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Tools for changing banking culture: FCA are you listening?

Why the FCA's IRHP mass dispute resolution system has failed and what the FCA can do about it

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Key points

- The mass dispute resolution system that the Financial Conduct Authority (FCA) set up in 2013 for customers of banks who had been mis-sold swaps has closed amid much criticism. It is currently the subject of judicial review proceedings and the FCA's own internal review.
- This article takes the opportunity to suggest to the FCA a new mass redress system of general application that would rapidly establish a publicly accessible body of authority on how the FCA's Handbook rights and duties are to be applied in practice. Such a system would further the FCA's overriding objective in creating the Handbook rights: achieving culture change in banking.
- The suggested approach is modelled on the Employment Tribunal system, which was the forum within which the new statutory rights not to be unfairly dismissed and not to be discriminated on the grounds of sex or race were worked out, in real cases, from the 1960s onwards. In a very short while, that combination of new rights and a claimant-friendly forum had profoundly changed not just employment culture, but civil society as whole.

1. The legal underpinnings of banking culture

There is much debate at the moment about how to change banking culture for the better.[1] Not all the issues involved are legal. However, culture has its legal underpinnings. Investment banking culture has a perfectly respectable legal basis under English common law: *caveat emptor*. Under the common law, the purchaser of a financial product who regrets buying it normally only has two causes of action:

(i) misrepresentation of fact at common law (as supplemented by statute); and

(ii) negligent breach of a duty at common law to advise with care.

As long as a supplier of financial services and products does neither of those things, he escapes liability to the purchaser under the common law. Before attacking this legal basis as unethical, it is worth observing that the English common law is the commercial law of choice around the world because it is highly developed and therefore predictable. It is predictable because it is delivered consistently by a well-respected judiciary/body of

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1 See, for example, the work of the Banking Standards Board, which was voluntarily established by seven banks in May 2013 in the wake of the LIBOR scandal. It published its inaugural report in May 2014, which proposed establishing the Banking Standards Review Council, a body, paid for by banks, which would have responsibility for establishing and ensuring compliance with a voluntary code of practice for all bankers operating in the UK. See also New City Agenda, *A Report on the Culture of British Retail Banking*, 24 November 2014.

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arbitrators. These virtues of certainty are enhanced by the central place that freedom of contract occupies and, in particular, by the absence of a general duty of good faith in commercial dealings. It is the absence of a general duty of good faith that basically restricts the causes of action to the two above. None of those fundamentals is going to change: the common law ain't broke and there is no appetite to fix it.

However, it has long been recognized that the basic common law position is not suitable for all areas of the economy, where the weaker counter-party needs additional protection: ie consumer cases.[2] The Unfair Contract Terms Act 1977, the Unfair Terms in Consumer Contacts Regulations 1999 and now the Consumer Rights Act 2015 are just three examples of legislation which introduce concepts of fairness into certain sub-sectors of the economy in order to level the playing field in favour of the consumer. In those sub-sectors, business continues on terms acceptable to both supplier and consumer despite departure from the common law.

2. Two ways for the FCA to achieve those strategic objectives

The FCA has—like its predecessor regulators and professional bodies in other markets—supplemented the common law by creating obligations on those it regulates to abide by standards of behaviour that go beyond their common law obligations to the customers. In the FCA's case, these are found in its Handbook.

By creating professional duties on those it regulates, the FCA arrogates to itself the right to punish miscreants for dereliction of those duties—without the need for a customer to bring an action, prove breach and that it suffered loss. What such enforcement needs instead is the FCA to spot the misconduct and to have the capacity to institute timely disciplinary proceedings.

However, the regulator cannot be expected to see everything or act on everything. Regulators across the world recognize that enhanced private law rights can also be a useful second route for regulation 'by proxy': grant private law rights aimed at generating culture change, then sit back and watch private entities enforce them for you. So it is, for example, that Directive 2014/104/EU now requires that, by 27 December 2016, EU Member States must grant private law rights for breach and competition rules without the need for a prior finding by a competent competition authority. The theory is that the aggrieved party will police transgressions against its rights more assiduously than will the state.

