by the FSOS in the VJ via its Standard Terms. The circumstances which the FSOS proposes to specify – for both jurisdictions – are described in the following paragraphs.
- 4.13 A small minority of complainants may attempt to pursue complaints which are clearly without any merit. A few may attempt to resubmit a complaint which has already been considered – either under the Scheme or by an equivalent body. So it is proposed to give a power of early termination where:
- the complaint is frivolous or vexatious, or clearly does not have any reasonable prospect of success;
  - the complainant has not incurred financial loss, distress or material inconvenience;
  - the matter has previously been considered under the Scheme (unless material new evidence has become available subsequently); or
  - the matter has already been dealt with, or is being dealt with, by a comparable independent complaints scheme or dispute resolution process.
- 4.14 The FSOS cannot overrule a court decision; that is a matter for the court appeal process. It would not be appropriate for a complaint which is also being considered by the court to be considered under the Scheme, unless the

court proceedings are stayed (by agreement of all parties or by order of the court) so that it could be handled under the Scheme. There will be a few cases which can only be dealt with appropriately in court or some other forum – for example, because they involve the rights of a third party in addition to the complainant and firm. So it is also proposed to give a power of early termination where:

- the matter has been the subject of court proceedings where there has been a decision on the merits;
- the matter is the subject of current court proceedings, unless the proceedings are stayed (by agreement of all parties or order of the court) in order that the matter may be considered under the Scheme; or
- it would be more suitable for the matter to be dealt with by a court, arbitration or another complaints scheme.

4.15 Additionally, the Bill envisages that the Scheme Rules might provide for a complaint to be dismissed without consideration of its merits if there are other compelling reasons why it is inappropriate for the complaint to be dealt with under the Scheme. We believe that there are a number of matters about which it would not be appropriate for complaints to be dealt with under the Scheme and which are indeed excluded from the terms of reference of the existing schemes.

4.16 It is, therefore, proposed that the following kinds of complaints should be excluded from the scope of the Scheme:

- complaints about the legitimate exercise of a firm's commercial judgement, for example, the refusal of credit or to accept an underwriting risk;
- complaints about investment performance;
- complaints from employees of firms relating to employment matters;
- complaints relating to health and safety matters;
- complaints relating to a firm's decision in exercising a discretion under a will or private trust, unless there has been maladministration or unfair treatment;
- complaints relating to a firm's failure to consult beneficiaries before exercising a discretion under a will or private trust where there is no legal obligation to do so, unless there has been maladministration or unfair treatment;
- complaints relating to investment business as defined in the Financial Services Act 1986, arising before that Act came into force on 29 April 1988. (Such matters could be dealt with under the Voluntary Jurisdiction.)

## Evidence

- 4.17 As mentioned above, the Bill gives the FSOS power to require information from the parties. It also gives power for the Scheme Rules to make provision about the evidence which may be required or admitted, the extent to which evidence should be written or oral, and the consequences if a party does not provide required information.
- 4.18 On the question of what evidence may be required or admitted, it is proposed to follow the pattern of Rules 32(1) and 32(2) of the Civil Procedure Rules 1998 – instituted as part of the recent civil justice reforms led by Lord Woolf. In addition, following normal ombudsman practice, it is proposed to give discretion to waive the technicalities of the law of evidence. Accordingly, the proposal is that:
- The Ombudsman may control the evidence by giving directions as to: the issues on which the Ombudsman requires evidence; the nature of the evidence the Ombudsman requires to decide those issues; and the way in which the evidence is provided.
  - The Ombudsman may use this power to: exclude evidence that would otherwise be admissible; and include evidence that would not be admissible in court.
- 4.19 The Ombudsman may need to examine, for example, records of the firm which include confidential information about other customers or details of a firm's security procedures. Ordinarily, fairness requires that all evidence be submitted to an Ombudsman on the basis that it may be shown to the other party unedited. Exceptionally, an Ombudsman may consider that it is necessary and appropriate to receive certain evidence in confidence – so that only its general nature or an edited version is disclosed to the other party.
- 4.20 The decision about whether to accept any evidence in confidence must rest with the Ombudsman, and not the party supplying the information. The power should be used sparingly. Circumstances where an Ombudsman might consider it necessary and appropriate to accept information in confidence include:
- where disclosure of the information would facilitate crime, or inhibit its detection;
  - where the information contains confidential details about third parties; or
  - where the information is commercially confidential and sensitive.
- 4.21 Where a complainant or firm fails to provide required information, it is proposed that the Ombudsman may reach a decision on the basis of what has been supplied (drawing any appropriate inference from the failure to supply all the required information). Alternatively, where it is the complainant who fails

to supply required information, consideration of the complaint may be terminated.

### Time limits

- 4.22 The Bill provides that Scheme Rules may allow an Ombudsman to fix, or extend, a time limit for any aspect of the proceedings. It is not proposed to impose universal, arbitrary time limits. Instead it is proposed simply to provide that an Ombudsman may fix time limits for any aspect of a case, and extend any time limit.
- 4.23 Where a complainant or firm fails to comply with a time limit, it is proposed that the Ombudsman may proceed to the next stage of the case. If it is the firm which fails to comply, its conduct may be taken into account in assessing any award for inconvenience. Alternatively, where it is the complainant who fails to comply with the time limit, consideration of the complaint may be terminated.

### Case-handling procedures

- 4.24 The Bill provides that a final decision, determining a complaint, can only be issued by an Ombudsman. But Scheme Rules may provide for other parts of the process to be handled by members of staff. It is proposed to make a rule enabling the Chief Ombudsman to arrange for any part of the process, apart from determination of a complaint, to be handled by any member of staff he considers to have appropriate qualification or experience.

Q4.1 Respondents' views are sought on the proposed Scheme Rules.

### FSOS standard terms

- 4.25 As explained in Chapter 3, the Scheme will have a CJ and a VJ. The extent of the CJ is to be established by FSA rules. The extent of the VJ is to be established by FSOS rules, approved by the FSA. Complaints in the VJ are to be dealt with in accordance with standard terms.
- 4.26 It is proposed that, so far as practicable, those standard terms should reflect the equivalent provisions applicable to the CJ. The intention is that a complainant should see no material difference in the way that a complaint is dealt with under the Scheme – whether it is in the CJ, the VJ or partly in one and partly in the other.
- 4.27 It will be necessary for the standard terms to impose on firms by contract certain provisions which, in the CJ, are imposed by FSA rules or by the Bill. In particular:

- The standard terms should require firms to have internal complaints procedures which, from a complainant's point of view, are equivalent to those required by the FSA complaints rules proposed in chapter 6. But the standard terms will not involve the provision of statistics to, or monitoring by, the FSA.
- The standard terms should also provide that an Ombudsman's final decision, if accepted by the complainant within the time limit specified by the Ombudsman, will bind the firm and may be enforced in court by the complainant in the same way as currently applies to an arbitration award.
- The standard terms will provide for VJ participants to pay appropriate fees (see Chapter 5).

Q4.2 Respondents' views are sought on the proposed standard terms.

