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By email: consultations@financial-ombudsman.org.uk

Dear Sir / Madam,

Financial Services Consumer Panel response to Financial Ombudsman Service discussion paper: creating a funding model for the future

The Financial Services Consumer Panel (the Panel) is an independent statutory body. We represent the interests of individual and small business consumers in the development of policy and regulation of financial services in the UK. Our focus is predominately on the work of the FCA, however, we also look at the impact on consumers of other bodies' activities and policy where relevant to the FCA's remit. We are responding to this consultation because the Financial Ombudsman Service is a key member of the regulatory family that works closely with the FCA to ensure that consumers get adequate redress for harm caused by FCA-regulated firms. Part of our own vision for financial services regulation is that consumers should get prompt and commensurate redress and the Ombudsman Service plays a vital role in this.

We support many of the proposals within this consultation which embody the Funding Principles (particularly that the service is free to consumers) and protect the key elements of independence, impartiality and longevity for the Ombudsman Service. A sustainable and effective Ombudsman Service should be the main goal of its funding arrangements, and we welcome this review with the aim of ensuring this goal continues to be met.

As we've said previously¹, we believe that the Ombudsman Service must be funded in such a way and to such a level that it is able to handle complaints efficiently, and deal with increasing complexity as well as fluctuations in caseloads. This will ensure consumers get redress and good service in a timely manner. We continue to support the principle that those firms which generate the most work should pay the most.

Though it is important to remember that the Ombudsman Service does a great deal of important work other than case-handling (which not funded by case fees), including:

- work to prevent harm occurring in the first place
- sharing of insight gained from complaints resolution
- consumer communications and outreach
- close engagement with the rest of the regulatory family

This work forms an important part of the Ombudsman Service's wider societal benefit and must be recognised in the new funding structure. This rightly requires a reduced focus on case-fee income and a shift towards a more stable funding basis.

We particularly support the restructuring of the Ombudsman Service's funding arrangements to focus on prevention as this aligns with the FCA's aims for the new

¹ https://www.fs-cp.org.uk/sites/default/files/final_fscp_response_financial_ombudsman_service_annual_plan_and_budget_20220131.pdf p6

Consumer Duty and will help drive the 'cultural reset'² needed in financial services. To achieve this, the Ombudsman Service needs both adequate funding for its proactive prevention work and to ensure the structure of case fees incentivises firms to handle complaints better in the first place (and indeed prevent them altogether) so that they do not reach the Ombudsman Service. We believe the proposals in this consultation will help ensure this is the case.

Our responses to the questions posed in the consultation are included at Annex A below.

Yours sincerely

Helen Charlton
Chair, Financial Services Consumer Panel

² <https://www.fca.org.uk/publication/consultation/cp21-36.pdf> p102

Annex A – Responses to consultation questions

Q1: Do you agree with how we suggest building on our current principles and are there any other factors we should take into account?

The overall principles that the Ombudsman Service is free to customers, fair and transparent are inalienable and must remain so.

We agree with proposal that 'businesses which generate the most work [pay] the most' for the Ombudsman Service. This is an important concept that must underpin the funding arrangements.

Q2: Do you agree with our option of changing the CJ levy to recover fixed overheads?

Yes. The Ombudsman Service provides a vital service to financial services consumers and recovering fixed overheads will help provide a more stable funding basis for the Ombudsman Service, ensuring it can continue to deliver its service.

Q3: Do you agree with our proposal for simplifying the VJ levy?

We would caution the Ombudsman Service to consider the impact of the proposals in this area on the number of firms signing up for the voluntary jurisdiction. On the one hand, the shift from a firm size-based fee to a fixed fee may act as a disincentive to sign up for the voluntary jurisdiction. The consultation says it does not anticipate the fixed fee being more expensive than the current arrangement, but without showing the working for this, firms may not be convinced. On the other hand, the certainty around a fixed fee may encourage more firms to sign up, especially if the Ombudsman Service set out what that fee would be.

Q4: Should we retain our single, flat case fee or do you support a differentiated case fee model?

We continue to support a more differentiated case fee model. Focus should especially be given to incentivising firms which are causing unreasonable delays for consumers to resolve issues more quickly.