And so, by what is now s 138D Financial Services and Markets Act 2000, the FCA has made some of the enhanced obligations in its Handbook enforceable as private law rights by certain types of person against those that the FCA regulates. Helpfully, the English Court of Appeal in *Green & Rowley v RBS* [2014] Bus LR 168 has confirmed that these Handbook/statutory rights are an entirely free-standing regime, discrete from common law rights of action. So the scene is set for the Courts to play their role in developing the

2 See the discussion in Gerard McMeel and John Virgo (eds), *McMeel and Virgo on Financial Advice and Financial Products* (3rd edn, Oxford 2014) 32–4 paras 1.67–1.71.

case law which substantiates the Handbook/statutory rights and embeds the desired culture in the industry.

3. The perpetual problem of party asymmetries

However—before we look eagerly for a new dawn in banking culture rising above our court system through empowered bank customers enjoying enhanced private law rights—it is worth noting a key characteristic of the relationship between bank and any retail customer, including small or medium enterprises (SMEs): a significant imbalance of information,[3] experience and resources in favour of the bank.

Imbalance between banks and SMEs at the point of sale gives rise to the common law causes of action described above. It is because those common law causes of action did not adequately protect the customer that the FCA has granted enhanced private law rights to the customer which the bank must comply with at the point of sale. So far so good.

At the point of dispute, however, the imbalance between banks and SMEs reasserts itself: the costs of litigation in time and resources fall much harder on SMEs than on banks. Few SMEs can afford to bring cases against banks. Some simply do not have the power, because at the point of dispute they are insolvent; the officeholder decides.

Where an SME does manage to bring a case, the asymmetries habitually manifest themselves by the bank defending to the action door of the court, draining the claimant of his resources, and then settling the case at the point of maximum exhaustion and uncertainty for its former customer. It is a well-recognized litigation tactic aimed in particular at preventing the creation of a legal precedent which might hurt the bank.[4]

Just as the common law is well respected as a commercial law of choice, the adversarial English Court system and the Bar that serves it are well respected as a Rolls Royce dispute resolution service. However, it is not a service many can afford unaided. Indeed, the most significant cost element of the English Court system—loser pays winner's costs, known as 'costs shifting'—is defended *precisely because* it deters a US-style, 'litigation-for-all' culture.

As a result, neither Parliament nor the FCA considered the English Courts as an effective way of rebalancing the playing field in favour of millions of customers it believes had been mis-sold products such as payment protection insurance (PPI), interest rate hedging products (IRHPs) and credit card protection insurance (CCP). Parliament therefore decided to empower the FCA to create a 'mass-redress system', which the FCA could deploy in appropriate circumstances and which would be effective in tilting the playing field in favour of the customers and away from the banks. In short, the FCA, like many before it, recognized that some dispute resolution journeys are more suitable for a bicycle than a Rolls Royce.

3 ibid 31f para 1.65.

4 See Havelock-Allen J, writing the Foreword to the third edition of *McMeel and Virgo* in September 2014: 'Gradually judgments which interpret [the Handbook] have begun to be reported. This has been a slow process since many of the financial institutions on the receiving end of claims have preferred to settle them than contest them in court . . . . To the best of my knowledge, only two claims for swaps sold since the millennium have been tried. The overwhelming majority have been settled as a consequence of the FCA Review.' See also *McMeel and Virgo* (n 2) 24 para 1.39.

4. The principal statutory vehicle available to the FCA: the consumer redress scheme

Parliament presented the FCA with a bicycle in s 404 Financial Services and Markets Act 2000 (FSMA2000, as amended principally by Financial Services Acts 2010 and 2012). This bestows on the FCA the power to set up a consumer redress scheme (CRS). In essence, this provision allows the FCA to require a firm or firms to review the sales of products they made to their customers and determine whether redress is payable to them for their own failure to comply with regulatory requirements.[5]

A lawyer will immediately see that the weakness of a CRS is that the offender is his own judge, jury and executioner. In judicial systems less robust than those we are accustomed to, that happy combination of roles is normally the privilege of the accuser and not the accused. Nevertheless, one can see that—where a widely-maintained complaint has been investigated by the FCA under its various inquisitorial powers[6] and found valid, with the result that determination of the right to and quantum of compensation is essentially an administrative matter—a CRS has a legitimate role in delivering redress to millions of dissatisfied customers. It also has a legitimate role in keeping that volume of technical disputes out of the Financial Ombudsman Service (FOS) and the Court system.