## FSOS costs rules

- 4.28 The Bill allows the FSOS to make costs rules, giving the Ombudsman the power to award costs in certain circumstances. Costs rules may require a complainant to make a contribution to the Scheme's costs only where he or she acts improperly or unreasonably or causes an unreasonable delay. They may not require a complainant to pay a firm's costs.
- 4.29 The FSOS does not propose to make costs rules at this stage, but will keep this matter under review in the light of experience. If such rules were to be made, the complainant would be given a 'costs warning' before any award of costs was made against him.

Q4.3 Do respondents agree with the proposal not to make costs rules at this stage?

## Complaints against the FSOS

- 4.30 The FSOS will also need to have in place arrangements for dealing with complaints against itself. Like the FSA, the FSOS proposes, to appoint an independent Complaints Commissioner to investigate such complaints. These arrangements would be confined to complaints about the operation of Scheme procedures (eg allegations of delay in handling a case). They would not provide a means for the merits of a complaint to be re-examined, since this would undermine the role of the Ombudsman. The Commissioner would report to the Board of the FSOS and make recommendations where appropriate as to how the Scheme's procedures might be improved.

Q4.4 Do respondents agree with the proposal to set up an independent Complaints Commissioner to investigate complaints about the Scheme?

# 5 Funding the Scheme

- 5.1 The costs of the new FSOS, like those of the FSA, will be borne by the industry. As in most of the current schemes which the new Scheme will replace, the service will be generally free of charge to the complainant.
- 5.2 The estimated budget for the Scheme's first year of operation (based on the aggregate costs of the existing schemes) is approximately £20 million.
- 5.3 The powers to make rules relating to the funding of the new Scheme are set out in the Financial Services and Markets Bill and are divided between the FSA and the FSOS. The Bill distinguishes between the powers relating to funding the ongoing '*operating costs*' of running the Scheme and the power to recover the '*establishment costs*' (ie the cost of setting up the new Scheme). These are dealt with separately below.

## Operating costs

### Compulsory Jurisdiction

- 5.4 The Bill provides both the FSA and the FSOS with fund-raising powers in respect of the operating costs of the Scheme's CJ. It enables the FSA to make rules requiring authorised persons (or classes of authorised persons) to pay to it – or to the Scheme Operator – specified fees. It also enables the FSOS, if it wishes, to charge case fees to authorised firms against which complaints are actually received. The FSOS could, if it wished, set different case fees for different stages of the proceedings or provide for fees to be waived, reduced or refunded in specified circumstances.

### Voluntary Jurisdiction

- 5.5 Responsibility for funding the VJ (which will include unauthorised firms) will fall entirely to the FSOS. The VJ will be funded in accordance with the

'standard terms' which will apply (by contract) to firms which choose to join it. These terms will be fixed by the FSOS with the written approval of the FSA and different standard terms may be fixed with respect to different matters or in relation to different cases. The intention is to avoid, as far as possible, cross subsidy between the two jurisdictions, although the cost of overheads and common functions will be allocated between the two jurisdictions on a fair basis. Fees will be collected from unauthorised firms in the VJ by the FSOS, not by the FSA, and the Scheme's budget will be required to distinguish between the CJ and the VJ.

- 5.6 The FSA and the FSOS propose to adopt the same basic method of funding for the CJ and the VJ, and the proposals which follow relate to both jurisdictions.

#### Funding of existing schemes

- 5.7 The 'charging' mechanisms of the existing schemes vary. Some are funded directly from regulatory fees.<sup>1</sup> Others, particularly those which handle high volumes of complaints, such as the PIAOB and the IOB, fund themselves via a combination of a general annual levy on all members and case fees which are paid by those who actually use the schemes. The proportion of the budget raised by a general levy as opposed to case fees varies from scheme to scheme. (Details of the various funding mechanisms are given at Annex C.)
- 5.8 The basis on which the existing schemes calculate their members' annual levy also varies, but, with one exception,<sup>2</sup> they all take account of firms' size and/or volume of business in some way:
- relevant turnover (IOB and FSA);
  - number of personal accounts (OBO);
  - net asset value (OBSO);
  - funds under management (OIO);
  - number of registered individuals (SFA and PIAOB);
- 5.9 Case fees are currently collected in one of two ways. Some schemes (PIAOB and PIAS) charge firms a case fee on a 'pay as you go' basis. Others (IOB and OBO) raise a general levy 'on account' at the beginning of the year and a set proportion of that levy is subject to a case-related adjustment at the end of the year. Firms receive either a credit or an additional levy, based on the number of complaints against them handled by the scheme. On average, case fees

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1 The Office of the Investment Ombudsman, the SFA Complaints Bureau and the FSA Complaints Unit are funded by the regulatory fees of IMRO, SFA and the FSA respectively.

2 PIAS charges member firms a flat-rate retainer.

work out at around £500, but this can vary and there is no common definition across the schemes of what constitutes a 'case' for charging purposes. Some schemes also impose lower charges where cases do not proceed to full investigation and provide rebates where cases are considered to be frivolous or vexatious. None of the existing schemes' charging structures takes into account the outcome of the complaint.

- 5.10 A new single charging mechanism will have to be introduced at N2 when the existing schemes come together on single terms of reference and common procedures in a single building. Policy issues of relevance to the development of a new funding mechanism were subject to initial consultation last year (in CP4), but require further consideration in the light of the responses received and subsequent developments. These are explored in more detail below.

### **How should the operating costs of the new Scheme be funded?**

- 5.11 The pros and cons of the various possible funding methods were set out in some detail in CP4 on 'Consumer Complaints' and the funding of the Scheme provoked more comment than any other single issue. A wide range of suggestions was put forward as to how an equitable system of funding could be achieved. (Detailed feedback was provided in the FSA's August 1998 Policy Statement.)
- 5.12 There was a general consensus in favour of a method which incorporates both a general annual levy and a case fee / 'user pays' element. However, the issue of how the case fee element should be calculated gave rise to a diverse range of views. Many of these were driven by firms' concerns that current funding mechanisms penalise them unfairly, in particular, by charging for complaints even where these are found to be invalid or by creating the potential for 'consumer blackmail' where the case fee exceeds the sum in dispute.
- 5.13 There was general agreement that any case fee needed to be pitched at a level which would encourage firms to settle complaints themselves wherever possible, but would not act as a deterrent where firms had good reason to seek a second, independent opinion. However, no clear consensus emerged as to how this should be achieved. The responses essentially highlighted the tension between devising a method which is fair and one which is relatively simple and cost-efficient to operate.
- 5.14 For example, the view that case fees should take account of whether or not a complaint is valid was expressed strongly by many respondents. In practice, however, this is problematic. Approximately 75-80% of cases are currently resolved at the conciliation stage (ie through compromise and ex gratia payments etc.) and we expect this to continue. It is therefore only at the

determinative (ie final award) stage that 'blame' is attributed, and even then, the issue of 'validity' is not necessarily clear-cut. An Ombudsman might, for instance, simply award an increased level of redress for the complainant where the firm has already accepted responsibility or he might uphold a complaint only in part.

