

## **Consultation on the use of Alternative Dispute Resolution as a means to resolve disputes related to commercial transactions and practices in the European Union**

### **Memorandum from the UK Financial Ombudsman Service**

*25 March 2011*

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#### **Introduction**

The Financial Ombudsman Service is the UK ADR scheme for financial services. It was created by law in 2001, replacing a range of predecessor statutory and voluntary ADR schemes covering particular financial industry sub-sectors, such as banking, insurance and investments. The role of the scheme is to resolve disputes between regulated financial businesses and consumers or micro-enterprises<sup>1</sup>, as an informal alternative to the courts.

Regulated financial businesses<sup>2</sup> with an establishment in the UK are required by law to submit to our jurisdiction. Consumers (or micro-enterprises) with an unresolved complaint against these businesses are eligible to bring their complaint to us – including if they live outside the UK. In most years around 90% of complaints are resolved informally to the satisfaction of both parties. In the remainder of cases a formal decision is made by an ombudsman, whose decision is binding on both parties if it is accepted by the complainant.

EEA financial businesses without a UK establishment can also submit to our jurisdiction voluntarily if their consumer contracts are made under UK law. Several dozen such businesses have done so, including the Luxembourg-based PayPal. Our jurisdiction works in the same way for these businesses, and complainants from both within and outside the UK are eligible to bring their complaints to us in the same way.

Last year we handled more than 925,000 consumer enquiries and resolved more than 166,000 cases. The service is free to consumers, and is funded by the financial businesses it covers. Ours is the largest ombudsman scheme in the world.

#### **General observation**

We welcome the Commission's initiative in this area, and we set out below our perspectives on the questions you have asked in your consultation.

We are aware that the jurisdiction that we have been given under UK law is one of the strongest in the Union and that not all other schemes have the powers or scope that we enjoy, and which both our industry and consumer stakeholders support. As such we would commend our ADR model as one that would successfully address many of the issues that the Commission raises in its consultation paper. We

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<sup>1</sup> As defined in Commission Recommendation 2003/361/EC concerning the definition of micro, small and medium-sized enterprises.

<sup>2</sup> Carrying on, in particular, banking, insurance, investment, consumer credit and payment services.

therefore hope that the Commission's eventual proposal will support the continuing functioning of ADR models such as ours.

## **Consumer and businesses awareness of ADR**

(1) What are the most efficient ways to raise the awareness of national consumers and consumers from other Member States about ADR schemes?

In our context, the regulator has set consumer awareness rules<sup>3</sup> which require financial businesses to inform their customers about the Financial Ombudsman Service. Customers must be informed at three stages: at or immediately after the point of sale; when acknowledging a complaint; and in their final response to that complaint. These obligations apply irrespective of whether the customer is based in the UK or elsewhere. The rules are subject to enforcement by the regulator.

In addition to these rules, we work with a range of consumer organisations and advice agencies to ensure that they are aware of the Financial Ombudsman Service, as many consumers will go to such organisations first if they have a complaint. This enables the consumer to be directed to us as appropriate.

(2) What should be the role of the European Consumer Centres Network, national authorities (including regulators) and NGOs in raising consumer and business awareness of ADR?

Although the consumer awareness rules set by the regulator are strong, it has to be recognised that many consumers who have suffered detriment will lack the confidence to complain, or to take the complaint further if it is initially rejected by the business. Other organisations with whom such consumers might have contact – such as consumer advice agencies and enforcers – do therefore have a role in raising awareness of ADR, and we work with such organisations to do this.

(3) Should businesses be required to inform consumers when they are part of an ADR scheme? If so, what would be the most efficient ways?

As mentioned above, consumer awareness rules set by the regulator require financial businesses to inform their customers about the Financial Ombudsman Service at three stages: at or immediately after the point of sale; when acknowledging a complaint; and in their final response to that complaint. We believe that this is an efficient way of informing consumers about ADR.

(4) How should ADR schemes inform their users about their main features?

Commission Recommendation 98/257/EC on the principles applicable to the bodies responsible for the out-of-court settlement of consumer disputes sets out measures to be taken to ensure the transparency of ADR schemes. We support those principles. Furthermore, in 2008 we asked Lord Hunt of the Wirral to carry out an external review of our approach to accessibility, following which we published a

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<sup>3</sup> See: <http://fsahandbook.info/FSA/html/handbook/DISP/1>

policy statement on our strategic approach to improving service to our users<sup>4</sup>. This set out the steps we have since taken to improve awareness of our scheme in the general population – for example, through targeted awareness campaigns, improvements to the website, and working with financial businesses and other third parties.

### **Involvement of traders/suppliers**

(5) What means could be effective in persuading consumers and traders to use ADR for individual or multiple claims and to comply with ADR decisions?

UK legislation and rules set by the regulator require financial businesses to submit to our scheme's jurisdiction and to inform consumers about this. Although this does not mean that consumers are obliged to use our scheme, the effect is that virtually all unresolved consumer disputes about financial services in the UK come to us rather than go to the courts.

ADR decisions by an ombudsman under our scheme are binding if the consumer accepts them. Compliance with these decisions is very high, and non-compliance is subject to enforcement by the regulator.

(6) Should adherence by the industry to an ADR scheme be made mandatory? If so, under what conditions? In which sectors?

We believe that mandatory adherence by the industry to an ADR scheme has worked well in the financial services sector in the UK. This model has long been recognised by both consumers and industry stakeholders as important in supporting consumer confidence in the sector.

(7) Should an attempt to resolve a dispute via individual or collective ADR be a mandatory first step before going to court? If so, under what conditions? In which sectors?