But perhaps in recognition of the inherent limitations of the CRS system, the FCA has adopted a practice of requiring banks and the FCA to ride in tandem: it normally orders banks to execute CRSs under s 404 while at the same time ordering under s 166 that 'skilled persons' appointed by the FCA ride alongside to keep an eye on things.

The s 166 skilled person power is, in effect, a general power to outsource the FCA's information-gathering and analytical roles to sub-contractors. It was perhaps conceived in recognition of the fact that the size of the markets would render the FCA incapable of monitoring them effectively in-house. By having the skilled persons pedalling alongside the banks, there is at least a reasonable expectation that the banks will arrive at the right destination, even if the banks would prefer to be freewheeling in the other direction.

This 'tandem' approach seems to have been used reasonably satisfactorily on a number of occasions in 2014 against payday lenders.[7] These schemes were deployed in respect of matters of fairly narrow scope, despite the large numbers who were granted redress.

5. The FCA's ad hoc mass redress system for IRPHs mis-sold to SMEs

In contrast, the complaints that banks had mis-sold IRHPs to SMEs were a matter of very broad scope indeed: in March 2013, the FSA required 11 banks to review the sale of some 40,000 of—presumably over the counter (OTC)—swaps from 1 December 2001.[8]

5 Guidance on their operation is provided by the FCA in its Guidance Note GN10 (2010).

6 See FSMA2000 pt XI, in particular ss 167–168.

7 Wonga Group Ltd, Ariste Holding Ltd and CFO Lending Ltd. The first s 404 CRS, instituted by the FSA in respect of the Arch Cru Fund on 1 April 2013, had no accompanying oversight by a skilled person under s 166.

8 *Interest Rate Hedging Products Pilot Findings*, FSA, March 2013.

There were two principal factors which meant that IRHP disputes between banks and SMEs were not suited to the s 404 CRS. First, on the basis of what appears now to be an outdated, pre-Lehman approach, CRSs under s 404 can effectively only be set up to vindicate the Handbook rights of private individuals.[9] The s 404 power, then, did not meet the need, as sole practitioners were a tiny proportion of SME trading entities that had been sold swaps.[10] Secondly, the disputes generally hinge both upon hotly contested factual evidence about what the salesman said to a customer at the point of sale, and upon expert evidence about (i) whether a product was suitable for an SME, (ii) whether it was adequately explained to the SME and, if not, (iii) what loss the SME has suffered. In short, IRHP disputes are the stuff of full-blown High Court litigation.

Mass County and High Court litigation of IRHP disputes is the last thing the FCA wanted. But the FCA's problem was that it did not have a statutory CRS vehicle suitable for the IRHP journey. So, in January 2013, the FSA (as it then was) did the best it could: it commandeered s 166. Follow that swap.

It would be unfair to say it looked like the banks were being chased by the Keystone Cops. Nevertheless, on 10 March 2015, the Treasury Committee published a report which was critical of the FCA's IRHP redress scheme.[11] On 24 April 2015 in the case of *R (on the Application of Holmcroft Properties Ltd) v KPMG LLP* the Administrative Court granted permission for a full hearing on the issue of whether it is reasonable for the 'skilled person' to refuse consequential losses to a successful claimant under the scheme.[12] It is said to be standard practice under the scheme to do so. On 17 July 2015, the chief executive who designed the scheme resigned. On 13 October 2015, the FCA's interim chief executive, when responding to the Treasury Committee's March report, accepted that it should initiate its own review into whether there was a system inherently flawed.[13]

9 Of the threshold criteria to the FCA instituting a s 404 CRS, the most restrictive is at (1)(b): it must appear to the FCA that 'consumers have suffered (or may suffer) loss or damage in respect of which, if they brought legal proceedings [in respect of a widespread or regular failure by a regulated firm] a remedy or relief would be available in the proceedings.' It is so restrictive because the Financial Services and Markets Act 2000 (Rights of Action) regs 2001 reg 3(1) restricts legal rights of action based on s 138D FSMA2000 to private individuals and what must be a very modest number of corporate entities which do not carry on a business. Most SMEs are, of course, companies that carry on businesses.