- 5.15 Similarly, the possibility of charging an additional fee for each stage of the process is attractive and it is an option for which the Bill explicitly provides. A 'tiered' approach of this kind would enable the fee to reflect the extra time spent on such cases and would also provide firms with an incentive to settle early. However, it could be time-consuming and complex to operate and would need to be applied in a way which did not deter firms from using the Scheme in appropriate cases.
- 5.16 The FSA and the FSOS agree that the funding mechanism should comprise a 'user pays' element as well as a general levy on all firms. A general levy will ensure that all firms capable of giving rise to an eligible complaint contribute towards the costs of the Scheme, reflecting the general 'consumer confidence' benefit which they will all derive from the existence of the Scheme, even if they do not actually have to use it. The 'user pays' element will provide firms with an incentive to resolve complaints themselves as far as possible and ensure that those firms which actually use the Scheme bear a greater proportion of the costs, in proportion to their usage.
- 5.17 However, the pros and cons of the various issues surrounding the basis on which case fees could be charged outlined above are finely balanced and cannot be decided in a vacuum. The pattern and volume of enquiries and complaints which will be received by the new Scheme will not necessarily reflect those experienced in the existing schemes, since the Scheme's scope will in some respects be broader, and its procedures may also be different in some respects from those of the existing schemes.
- 5.18 In view of the complexity and diversity of these issues, funding is the subject of continuing discussions and we have concluded that it is inappropriate, at this stage, to determine a fixed funding formula. **We therefore propose to put in place a funding mechanism which will be reviewed and refined in the light of the actual experience of the Scheme and further consultation with the industry.**

## Proposed funding arrangements for the CJ

- 5.19 In determining appropriate funding arrangements for the Scheme, the objective is to ensure that they:
- are fair as between firms;

- are efficient and administratively simple to operate and to collect;
- provide the FSOS with an appropriate degree of certainty and flexibility for budget planning purposes; and
- provide firms with an incentive to resolve complaints, where possible, at an early stage, but avoid deterring them from using the Scheme, where appropriate.

However, no method of funding can ever mirror the exact cost of dealing with a complaint and the proposals set out below aim to produce a result which is generally fair to all firms, but which will be practical to operate.

- 5.20 It is also necessary to bear in mind the fact that the date when the legislation comes into force is unlikely to coincide with the beginning of a financial year and, consequently, firms from the different constituencies will already be subject to their respective scheme's funding arrangements for that year. As noted above, these vary significantly from scheme to scheme. Transitional arrangements will therefore be required to deal with this situation and these are discussed at paragraphs 5.31 to 5.32 below.
- 5.21 The proposals which follow relate to the CJ and will be achieved through FSA Rules. However, the FSOS proposes to adopt as similar an approach as possible in relation to the VJ (see paragraph 5.33 below).
- 5.22 We propose a method of funding built on the following principles:
- **Allocation of costs.** For the first full year of the Scheme (ie 2001/2), the allocation of costs will be based on the *budgeted* costs of the Scheme. The operating costs will be calculated and apportioned as an integral part of the FSOS's management accounts and the method of allocation will be reviewed in consultation with the external auditors. However, the FSOS will want to consider, in the light of handling complaints in accordance with standardised procedures and with common overheads, whether there are different unit costs (in terms, for example, of the complexity or time taken) in dealing with different types of complaint, which justify differential charges for different sectors of the industry.
  - **Recovery of costs.** The operating costs will be recovered from firms by a combination of a general levy and a charge based on the number of cases handled under the Scheme. We propose to recover 50% of operating costs through the general levy and 50% through the case-related charge. (We believe that a 50:50 split represents a pragmatic approach in the first instance, particularly since those of the existing schemes' funding mechanisms which currently incorporate a case-related charge raise at least half of their costs in this way. )

- **Initial ‘on account’ general levy.** At the beginning of the year, there would be an initial general levy, which would raise 100% of the budgeted operating costs of the Scheme on account. The levy would be apportioned between members on the basis set out in paragraphs 5.23 to 5.30 below.
- **Case-related charge.** At the end of the year, 50% of the operating costs would be re-allocated to firms on the basis of the number of cases handled under the Scheme and offset against the following year’s fees. The case-related charge would be calculated initially on a ‘flat-rate’ basis (ie by dividing 50% of the costs by the number of completed cases). However, as indicated above, the FSOS will want to consider, in the light of experience of operating standardised procedures, whether certain types of complaint are more complex to handle and justify differential charges for different sectors of the industry.
- The FSOS does not, at present, propose to take account of the validity (or otherwise) of the complaint in the calculation and apportionment of workload costs to individual firms for the reasons set out in paragraph 5.14.
- **Further consultation with the industry.** The FSA and the FSOS propose to liaise with the industry to consider whether there is further scope to improve the balance between fairness and simplicity by refining the methodology proposed above. In particular, consideration will be given to whether it is appropriate to apply different charges in respect of different stages of the complaints-handling process or for different types of complaint.

#### Apportionment of general levy

- 5.23 As noted at paragraph 5.8 above, the existing schemes use a variety of different bases to determine how the general levy is allocated between their respective members, reflecting the different nature of the business done in each of these sectors. All of these aim, in some way, to take account of firms’ size and /or volume of business, but there is currently no single unit of measure which runs across all of the various industry sectors.
- 5.24 The FSA suggested in CP4 that the simplest and most straightforward method of allocating the general levy in the CJ would be to link this to the FSA’s regulatory fees and this gained widespread support. However, the Government’s subsequent decision to allow the Scheme to cover *potentially regulated* financial services activities in specified circumstances means that the coverage of the Scheme can now go beyond that of the FSA. A levy based on the FSA’s regulatory fee might not reflect the extent to which a firm was doing *regulated* business which was *not* subject to the Scheme’s jurisdiction or *unregulated* business which *was* subject to the Scheme’s jurisdiction. Nor

would it take account of the extent to which a firm's business was done with eligible complainants.

5.25 Subject to respondents' views, we therefore propose, in the first instance at least, to recover the total operating costs of the Scheme using, as far as possible, the units of measure used by the existing schemes, but rationalised wherever possible. The proposed relevant units of measure are:

- **Numbers of relevant accounts** – banks and building societies (currently OBO/OBSO)
- **Relevant turnover** – all insurance companies (life and general); (currently IOB and PIAOB)
- **Funds under management** – investment managers (currently OIO)
- **Number of registered individuals/approved persons** – IFAs (currently PIAOB) and current RPB members (currently RPB schemes); stockbrokers and futures and options dealers (currently SFA Complaints Bureau).

For IFAs (and current RPB members) the relevant unit of measure could be **relevant turnover** (as with insurance companies) rather than the **number of registered individuals**.

**We would welcome views from these firms as to which unit of measure would be more appropriate.**

5.26 Where firms are able to provide figures which reflect their 'eligible business' (ie the extent to which their business activities fall within the scope of the CJ and are conducted with potentially eligible complainants) we will use these figures. However, we recognise that some firms may find it problematic – or administratively burdensome – to provide precise data. Where this is the case, we propose that this information should be provided on a 'best estimates' basis.

5.27 A matrix will then be needed in order to equate these different measures.<sup>3</sup> Annex D sets out a possible matrix, which attempts to band different types of firm into 5 comparable categories, ranging from very small organisations (Band A) to very large organisations (Band E). It also seeks to give an approximate indication of the likely levy which firms in each category might expect to pay.