As we said in our response to the annual plan and budget³, the Ombudsman Service could consider differential fees based on the number of complaints received proportionate to the size of a firm's customer base. Firms with a higher proportion of complaints relative to the size of their customer base should be charged higher fees. Another potential option is to charge firms additional fees/penalties for delays and make consumers aware of these additional costs and the reasons for them. Both of these options help drive the regulatory prevention agenda as they incentivise firms to prevent complaints arising in the first place.

To maximise the impact of this across the market, the Ombudsman Service should seek to rely more heavily on reputational tools to drive good behaviour, increasing its focus on clearer external communications. We would like to see the Ombudsman Service use the insights it gathers from complaints volumes and uphold rates to publish key performance indicators (KPIs) on how firms are treating consumers. These KPIs should be simple, updated regularly and capable of being understood by consumers so that they can drive consumer decision making. We believe this goes hand-in-hand with the FCA's aim to be

³ https://www.fs-cp.org.uk/sites/default/files/final_fscp_response_financial_ombudsman_service_annual_plan_and_budget_20220131.pdf p7

more outcomes-focused and publish progress metrics, which will help ensure a consistent message across the regulatory family.

Q5: Do you agree that we should charge different case fees according to the stage the case has reached before it is resolved? Do you consider this would create any unhelpful incentives?

Yes. We support the Ombudsman Service's principle that its costs are 'broadly proportionate, with the businesses which generate the most work paying the most, and that it should be 'simple to administer'.

Q6: Do you agree that we should vary case fees according to the type of product the complaint relates to? If you agree, do you think we should also introduce fees that are chargeable according to case stage?

No. There is too much variation within product types in terms of complaint subject and complexity. For example, a person may have a complaint relating to a complex product (e.g. a pension) which concerns a simple issue (e.g. a lack of disclosure of a fee), and vice versa. There is also a risk that this approach would make some products more expensive as firms pass on the increased Ombudsman Service costs to consumers.

Q7: Do you agree with reducing the margin of 15% to 5% and removing the free case allowance in group fee account arrangements?

We have no comment on the reduction of the margin for group account free arrangements. However, we note that the threshold for what is classed as a group has been in place for nearly 10 years and so should be reviewed.

We agree that the free case allowance should be removed for group account fee arrangements. If a firm generates high case volumes, as a matter of fairness, it should pay more.

In fact, we would support the removal of free cases across the system. We believe that the practice of offering free cases is not appropriate and reduces the incentive for firms to do the right thing in the first place. The Panel's view is that, subject to the safeguards on costs incurred as a result of any 'frivolous or vexatious' claims (which are rare), every complaint referred to the Ombudsman Service should be funded by a case fee payable by the firm.

As we said in our response to the Ombudsman Service's annual plan and budget⁴, the Panel believes that the practice of offering 'free' cases needs more detailed consideration to assess what impact the practice has on the ability of the Ombudsman Service to incentivise behaviour change, and fund all the work it needs to do (not just in terms of case-handling but also increased work around prevention, sharing of insight, consumer communications and outreach, and working more closely and effectively with the rest of the regulatory family). An important part of this consideration will be the environment the Ombudsman Service is operating in, which is to a large extent unpredictable in terms of case volumes and 'new' issues that may generate additional work in all workstreams listed above.

Q8: Do you agree that an initial fee at conversion will protect us and levy payers from the risk of not recovering costs for completed work?

⁴ https://www.fs-cp.org.uk/sites/default/files/final_fscp_response_financial_ombudsman_service_annual_plan_and_budget_20220131.pdf p6

Yes. The consultation cites approximately £15 million of bad debt and lost income in 2021/22 with this expected to rise to £17 million in 2022/23. This shows the significant risk to the Ombudsman Service and its ability to operate effectively within a sustainable budget. In addition, the current economic circumstances are expected to worsen over the coming year which could see more firms struggling and unable to pay their debts, including costs due to the Ombudsman Service. Under the present model, firms that are aware they are in financial difficulty when a complaint is referred to Ombudsman Service have a perverse incentive to delay settlement of the case in order to avoid paying the fee. The proposal to introduce an initial fee at conversion therefore seems like a sensible approach to mitigating that the risk of non-payment, and consequent under-funding of the Ombudsman Service, in the current economic climate.

Q9: Do you agree that a time limit of 12 months to claim for overpayment of fees provides firms with a sufficient opportunity to make any claim for repayment?

No comment.

Q10: Do you agree that we should include the data that results from any new fee structure as part of the quarterly report we publish on our website?