10 For the PPI consumer redress scheme, the FSA simply stepped outside s 404, freeing it from the threshold criteria entirely. It issued Policy Statement 10/12 in August 2010, which instructed banks on how to approach compensation of dissatisfied customers; it then appended as Appendix 3 to the Disputes Resolution Sourcebook in the Handbook. That Policy Statement treated breaches of high-level Principles as giving rise to a right to compensation despite the fact that their breach did not give rise to private law rights. It was this decision that was the principal ground for the unsuccessful application for judicial review by the British Bankers' Association: *British Bankers Association v Financial Services Authority and Financial Ombudsman Service* [2011] EWHC 999 (Admin), Ouseley J.

11 The Treasury Committee's 11th Report 2014–2015: Conduct and Competition in SME Lending, 10 March 2013, ch 4.

12 The full hearing was heard in the Administrative Court over three days from 25 January 2016 before Elias LJ and Mitting J. Judgement is reserved.

13 See paras 3.4–3.8 of the FCA's response dated to the 11th Report of the Treasury Committee 2014–2015, 'Conduct and Competition in SME Lending of June 2015', reported in *The Times* on 13 October 2015: 'Victims Win Fight for Review of Interest Rates Swap Compensation'.

6. The key problems with the FCA's ad hoc mass IRHP redress system

The FCA had approached the IRHP redress problem this way. It secured a voluntary agreement with nine big banks that—irrespective of the absence of a s 404 CRS—they would (i) investigate their own mis-selling of swaps to their customers, (ii) determine whether they had mis-sold them and, if they had, (iii) assess the amount of compensation they themselves would pay to those customers. To ensure fairness/compliance, those banks would subject their handling of this process to oversight by 'skilled persons' under s 166—who were in turn overseen by the FCA.

The voluntary nature of this ad hoc mass redress system meant that its net could be cast more widely than a s 404 CRS. It also meant that the disputes were—at least in the first instance—kept out of the FOS and the Court system. To the accountants who seemed to have designed and overseen the system, this solution appeared to be the holy grail of dispute resolution: a simple and inexpensive way of delivering justice to millions of consumers at the expense of the bank.

A little more experience in traditional dispute resolution might have alerted them to some of the key flaws. First, it was replete with conflicts of interest: the eight participating banks were the principal investigator and judge in the cause against them; the skilled persons who oversaw them were the banks' best clients/suppliers, the big four accountancy firms. The relationships were too cosy for public confidence.

Secondly, the process was inquisitorial, technical and administrative: the complainant had limited access to information and opportunity to submit evidence or to make submissions. A public used to an adversarial system felt the process did not deliver justice because, in particular, the contested evidence about who said what to whom at the point of sale was not the subject of challenge. They wanted their 'day in court'.

Thirdly, the tight threshold criteria[14] for eligibility to enter the scheme and some of the outcomes—in particular the practice of excluding consequential losses from awards of compensation—suggested that fears that the relationship between the FCA, the banks and skilled persons was just too cosy were indeed well founded. Permission for judicial review followed, confidence in the IRHP redress process drained away and the scheme closed.

It is tolerably clear already that the FCA's creative use of s 166 to help create a mass dispute resolution system suffered from the limitations inherent in s 166. That section provides the FCA with a device it can use to oversee what the banks are doing. When deploying s 166, the FCA will always have to rely on the banks to do the thing the skilled persons oversee. If what the FCA asks the banks to do under s 166 is to run a dispute resolution system to punish their own misdeeds, a system run by the banks is unlikely to win the confidence of the public in anything but the simplest of disputes. The public has

14 The FCA introduced complex qualification criteria, which in outline were: (i) the IRHP had to be a stand-alone sold after 1 December 2001; (ii) for those sold before 31 October 2007, the consumer had to be a 'private customer'; (iii) for those sold after 31 October 2007, the consumer had to be a 'retail client'; (iv) the consumer could not be 'sophisticated', which was determined by turnover, balance sheet and payroll and (v) the notional value of the swap had to be less than £10m.

been told that self-regulation by banks does not work. But to consumers, self-regulation is not far off what the IRHP redress system looked like.