5.28 However, it must be stressed that these figures are illustrative only, based on current available data from the existing schemes. This is not a precise science and these figures will, in any case, have to be adjusted to take account of 'new

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3 For the purposes of the matrix at Annex D, it has been necessary, in the case of banks, to use the value of personal sector deposits, rather than the number of relevant accounts, (which is the unit of measure proposed in paragraph 5.25) because information on the latter is not currently available.

firms' which are not currently members of the existing schemes (eg RPB firms). We propose to do further work on the matrix of unit measures in consultation with the industry and, in the longer term, the FSA and the FSOS will want to consider whether it is possible to identify a single yardstick which all sectors could use. **In the meantime, however, we would welcome views from firms about the appropriate 'banding' criteria for the matrix.**

- 5.29 This matrix cannot, of course, reflect the effect of the case-related adjustment, which will depend on the number of complaints against individual firms resolved under the Scheme. However, assuming, for example, operating costs of £20 million, a constituency of 10,000 firms in the CJ and a total of 30,000 cases handled under the Scheme per year, this would produce a flat-rate case-related charge of £333 (ie 50% of £20 million divided by 30,000 complaints). This would be applied to firms in proportion to the number of cases about them handled under the Scheme. If a firm generated no complaints, it could expect to pay only half of the amount indicated in the matrix, (plus, in the initial years of the Scheme, its contribution to the cost of setting up the Scheme – see section on 'Establishment Costs' below).

#### Should charges be weighted in favour of small firms?

- 5.30 A further issue for consideration is whether, once the basis for assessment of the general levy has been applied, a small firm's contribution should be calculated on the same basis as that appropriate for much larger institutions. The FSA believes that there is a case for applying a reducing scale of charges so that a small firm would pay a proportionately lower fee in relation to its unit of measure than a larger firm. The figures at Annex D show how such weighting might work. Any case-related charge might be similarly moderated. For very small firms in Band A, a special arrangement might be possible whereby contributions for a group of small firms (eg cash plan health providers) could be pooled.

Q5.1 Views are sought on:

- (a) whether respondents agree with the overall approach set out above;
- (b) whether respondents agree with the proposed units of measure for different sectors and, for IFAs and current RPB members, which of the two proposed measures they would prefer;
- (c) the extent to which firms will be able to identify their 'within scope' business;
- (d) the form which the matrix should take; and
- (e) whether a reducing scale should be applied in calculating the general levy.

## Transitional funding arrangements for 2000-2001

5.31 Transitional arrangements will be needed to fund the first few months of the new Scheme's operation up to the end of March 2001, as it is expected to assume its statutory powers (including its funding powers) part way through the financial year 2000-2001. The existing schemes (which currently have different financial year ends) will have to raise their fees prior to N2 in 2000 in accordance with their existing procedures. It therefore makes sense for the post-N2 portion of this particular year to be funded, as far as the CJ is concerned, in a way which is based as far as possible on the existing schemes' funding mechanisms.

5.32 We therefore propose that:

- the levies raised by the existing schemes during the course of 2000 should be raised in accordance with their existing procedures (including any case-related adjustments) but should *all* be calculated on the basis of a year end of March 2001;
- the remaining portion of the sums raised by each of the schemes should, subject to the agreement of the existing schemes, be transferred to the FSOS at N2 to fund the new Scheme's operations for the remainder of the year; and
- additional fees will need to be raised at N2 for 'new' firms / sectors which were not members of any of the existing schemes prior to N2 (eg solicitors or accountants who will require authorisation by the FSA).

Q5.2 Do respondents agree with the proposed transitional funding arrangements?

## Proposed funding arrangements for the Voluntary Jurisdiction

5.33 The FSOS proposes to fund the VJ along as similar lines as possible to the CJ, although the budgets will be separate. As in the CJ, VJ participants would be required to pay an annual levy on account, 50% of which would be adjusted on a case-related basis. The FSOS will identify an appropriate size-related measure in relation to VJ participants' eligible business for the purpose of calculating the annual levy. The precise measure may vary as between different categories of VJ participant, depending on the nature of the business which they conduct. Should an authorised firm which is subject to the CJ choose to join the VJ in respect of its non-CJ activities, its annual levy will be calculated on the same basis and increased accordingly. Unlike the CJ, there will be no need for special arrangements to cater for the likely mid-year timing of N2, since the VJ will, by definition, cover ground not previously covered by the existing schemes.

Q5.3 Do respondents agree with this approach to funding the VJ?

## Who should fund the operating costs of the new Scheme?

- 5.34 All FSA authorised firms which are capable of giving rise to eligible complaints will be required to contribute towards the operating costs of the CJ, irrespective of whether or not they actually generate complaints.
- 5.35 As noted in Chapter 3, we will, however, be willing to consider applications for an exemption from this obligation from authorised firms whose 'permissions' rule out the possibility of their doing business which could give rise to an eligible complaint (eg where they cannot conduct activities subject to the CJ or are not permitted to do business with potentially eligible complainants). However, the onus will be on the firm to seek the exemption.
- 5.36 The operating costs of the VJ will be funded by those firms which choose to participate in it in accordance with standard terms set by the FSOS.
- 5.37 **The FSA therefore proposes that all firms which are capable of giving rise to an eligible complaint in the CJ or the VJ should contribute towards the operating costs of the Scheme, but that authorised firms which cannot give rise to an eligible complaint should be able to apply to the FSA to be exempted from this obligation in respect of the CJ.**

## Establishment costs

- 5.38 The Bill enables the FSA to recover the costs of setting up the new Scheme, (including those incurred before N2) from the firms which the FSA will authorise at N2. These 'establishment costs' will include, amongst other things:
- employment costs prior to N2 (Board and interim staff etc);
  - cost of consultants; and
  - co-location costs
- 5.39 Establishment costs are currently being underwritten by the FSA until the FSOS obtains its own line of credit, based on the prospective funding powers in the Bill. A separate record is being kept of these costs and they will be recovered after N2 when the relevant powers come into force.
- 5.40 The FSA proposes that, as with the operating costs, these costs should be recovered from *all* authorised firms which are capable of giving rise to an eligible complaint<sup>4</sup> since, as noted above, all firms will benefit from the existence of the new Scheme. We propose that these costs should be recovered

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4 (ie excluding those firms exempted in accordance with the proposals at paragraph 5.35 above)

evenly over a period of three years from the year following the commencement of the Financial Services and Markets Bill. Subject to the views of respondents, we would propose to do this by adding one third of the 'establishment costs' to the operating costs of the Scheme in each of those years and allocating the combined total between those firms on the same basis as the 'on account' levy. The case-related adjustment would be applied to 50% of the *operating costs for the relevant year* (ie excluding the additional establishment costs element).

Q5.4 Do respondents agree with this proposal for recovering the 'establishment costs' of the Scheme?