We do not believe that it would be appropriate to require ADR as a first step before going to court. The legitimacy of ADR depends in part on it being an alternative to the courts, not a replacement for them. Furthermore, in the financial services sector in the UK, there has always been a proportion of disputes that are more appropriate for resolution in court in any event – such as disputes over large sums of money, those involving multiple parties, or those brought by high-net-worth individuals. It is also worth noting that, in our context, if a business takes a consumer to court, the consumer can ask the court to adjourn, in order to allow an ombudsman to consider and decide the case.

(8) Should ADR decisions be binding on the trader? On both parties? If so, under what conditions? In which sectors?

Under our scheme, the decision of an ombudsman is binding on the trader if the consumer accepts it – and if the consumer does not accept it, they remain free to go

<sup>4</sup> See: <http://www.financial-ombudsman.org.uk/publications/policy-statements/accessibility-jul08.pdf>

to court. We accept that this can be perceived as an imbalance between the two parties to the dispute, but we (and the UK authorities) believe that this is justified in order to redress the wider imbalances that are inherent in the relationship between financial services businesses and their customers.

### **ADR coverage**

(9) What are the most efficient ways of improving consumer ADR coverage? Would it be feasible to run an ADR scheme which is open for consumer disputes as well as for disputes of SMEs?

It is feasible to run an ADR scheme which is open for SME as well as consumer disputes. Our scheme accepts complaints from micro-enterprises in the same way as those from individual consumers. This possibility is provided for, for example in the Payment Services Directive<sup>5</sup>, and recognises that the relationship that consumers and micro-enterprises have with financial services businesses are fundamentally the same.

(10) How could ADR coverage for e-commerce transactions be improved? Do you think that a centralised ODR scheme for cross-border e-commerce transactions would help consumers to resolve disputes and obtain compensation?

We do not see a significant difference in nature between disputes concerning on-line, distance-selling or face-to-face transactions. We have therefore designed our service to be able to deal with all of these types of dispute, including the ability to communicate with the parties in the way that is most suitable to them – whether that is on-line or off-line.

(11) Do you think that the existence of a “single entry point” or “umbrella organisation” could improve consumers’ access to ADR? Should their role be limited to providing information or should they also deal with disputes when no specific ADR scheme exists?

In the context of financial services in the UK, the existence of “single entry point” or “umbrella” organisations would have little impact because of the already comprehensive nature of the ADR and complaint-handling arrangements in this sector. In a cross-border context, however, such organisations have greater value. FIN-NET, for example, effectively signposts hundreds of consumers to ADR schemes in other member states. The limit to its current effectiveness, however, is the lack of complete ADR coverage across the financial services sector in some member states – for which the better solution would be to encourage comprehensive ADR coverage in those member states rather than to enable FIN-NET to deal with disputes itself.

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<sup>5</sup> Directive 2007/64/EC of the European Parliament and of the Council on payment services in the internal market.

(12) Which particular features should ADR schemes include to deal with collective claims?

ADR schemes deal best with the individual circumstances of particular cases. In our experience of collective claims scenarios, it is rare that all claimants have identical circumstances. This means that claims need to be resolved individually in any case. However, we recognise that in some scenarios it may be appropriate for a collective issue not to be resolved by regulatory action but rather by the ADR scheme resolving individual claims on a case-by-case basis.

(13) What are the most efficient ways to improve the resolution of cross-border disputes via ADR? Are there any particular forms of ADR that are more suitable for cross-border disputes?

In our experience, ADR schemes are most effective – and compliance with ADR decisions is highest – when ADR decisions are enforceable at law in the member state of the ADR scheme. This is why our scheme is designed to be able to deal with complainants anywhere in the world – but only in relation to complaints against businesses which either have an establishment in the UK or against non-UK businesses which have joined our jurisdiction voluntarily and whose consumer contracts are made under UK law. For all other complaints, we believe it is more effective for consumers to be signposted to ADR schemes in the member states where ADR decisions are enforceable. This is one of the principles under which FIN-NET operates.

## **Funding**

(14) What is the most efficient way to fund an ADR scheme?

We believe that ADR schemes should be fully funded by industry, as our scheme is. The most efficient way to do this will depend on nature of the sector concerned and the political circumstances of the member state in question. For our scheme, this involves a parafiscal levy which all businesses under our jurisdiction pay (proportionate to the size of the business and the likelihood of complaints coming from that business's industry sub-sector). This levy covers about 20% of our costs. The remaining costs are recovered through case fees paid by the businesses against whom complaints are made. These are non-outcome related, and the first three cases per business per year are free (in order to ensure a proportionate impact upon smaller businesses). We believe that it would be both wrong and inefficient for consumers to fund our service, even partially (see below).

(15) How best to maintain independence, when the ADR scheme is totally or partially funded by the industry?

Although our scheme is fully funded by industry, feedback from stakeholders has consistently shown that this does not affect their perception of our independence. This independence is secured by our scheme complying both with the terms of Commission Recommendation 98/257/EC and with the criteria set down by the

British and Irish Ombudsman Association<sup>6</sup>. The latter criteria require certain standards to be met in order to guarantee the scheme's independence including, for example, independent procedures the appointment of ombudsmen.

(16) What should be the cost of ADR for consumers?

We believe that there should be no cost for consumers. Our experience suggests that requiring consumers to pay even a small refundable fee would deter many consumers – in particular vulnerable ones – from pursuing valid complaints. Furthermore, we are not convinced that consumer fees would deter vexatious complaints, as many such complaints go to the courts in spite of such fees.

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<sup>6</sup> See: <http://www.bioa.org.uk/criteria.php>