7. Where the FCA is today on effecting culture change in markets

As the FCA initiates is review of the s 166 IRHP scheme, now is a good moment for it to take stock. As a matter of policy, the FCA wishes to take a more proactive approach to regulation so as to move the markets from *caveat emptor* to one in which banks have more of a sense of responsibility to their customers: ie change from sales to relationship cultures.

The FCA has taken the decision that the general *caveat emptor* common law rule does not protect the consumer of financial products and services adequately. It has therefore granted private law rights to consumers in the Handbook, which effectively push firms from avoiding advising or misrepresenting—as they could do under the common law—to proactively gathering information about the client and giving him advice.

Some would say—and the FCA's ad hoc s 166 CRS for IRHPs would suggest—that the time has come[15] to extend these private law rights from private persons[16] to retail clients,[17] classification of which includes corporates and SMEs. Be that as it may, the world waits to see how such Handbook rights as now exist will develop through the cases and how the cases will effect change in the culture of the markets.

Meanwhile, the FCA has been busy deploying its numerous 'macro' tools directly against banks to create cultural change, with some degree of success: LIBOR prosecutions by the Serious Fraud Office (SFO)[18] have been a powerful indication of a new beginning. Market analyses and thematic reviews have focused the markets' attention on delivering customer value and service—even if sometimes, such as in the case of the life insurance review,[19] they too have attracted criticism for the way they have been handled. New City Agenda[20] credits LIBOR in particular with bringing the banks to the 'culture change' table. It was after that manipulation scandal that the banks funded the Banking Standards Board (BSB) which, in turn, went on to create the Banking Standards Review Council (BSRC). So far so good.

The CRS that exists in s 404 is a useful tool where a thematic review, market analysis or investigation has determined that a product breaches some of the private law Handbook duties to private individuals and the remaining task is to cause the banks to deliver

15 In November 2015 the FCA issued Discussion Paper DP/15/7: 'Our approach to SMEs as users of financial services'. That paper seeks responses to questions which include whether the FCA should extend some of the rights that private persons enjoy under the Handbook to corporate SMEs (see esp. Chpt 4, Q2 and Q3).

16 reg 3 Financial Services and Markets Act 2000 (Rights of Action) Regulations 2001.

17 Conduct of Business Sourcebook COBS 3: Client Classification, a classicisation derived from MIFID 1, which came into force in August 2007 and implemented in the UK on 31 October 2007.

18 The first, Tom Hayes, charged in June 2013, convicted and, on 3 August 2015, sentenced to a 14-year term of imprisonment. On 21 December 2015 the Court of Appeal reduced his sentence to 11 years. Other benchmark investigations and prosecutions are just beginning to gather pace: FX, LBMA Gold Price and ISDAFIX.

19 *Report of the Inquiry into the events of 27/28 March 2014 relating to the press briefing of information in the Financial Conduct Authority's 2014/15 Business Plan*, Simon Davis, Clifford Chance LLP, 20 November 2014.

20 A think tank concerned with the financial services industry, supported by Prudential, Berenberg UK, HSBC, The London Stock Exchange Group and the City of London Corporation.

predetermined forms of redress to consumers. But the s 404 CRS, being a private process, creates little additional impetus towards developing a new culture. And neither it nor its accompanying s 166 oversight tool is suitable for resolution of disputes where arguments over breach, causation and loss are substantial. As things stand, those disputes are to be resolved through the FOS or the Courts.