# 6 Complaints handling by firms

- 6.1 The FSOS will play a vital role in providing consumers with access to speedy and effective dispute resolution. However, it is essentially the backstop in a two-stage process. Responsibility for attempting to resolve a complaint must rest, in the first instance, with the firm itself. It is in the interests of both firms and consumers that complaints should be resolved at the earliest possible stage.
- 6.2 The new legislation will give the FSA the power to make rules requiring authorised firms to establish appropriate procedures for resolving complaints which arise out of activities (whether regulated or unregulated) which are subject to the CJ.<sup>1</sup> The FSA will be able to make rules preventing a complaint from being dealt with under the Scheme unless the firm has had a reasonable opportunity to attempt to deal with the matter, and is also required to set time limits within which a consumer should refer a complaint to the Scheme once the firm has finished dealing with it. The FSOS will impose similar requirements on unauthorised firms which choose to join the Scheme's VJ.
- 6.3 This Chapter deals with the complaints-handling requirements which the FSA proposes to apply to authorised firms which do business with consumers who will be eligible to use the Scheme. The requirements outlined below will not apply to authorised firms who are not permitted to do business which could give rise to an eligible complaint (eg firms which deal solely with professional customers, such as market counterparties). The FSA recognises that these firms' customers do not need or want the same level of protection as is necessary for retail consumers. However, we believe that it is good practice for all firms to have a complaints procedure in place which is appropriate to the nature of their business and would, therefore, encourage wholesale firms to subscribe to alternative dispute resolution mechanisms specifically designed for this purpose.

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1 Paragraph 14 of Schedule 14 to the Financial Services and Markets Bill.

## Current position

- 6.4 Most firms which will be authorised by the FSA are already subject – on either a compulsory or a voluntary basis – to a requirement to have internal procedures in place for dealing with complaints which they receive from consumers and the majority of complaints are settled between the firm and the consumer without recourse to an independent mechanism.
- 6.5 Investment businesses authorised under the Financial Services Act 1986 are already subject to compulsory regulatory requirements, which set out in detail the steps which must be followed in handling a complaint. Building societies are also subject to specific complaints-related requirements under the current building societies legislation. Whilst banks and insurance companies are not currently subject to compulsory requirements on complaints handling, approximately 95% of those which deal with retail customers have internal complaints procedures in place and belong to the relevant voluntary Ombudsman Scheme, in line with voluntary codes of practice to which they subscribe.
- 6.6 The number of firms which will be authorised by the FSA but are not already required to have internal procedures in place is therefore relatively small, and most of these firms are, in any case, likely to have in place some mechanism for dealing with complaints which they receive, as a matter of good commercial practice.
- 6.7 In the interests of protecting consumers, the FSA believes that *all* authorised firms which deal with private individuals (or small businesses which would be eligible to complain to the Scheme) should, in future, be *required* to have appropriate complaints-handling procedures in place. We believe that the costs of doing so will be outweighed by the benefits both for firms and consumers alike.

## Good internal complaints-handling procedures

- 6.8 The benefits of effective complaints procedures are already widely recognised by firms as well as by consumers. The fact that such a high proportion of banks and insurance companies with retail customers have *voluntarily* joined the existing ombudsman schemes would appear to be strong evidence of this. However, research conducted for the FSA<sup>2</sup> suggests that complaints-handling procedures in some financial services organisations are not working as effectively as they might and annual figures from all of the existing ombudsmen schemes for financial services show that the number of complaints being referred to the schemes is increasing year on year.<sup>3</sup>

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2 NOP Survey conducted for the FSA, 1999.

3 Latest annual reports of the Banking Ombudsman, Building Societies Ombudsman, Insurance Ombudsman, Investment Ombudsman and the PIA Ombudsman.

- 6.9 An increase in complaints received by a firm is not necessarily a reflection of deteriorating standards of service – it could be an indication that the firm has accessible complaints procedures. However, an increase in the proportion of complaints going through to the Ombudsman from a particular firm would seem to suggest that a firm’s complaints procedures are not as effective as they might be.
- 6.10 Extensive research published by the Consumers’ Association<sup>4</sup> on the handling of consumer complaints by a wide range of businesses, including financial services firms would appear to support these findings. It seems that:
- many consumers do not actually make a complaint when they are dissatisfied because they do not find complaints procedures accessible or easy to use;<sup>5</sup>
  - those who do make a complaint frequently feel that their complaint is being ignored;<sup>6</sup>
  - many consumers are not happy with the way in which their complaints are handled – particular sources of consumer dissatisfaction with the complaints-handling process include the length of time taken by the firm to investigate the complaint and the firm’s failure to keep them informed of progress; and
  - many consumers are dissatisfied with the outcome of their complaints and feel that the firm’s response does not properly address or resolve the cause of their complaint.<sup>7</sup>
- 6.11 Many financial services firms do, however, attach importance to handling consumer complaints well. Our aim is to build on current good practice within the industry and beyond and make this the norm across the FSA authorised constituency. The FSA proposes to assist firms as far as possible to achieve high standards in complaints handling and, in addition, the FSOS proposes to publish guidance and regular bulletins and advice.
- 6.12 A great deal of work has been conducted by various organisations about what constitutes best practice in terms of handling complaints. In particular, the British Standards Institution has recently produced a new British Standard, ‘Complaints Management Systems – Guide to Design and Implementation’ (BS8600). This Standard was drawn up by a technical committee comprising a wide range of largely private sectors groups, including small businesses, and has been designed to be applicable to firms of any size or type.

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4 *Handled with care? Consumer Complaints 1991-7* Consumers’ Association Policy Report

5 CA Policy Report.

6 NOP Survey.

7 NOP Survey; CA Policy Report; TPR Report prepared for ABI, July 1998.

- 6.13 British Standard 8600 identifies the key attributes of a good complaints-handling process as follows:
- **a complaints policy:** outlining the organisation's commitment to – and procedures for – dealing with customer complaints;
  - **visibility:** making sure customers know where to complain and have all the information to hand;
  - **accessibility:** enabling the customer to complain, with ease, at any point in the process; and
  - **fairness:** making the system fair to both customers and staff.
- 6.14 In particular, it highlights the need for:
- **adequate resources** to deal with the complaints received;
  - **staff training** to ensure that those who deal with customers understand the procedures and operate them properly;
  - **delegation of responsibility** to enable staff to deal quickly and efficiently with routine complaints;
  - **escalation procedures** to ensure that in the event of a serious complaint, key staff are alerted and the problem is dealt with by whoever has the appropriate expertise;
  - **external review mechanism** to be available where internal procedures become deadlocked; and
  - **follow-up action** to ensure that the firm learns from any mistakes, and improves products and services and the complaints system where necessary.

## Proposed FSA requirements

- 6.15 In setting the rules relating to firms' complaints-handling procedures, we believe that the focus should be on achieving settlements which are fair both to the firm and to the consumer. The proposals which follow aim to provide firms with sufficient flexibility to enable them to adopt complaints-handling arrangements which suit their particular type of business and take account of the size of the firm. This is particularly important given the wide range of businesses which will be authorised by the FSA.

### Firms' complaints procedures

- 6.16 The FSA therefore proposes to make a simple over-arching rule, requiring all relevant firms to have in place an appropriate written complaints procedure

and to ensure that this is operated effectively. A small number of specific rules will also be necessary in order to set out what the FSA sees as the minimum standards for an appropriate complaints procedure. These will include, for example, time limits for dealing with complaints and requirements concerning firms' relationship with the FSOS.