Yes. We agree that this data would be useful to, for example, highlight the way different firms respond to complaints and at what stage. It could therefore complement the existing complaints data available. As discussed under Q4 above, the Ombudsman Service's data can be used as a reputational tool to drive good behaviour amongst firms and influence consumer decision making.

Q11: Do you have evidence to demonstrate problematic behaviours from CMCs and do you think a charge from the Financial Ombudsman Service would prevent them?

We do not ourselves have evidence of problematic behaviours from CMCs, though we are aware of concerns amongst industry about poor practice especially in regard to activities of CMCs that are not regulated by the FCA. For example, the FCA is not the regulator for claims management activities that are carried on in the ordinary course of legal practice by some legal professionals, including solicitors and legal executives. Generally, we agree with the observation in the consultation document that 'frivolous or vexatious' cases are rare.

We would therefore caution against imposing a charge for professional representatives as it is likely this charge would be passed on to consumers. This goes against the fundamental principle that the Ombudsman Service should be free to the consumer. Consumers should be free to choose whether to bring their own case (and we have said that this should be encouraged⁵) or to use a representative. It should be remembered that some consumers would not be comfortable or able to bring their own complaint, for example because of a disability or vulnerability, and for these consumers to end up paying more to access redress would be unfair and could amount to a breach of the Equality Act 2010.

Q12: Would you like us to consider introducing differentiated fees based on case complexity in future? How should complexity be defined and how could fees based on complexity be applied most effectively?

We support the proposal to keep the option of refining differentiated fees further to capture case complexity under review. We recognise the challenges this would present for the

⁵ https://www.fs-cp.org.uk/sites/default/files/final_fscp_20210413_response_to_fca_consultation_on_cmc_fee_price_cap_3.pdf

Ombudsman Service but would welcome the opportunity to feed into a future review once thinking has been developed further.

Q13: Would you like us to consider offering discounts for cases resolved in batches in future, or do you think that fees based on the stage a complaint reaches would have the same impact? What would be an appropriate minimum and maximum number of complaints to form a batch?

The Panel feels that the proposal to charge fees based on the stage a complaint reaches would be simpler and would achieve a similar result.

We would also signal the risk that cases settled within a batch resolution regime could equally lead to some consumers complaints not receiving the right level of scrutiny and therefore not achieving the best outcome for them, for example because their individual circumstances may not be taken fully into consideration.

While we recognise the benefits of this approach to mass claims such as PPI, beyond those hopefully rare occasions where mass claims arise, we would always want to see each individual consumer's complaint considered in relation to the harm they have suffered as an individual.

Q14: Would you like us to introduce supplementary fees for firms which are uncooperative and how do you define 'uncooperative'?

Yes. The new Consumer Duty aims to 'drive a cultural reset'⁶ in the financial services sector and fees for uncooperative behaviour would provide a good incentive for firms to improve their behaviour and therefore drive cultural change.

Although unlikely to be included in the definition of 'uncooperative', we would also like to see the Ombudsman Service being clearer about action it takes in response to repeated complaints about the same firm.

Q15: Do you agree that these options should not be taken forward or should we reconsider any of them – and if so, why?

We comment on Option 2 and Option 3 only below.

Option 2: Remove the three free cases allowance for non-group firms.

We do not understand why removing the three free cases for non-group firms would add significantly to the Ombudsman Service's administrative costs. As discussed under Q7 above, we believe that the practice of offering 'free' cases is not appropriate and reduces the incentive for firms to do the right thing in the first place. The Panel view is that, subject to the safeguards on costs incurred as a result of any 'frivolous or vexatious' claims (which are rare), every complaint referred to the Ombudsman Service should be funded by a case fee payable by the firm.

Option 3: Charge a higher fee for cases we find in favour of the consumer, in line with the 'polluter pays' model.

In general, the Panel supports the 'polluter pays' principle and would welcome a more detailed analysis of the impact of implementing this. We acknowledge the concerns raised in the consultation about the income of the Ombudsman Service being linked to the outcome of complaints. However, the 'polluter pays' model may have benefits for consumers by providing stronger incentives for firms to prevent harm and resolve

⁶ <https://www.fca.org.uk/publication/consultation/cp21-36.pdf> p102

complaints more effectively. Therefore, a fuller analysis of this issue is required to show the balance between the risks and benefits of this model.