The FOS is a well-established 'evaluative mediation' tool available to the FCA. It is suitable for ad hoc, smaller consumer complaints: its jurisdiction is limited to £150,000[21] and its tight eligibility criteria[22] exclude most SMEs. Its mechanisms begin with facilitated settlement through adjudicators and end with 'determination' by an ombudsman (effectively an expert third party's suggestion of a reasonable settlement, which is binding on the parties only if the consumer accepts the suggestion[23]). These characteristics mean it is not suitable for an IRHP mass redress system. Nor is the FOS a means of rolling out the culture change through working out the Handbook rights in the cases, because the vast majority of cases settle without a 'determination'.[24]

The Courts, meanwhile, created a Financial List on 1 October 2015, with specialist judges who will determine disputes over complex financial products valued over £50m, which require particular expertise or which raise issues of general importance to financial markets.[25] The Financial List benefits from special Civil Procedure Rules (CPR),[26] which include a predetermination regime in which costs shifting has been excluded.[27] The idea is to encourage high-quality determination of disputes with significance to markets. These disputes are, of course, not normally the disputes of retail clients, let alone private individuals.

Outside the confines of that rarefied List, Handbook claims proceed through the general lists of the County Courts—or perhaps the High Court—in accordance with normal CPR. Is this where the FCA wants its Handbook disputes to be? How effective will those Courts be in working out the Handbook rights through case law and in helping the FCA deliver rapid cultural change to markets? Is there a better way of achieving that goal? Can the FCA think of a historical precedent for a robust, specialist mass dispute resolution system which *has* delivered rapid and effective culture change?

8. A successful precedent for a mass dispute resolution system

This author, for one, is struck by a parallel between the financial services market in the 2010s and the employment market in the 1960s.

21 DISP 3.7.4R1/01/2012. Whether this limit on the FOS's jurisdiction should remain is the subject of consultation in the FCA's Discussion Paper DP 15/7 Chpt 5 Q5.

22 DISP 2.7. Whether these limitations on the FOS's jurisdiction should remain are the subject of consultation in the FCA's Discussion Paper DP 15/7 Chpt 5 Q4.

23 DISP 3.6.6R1/04/2013.

24 See the FOS annual review for 2013–2014: 2,357,374 enquiries or complaints; 51,267 new cases; 487,749 cases resolved by adjudicators; 3,129 cases resolved by ombudsmen's 'determinations'.

25 Following the lead of P.R.I.M.E. Finance, the international arbitral institution and panel of experts established in January 2012, which, announced on 9 December 2015, is to be administered by the Permanent Court of Arbitration in The Hague.

26 CPR 63A, plus the Practice Direction at CPRPD 63AA, together with the Financial List Guide.

27 The Financial Markets Test Case Scheme at para 9 of the Guide and CPRPD 51M.

By the 1960s, it had begun to be accepted that the common law did not go far enough to protect workers. The imbalance of negotiating power between employer and employee at the time of contracting meant that notice periods were short. A common law action for wrongful dismissal only compensated the employee for loss during his notice period. On dismissal, therefore, it was hardly worth suing the employer. Even if it was, a dismissed employee could rarely afford to pay lawyers to fight his case when he had just lost his job. In particular, he could not assume the risk of paying his ex-employer's costs if they lost their case in the common law courts.

As a result, good behaviour by employers towards employees was effectively voluntary. In addition, hostility to increased levels of immigration meant that bad behaviour in the workplace by employers and between employees went without sanction. By the 1960s, this status quo became politically unacceptable.

In response, Parliament granted a wave of new substantive rights to employees in the 1960s[28] and 1970s:[29] principally the rights not to be unfairly dismissed and not to be discriminated against on grounds or race or sex. Parliament entrusted to a specialist statutory tribunals system the task of determining the application of those rights to the facts of individual cases. That system created its own body of case law at first instance and appellate level. It reconnected with the common law courts at Court of Appeal level.

When what are now called the Employment Tribunals[30] were given that jurisdiction, they had before them a central task: to work out, case by case, what it meant to dismiss an employee unfairly. Later, they were asked to work out, case by painful case, what it meant to treat someone less favourably on grounds of race, sex or other proscribed ground. Within 30 years, not only had the legal principles been worked out through the cases, they had transformed employment culture.