- 6.17 The British Standard on Complaints Management Systems provides a helpful source of guidance on what constitutes an appropriate complaints procedure for the purposes of these rules, and the FSA would strongly encourage firms to adopt a procedure which complies with this Standard as a means of fulfilling the requirements laid down in the rules. Copies of the British Standard are available from the British Standards Institution.<sup>8</sup>

### Definition of complaint

- 6.18 For the purposes of rules relating to a firm's own complaints-handling arrangements, the FSA proposes that the definition of 'complaint' should be widely drawn and include any expression of dissatisfaction from a customer, whether oral or written and whether justified or not. For Scheme purposes, however, a 'complaint' should also involve an allegation that the complainant has suffered financial loss, distress or material inconvenience.

### Access

- 6.19 It is proposed that firms should be required to publish their complaints-handling procedures and to make them easily available to consumers. In particular, firms should publicise the availability of their complaints procedures and their membership of the Ombudsman Scheme at the initial point of sale and should send complainants a copy of these procedures when a complaint is first made.
- 6.20 We also propose to include on the FSA's Register of authorised firms details of a contact point within a firm whom consumers should contact in the first instance. These details could include the name, telephone number and address (including e-mail) of the designated contact point or, for those firms which have established them, it could include a dedicated customer-service telephone number.

- Q6.1 Do respondents agree that the FSA Register should make these details available to consumers?

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<sup>8</sup> British Standards Institution, 389 Chiswick High Road, London, W4 4AL. Telephone 020 8996 9000  
Website: [www.bsi.org.uk](http://www.bsi.org.uk)

## Handling

- 6.21 We propose to require firms to investigate all complaints promptly and, wherever possible, to make provision for the complaint to be reviewed by a senior member of staff who was not involved in the matter. Details of the proposed time limits for handling complaints are set out below. In addition, we propose that firms should ensure that complainants receive a prompt acknowledgement of their complaint, which sets out the name of the relevant contact point in the firm and when the complainant can expect to receive a substantive response.
- 6.22 It is also proposed that firms should be required to ensure that appropriate management controls are in place to ensure that complaints are handled fairly and consistently and that recurring or systemic problems are identified and remedied. Most firms will already have such controls in place as a matter of good business practice.

### Time limits:

For firms to resolve complaints

- 6.23 The current requirements relating to the maximum length of time it should take for a firm to deal with a complaint vary across the different financial sectors. It is proposed that there should be a standard time limit of 4 weeks from the date when a firm first receives a complaint for the firm to respond to the complainant with a substantive response which either:
- (a) accepts the complaint and offers redress, where appropriate;
  - (b) rejects the complaint with reasons for doing so; or
  - (c) explains that the firm has been unable to resolve the complaint and needs more time in which to do so, giving reasons for the delay.
- 6.24 In the case of either (a) or (b), the complainant should be informed that if he or she is not happy with the firm's response, he or she has the right to refer the matter to the Scheme. A Scheme complaint form and explanatory leaflet should also be sent to the complainant at this point. Where (c) applies, we propose that the firm should be permitted a further 4 weeks to attempt to resolve the complaint. If, during the extended time period, the firm either accepts or rejects the complaint, it should follow the procedure outlined for (a) or (b) above. However, if, after the expiry of this extended time limit, the firm is not able to resolve the complaint, the complainant should be informed of his or her right to refer the matter to the Scheme.

For complainant to refer a complaint to the Scheme

- 6.25 Time limits for referring complaints to the existing schemes following investigation by the firm also vary. We propose that there should be a time limit of 6 months from the date of receipt of the firm's substantive response for complainants to refer the matter to the Scheme. The Ombudsman would be entitled to refuse to handle complaints which were not sent to the Scheme within this time frame, but would have discretion to waive this time limit in circumstances where he saw fit.

For complainant to make a complaint

- 6.26 Again, the current time limits for making a complaint after the act or omission giving rise to the matter in question varies between the existing schemes. For the purposes of the new Scheme, we propose to apply the time limits enshrined in English law relating to the limitation of actions. In other words, the Ombudsman would be entitled to refuse to investigate a complaint which was brought to the Scheme more than 6 years after the event or more than 3 years after the date when the complainant became aware or ought reasonably to have become aware of the cause of complaint, if this was longer. However, the Ombudsman would have discretion to deal with such complaints where he considered this to be appropriate. These provisions are slightly more generous than the equivalent provisions applicable in Scotland, but we propose that a single limit should be applied.

Q6.2 Do respondents agree with the proposed time limits?

### Outcome

- 6.27 Where a firm decides that a complaint is valid, the FSA proposes that the firm should offer the complainant an appropriate level of redress. Where a firm decides that a complaint is not valid, it should give its reasons for reaching this decision.

### Reporting requirements

- 6.28 Firms which are currently subject to conduct of business regulation will be familiar with the requirement to report details of complaints they receive to their regulatory authority (although the particular requirements of each regulatory authority differ). Firms which are subject to prudential supervision only are not currently required to report details of complaints to a supervisory body. Such firms include banks, insurance companies and building societies.
- 6.29 The FSA will continue to need feedback on the number and nature of the complaints received by firms which will be subject to conduct of business regulation. Such feedback provides valuable information to the FSA. This

would, however, not involve disclosure of individual cases and information could, wherever possible, be provided electronically.

6.30 In order to gain a comprehensive picture, it would be desirable for the FSA to receive information on complaints from *all* authorised firms. However, to introduce reporting rules for firms subject only to prudential supervision would be a new departure in this area. Nevertheless, we would expect that, as a part of good management practice, most firms would collect data about the number and type of complaints they receive for internal use, and many larger retail firms will have unified corporate systems for complaints monitoring, regardless of whether the activity is regulated on a prudential or conduct of business basis.

Q6.3 The FSA would therefore welcome views from prudentially supervised firms as to how onerous it would be to provide such data. In particular, we would welcome views from firms where some aspects of the business are subject to conduct of business regulation and others subject to prudential supervision, as to whether it would be simpler to report details of all their complaints to the FSA, rather than to separate them – especially as some complaints might relate to both types of business.

6.31 Whilst feedback on complaints experience will be an important part of the regulatory picture for the FSA, we are keen to avoid imposing unnecessary burdens on firms. With this in mind, we propose that authorised firms should be required to provide the FSA, on a bi-annual basis, with returns, giving information about:

- (i) the number of complaints received;
- (ii) the percentage of complaints resolved within the 4 week and 8 week period; and
- (iii) a breakdown according to the subject of those complaints.

6.32 We appreciate that it will not necessarily always be clear to a firm whether a complaint has been resolved or not. We therefore propose that, for the purposes of (ii) above, a firm should be able to regard a complaint as 'resolved' where it either knows that the complainant has accepted the firm's position or has no evidence, after a period of 6 months, to suggest that the complainant has not done so.

6.33 In providing a breakdown of the types of complaints received, it would be helpful if firms were to categorise complaints on a common basis. We should therefore welcome views on what categories might be appropriate – for example, complaints about customer service; unfair charges; poor or misleading information; maladministration.

Q6.4 Do respondents agree with the proposed frequency and content of these reports and do they have views on what the appropriate categories should be?

### Monitoring the quality of firms' complaints handling

- 6.34 The FSA proposes to monitor the quality of firms' complaints-handling procedures in a variety of ways:
- **through consumers** – by encouraging consumers to contact the FSA if they are unhappy with how a firm is handling their complaint;
  - **through firms** by reporting requirements (see above); and
  - **through regulatory means** – ie via the FSA's monitoring teams.
- 6.35 Consumer feedback on whether or not firms' complaints procedures are working will play an important part in helping us to monitor the quality of those procedures. The FSA intends to be proactive in promoting understanding of consumer rights so that consumers will know what they can and should expect from the financial services firms with which they deal. Consumers will be encouraged to contact the FSA Consumer Helpline if they experience any difficulty in getting a firm to deal with their complaint. This is not to suggest that the FSA will become involved in looking at the merits of a particular case where the consumer is unhappy with the firm's response – that will be the role of the new Scheme.

### Record-keeping requirements

- 6.36 The quality of firms' complaints-handling procedures will also be monitored by the FSA's supervision teams. They will need to have access to firms' complaints files in the course of compliance visits in order to satisfy themselves that a firm's procedures are being properly operated in practice. Firms will, therefore, need to make and retain records of any complaints which they receive for a set period of time. Current requirements vary between sectors and some sectors are not subject to any specific requirement to retain records. **We suggest that the length of time that complaints records should be retained should be linked to a firm's monitoring cycle. However, firms will need to retain their complaints files until after the expiry of the period when a complaint could be referred to the Ombudsman Scheme (ie for at least 6 months after the firm's final response to the complainant) if this is longer.**

Q6.5 We should welcome views on these proposed requirements.

## Feedback from FSOS to the FSA

- 6.37 The FSA also expects to receive some feedback from the FSOS itself, since the new Scheme will be an important part of the new regulatory system, with a crucial role to play in enabling the FSA to fulfil its consumer protection objective. Apart from providing valuable early warnings of problems in particular firms or sectors, or with particular products or regulatory requirements, complaints may also indicate the existence of a more widespread, systemic problem which requires FSA attention. In addition, the FSA will require information to enable it to fulfil its own statutory duty of ensuring that the FSOS is at all times capable of exercising its statutory functions.
- 6.38 The need for the FSA and the FSOS to share information was highlighted in CP4 and widely accepted by respondents. Some concerns were expressed about the provision of case-specific information, focussing mainly on confidentiality and data protection issues. The FSA fully accepts the need to respect the confidentiality of personal information provided under the Scheme and does not expect the FSOS to provide it with specific information about individual cases unless it decides to do so. There is no question of the FSOS's being required to notify the FSA of every rules breach which it identifies or to pass over individual case files. The FSOS will retain discretion over what (and when) information is provided.
- 6.39 In some circumstances, it may be appropriate for the FSA to provide the FSOS with information relevant to the performance of its functions – eg where the FSA may be taking disciplinary action which might result in restitution for complainants. This would enable an FSOS Ombudsman to decide whether he wished to stay his investigation of a complaint against that firm pending the resolution of the regulator's disciplinary proceedings.

## Co-operation with the FSOS by firms

- 6.40 The FSA proposes to require authorised firms to co-operate fully with the FSOS in its investigation of complaints. Co-operation with the FSOS is not confined to complying with Scheme requirements, such as producing requested documents without undue delay, attending oral hearings where these are required and complying promptly with any settlements agreed as a result of conciliation or final awards made by the Ombudsman. It also involves complying with the spirit of the Ombudsman Scheme in a way which recognises the importance attached to speed, informality and flexibility.
- 6.41 An open, co-operative and constructive approach from firms will be particularly important given the emphasis which will be placed on the use of conciliation between parties to resolve disputes. The FSA therefore proposes to encourage firms not to take any precipitate action (such as pursuing legal

proceedings) which would prejudice the resolution of a bona fide complaint under the Scheme or under the FSA's procedural rules.

Q6.6 We would welcome respondents' views on this approach and on how it might best be achieved without restricting firms' rights unduly.

### Cost benefit analysis

- 6.42 The FSA does not believe that the proposals outlined in this chapter should place a material burden on authorised firms by way of additional costs, since the vast majority of firms to which these rules will apply have already established, under either compulsory or voluntary regimes, internal complaints procedures for dealing with complaints from their customers.
- 6.43 The proposed new rules may, however, necessitate some modifications to existing systems, particularly where firms are not currently subject to specific formal rules, and these may involve some one-off costs. However, the ongoing costs of compliance should not be greater than currently.
- 6.44 Costs are likely to be greater for those firms which are not currently subject to any requirement to have internal complaints procedures in place, unless they have put such procedures in place as a matter of good business practice. We expect that a substantial number will have done this, but we have no precise information on this point. **We should therefore particularly welcome views from these firms as to the extent to which our proposals will impose additional costs on them.**
- 6.45 We believe, however, that the benefits to be derived from implementing high standards of complaints procedures across the industry will outweigh any costs incurred. These will include increased consumer protection in the form of a simpler, more comprehensive and accessible complaints mechanism and greater consumer confidence in the financial services industry as a whole, from which firms, in turn, will also benefit.

# FSOS Board members

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Charles Wilson

# List of types of disputes covered by Compulsory Jurisdiction under Option (2)

	Currently covered by
<b>Deposit Taking and Lending</b> <i>including disputes about:</i>	
- current accounts – sales/service/charges/interest	OBO/OBSO
- deposit/savings/investment accounts – sales/service/charges/interest	OBO/OBSO
- cash ISAs	OBO/OBSO
- card services and cash machines, including credit/debit and cheque guarantee cards	OBO/OBSO
- unsecured lending/overdrafts – sale/service/charges/interest	OBO/OBSO
- payment systems including direct debits and standing orders	OBO/OBSO
- mortgage lending – sale/service/product/set-up/information/release/penalties	OBO/OBSO
- mortgage interest/charges	OBO/OBSO
- mortgage repayments	OBO/OBSO
- mortgage repossession practice	OBO/OBSO
<b>Insurance</b> <i>including disputes about:</i>	
- general insurance – sales/service/issue/admin/marketing/failure of initial proof/no claims discount/non-disclosure/policy terms/under-insurance/quantum	IOB/PIAS/OBO/OBSO
<b>Investments</b> <i>including disputes about:</i>	
- life insurance – advice/suitability/sales/advertising/arranging/negligent management/rule breaches/commission	PIAOB
- life insurance – administration	PIAOB VJ
- non-investment life insurance – advice/suitability/sales/advertising/arranging/administration	PIAOB VJ/IOB
- investment management – mismanagement	OIO
- unit trusts – advice/sales/suitability/management	OIO/PIAOB
- PEPs/ISAs (stocks & shares and insurance) – advice/sales/suitability/management	OIO/PIAOB
- securities and derivatives – advice/dealing/management/administration/advertising	SFACB
- personal pensions – advice/suitability/sales/advertising/management/rule breaches/commission	PIAOB/OIO/SFACB
- stakeholder pensions (from 2001) – advice/sales	N/A
- SERPS (contracted out by protected rights)	PIAOB
<p>Key: OBO: The Office of the Banking Ombudsman; OBSO: the Office of the Building Societies Ombudsman; IOB: Insurance Ombudsman Bureau; OIO: the Office of the Investment Ombudsman; PIAOB (VJ): PIA Ombudsman Bureau (Voluntary Jurisdiction); PIAS: Personal Insurance Arbitration Service; SFA CB: SFA Complaints Bureau and Arbitration Service.</p>	

## Funding mechanisms of existing ombudsman schemes

	Insurance Ombudsman Bureau	Office of the Building Societies Ombudsman	Personal Investment Authority Ombudsman Bureau	The Office of the Banking Ombudsman	Investment Ombudsman SFA Complaints Bureau
Sources of Funding	Fixed case charge Balance collected by levy	50% case fees (approx) 50% standing levy (approx)	100% of fixed costs and 30% of variable costs are funded by the regulator 70% of variable costs funded through case fees	5% (approx) collected by levy and case charge on small banks. Balance of 95% collected on basis of levy and case charge from larger banks	Funded from SRO membership fees
Calculation of Standing Charge/Levy	Insurers: Levy is based on annual turnover (gross premium income)  Non Insurers: Levy is based on total gross brokerage and fees (with minimum levy of £50 for turnover under £0.5 million and maximum of £5,000 for turnover over £50 million)	Standing levy is based on value of building societies' assets with a min. fixed charge of £1,725 and a maximum of £11,500  1. Under £100 million Fixed: £1,725 Variable: Nil  2. Up to £500 million Fixed: £3,500 Variable: £2.25 per million  3. Up to £1 billion Fixed: £7,000 Variable: £2.25 per million  4. Over £1 billion Fixed: £11,500 Variable: £2.25 per million	Same basis as PIA membership fees	1. Flat Rate levy of either £5,000 or £2,500 charged to smaller banks (based on number of accounts)  2. Once the flat rate levy and case charges are collected from smaller banks, the remaining budget apportioned to larger member banks – 25% according to number of accounts and 75% according to the number of written complaints received	Same basis as IMIRO/SFA membership fees
Case Charge	Flat rate case charge  Where the complaint is also against the insurer there is a reduced case charge for the non-insurer	Flat rate case charge	Flat rate case charge	Large banks pay a variable case charge, as described above  Small banks pay a flat rate case charge	No case charge
Credits or Refunds?	No charge when case is closed prior to investigation	A reduced fee for repeat case or frivolous/vexatious Full refund where case is outside terms of reference	Full credit if case is determined to be frivolous or vexatious	None	None

Illustrative annual levies					
	Band A	Band B	Band C	Band D	Band E
Relevant Turnover (income from premiums)	N/A	N/A	Under £10m	£10m – £100m	Over £100m
No. of Life Offices (PIAOB) <sup>1</sup>	N/A	N/A	136	129	113
Registered Individuals	1 – 5	6 – 10	11 – 50	51 – 150	151+
No. of SFA Firms (SFA CB) <sup>2</sup>	505	255	411	123	72
Funds Under Management	N/A	N/A	Under £250m	£250m – £1bn	Over £1bn
No. of IMRO Firms (OIO) <sup>3</sup>	N/A	N/A	399	132	192
Relevant Turnover	Under £100,000	£100,000 – £500,000	£500,000 – £1m	£1m – £5m	Over £5m
No. of IMRO Firms (Advisors) (OIO) <sup>3</sup>	125	139	51	89	30
1. Relevant Turnover (commissions and fees)	Under £100,000	£100,000 – £800,000	£800,000 – £1,900,000	£1,900,000 – £7,500,000	Over £7,500,000
2. Registered Individuals	1	2 – 10	11 – 25	26 – 100	101+
No. of IFAs (PIAOB) <sup>1</sup>	1276	2045	136	62	26
Relevant Turnover income from premiums)	N/A	N/A	Under £10m	£10m – £100m	Over £100m
No. of General Insurance Cos (IOB) <sup>4</sup>	N/A	N/A	52	40	28
No. of private customers	Under 20,000	20,000 – 50,000	50,000 – 250,000	250,000 – 1m	Over 1m
No. of Building Societies (OBSO) <sup>5</sup>	19	15	17	12	5
Value of Personal Sector Deposits <sup>6</sup>	Under £100,000	£100,000 – £500,000	£500,000 – £1m	£1m – £10m	Over £10m
No. of Banks (OBO) <sup>7</sup>	255	65	31	50	11
Total number of firms <sup>8</sup>	2180	2519	1233	637	477
Illustrative Levy <sup>9</sup>	£200 – £300	£350 – £500	£1.5K – £2.5K	£5K – £7K	£25K – £30K

1 Source of data, PIA. 2 Source of data, SFA. 3 Source of data, IMRO. 4 Source of data, IOB. 5 Source of data, BSA Year Book 1999/2000.

6 It has been necessary to use the value of personal sector deposits, rather than the number of relevant accounts, (which is the unit of measure proposed in paragraph 5.25) because information on the latter is not currently available.

7 Source of data, FSA.

8 NB The matrix does not include 'new firms' which are not currently members of the existing schemes but will be in the CJ after N2. Further, the total number of firms for the general insurance constituency is based on current membership of the IOB which is voluntary. It does not include all insurance companies which will be authorised by the FSA and potentially subject to the CJ of the new Scheme.

9 These illustrative levy ranges have been calculated on the basis of assumed operating costs of £20m.

# Glossary

<b>BIOA</b>	British and Irish Ombudsman Association
<b>CJ</b>	Compulsory Jurisdiction
<b>CP4</b>	FSA Consultation Paper 4: Consumer Complaints
<b>ECHR</b>	European Convention on Human Rights
<b>EEA</b>	European Economic Area
<b>FSA</b>	The Financial Services Authority
<b>FSOS</b>	Financial Services Ombudsman Scheme Limited
<b>GISC</b>	The General Insurance Standards Council
<b>IFA</b>	Independent Financial Adviser
<b>IMRO</b>	Investment Management Regulatory Organisation
<b>IOB</b>	Insurance Ombudsman Bureau
<b>N2</b>	The date when the Financial Services Authority will acquire its powers under the Financial Services and Markets Act.
<b>OBO</b>	Office of the Banking Ombudsman
<b>OBSO</b>	Office of the Building Societies Ombudsman
<b>OIO</b>	Office of the Investment Ombudsman
<b>PIA</b>	Personal Investment Authority
<b>PIAOB</b>	Personal Investment Authority Ombudsman Bureau
<b>PIAS</b>	Personal Insurance Arbitration Service
<b>RPB</b>	Recognised Professional Body
<b>SFA</b>	Securities and Futures Authority
<b>SFACB</b>	Securities and Futures Authority Complaints Bureau and Arbitration Service
<b>SME</b>	Small and Medium Enterprise
<b>SRO</b>	Self-Regulating Organisation
<b>VJ</b>	Voluntary Jurisdiction

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