It is no over-statement to say that the statutory system developed from the 1960s onwards was part of a legislative programme that aimed to change the way civil society operated.[31] It has been very effective. To test is success, one only needs to remind oneself of the archaic terms that the common law courts applied to employer and employee,

28 The Contracts of Employment Act 1963 and the Redundancy Payments Act 1965. In 1965, Lord Donovan was asked to chair the Royal Commission on Trade Unions and Employers' Associations. The Commission reported in 1968. The report was largely concerned with the right framework industrial action. However, one of the report's recommendations was to create a statutory right not to be unfairly dismissed (Donovan Report, vol 1 ch IX, 141–54). It proposed this and other employment rights should be determined exclusively by 'Labour Tribunals' (Donovan Report, vol 1, ch X, 155–59). In making that suggestion, it noted that many unofficial strikes were called due to disputes about individual offers of employment, suspensions or dismissals—no doubt because of the lack of redress the Courts offered to workers (Donovan Report, vol 1, 143, para 528).

29 The Equal Pay Act 1970 introduced the right to equal pay between sexes, the Industrial Relations Act 1971 introduced the right not to be unfairly dismissed, and the Sex Discrimination Act 1975 and the Race Relations Act 1976 prohibited discrimination on those eponymous proscribed grounds.

30 Known as Industrial Tribunals until 1 August 1998. They trace their history back through the National Industrial Relations Court (1971–1974) to the Industrial Appeal Tribunals that had originally been set up under s 12 of the Industrial Training Act 1964 to determine complaints that an employer had been levied with the cost of a training programme by the Industrial Training Board. As new employment rights for private individuals were created, determination of their application to cases was handed to these specialist tribunals.

31 The terms of reference of the Donovan Report was as follows: 'to consider relations between managements and employees and the role of trade unions and employers' associations in promoting the interests of their members and in accelerating the social and economic advance of the nation . . . ' (Donovan Report, vol 1, 1).

respectively, at that time[32]—master and servant[33]—or indeed the kind of discrimination which was then overt and commonplace in society, and which today is considered a secular sin.

The FCA has created a series of private law duties on banks, the essence of which is to treat the consumer 'fairly'[34] and 'to provide appropriate information . . . to [allow the client to] take investment decisions on an informed basis'.[35] It stands where Parliament stood in the 1960s: in need of the right forum for those duties to be worked out in practice through the cases—and thereby achieve cultural change in retail banking.[36] The Employment Tribunals provide a successful historical precedent for such a programme.

9. How the Employment Tribunals system effected cultural change

What was it about Employment Tribunals that allowed them to achieve such success in creating change in the civic and employment cultures? This author sees four key characteristics which gave rise to their success.

First, the costs-free regime. This meant that employees could afford to bring cases and to fight them to judgment. They did so in large numbers. Employees were therefore granted access to justice they were previously denied. But even more importantly for cultural change, it meant that a body of case law was able to develop very quickly, which worked out what unfairness or less favourable treatment is.[37]

Secondly, specialization. The tribunals system is operated by specialists: lawyers in the role of Employment Judges and advocates before them at the bar. On the wings of the tribunal are market specialists: one member from 'business' and the other from 'labour'—this constitution even at the level of the Employment Appeals Tribunal. This balance of legal expertise and employment experience gives the system a sense of 'buy in' from society, and therefore, a sense of ownership by the practitioners, among whom there is the confidence to develop both the law and the culture.

32 And to this day, perhaps. Although statistics must be approached with extreme caution, a free text search on Westlaw under 'master and servant' in the last 20 years yields 19 cases in the Supreme Court/House of Lords, 57 cases in the Court of Appeal and 84 in the High Court. There are only 33 uses of the phrase in the Employment Appeals Tribunal over the same period, most with some kind of 'scare' quotes. The last reported case (though such cases are rarely reported) in the Employment Tribunals was 20 years ago. The caseload and subject matter of those various jurisdictions of course influence these statistics.

33 A phrase that found legislative expression in the Master and Servant Acts of 1747 onwards: see S Deakin, 'The Contract of Employment: A Study in Legal Evolution' (2001) Centre for Business Research esp 19ff.

34 COBS 2.1.1(1) of the Handbook. Also at COBS 2.(1) 'honestly . . . and professionally'.

35 COBS 2.2.1(1) of the Handbook 'the duty is to provide 'appropriate information in a comprehensible form . . . so the client is reasonably able to understand the nature of the risks of the service . . . that is being offered, and consequently, to take investment decisions on an informed basis'.

36 Cases such as *Saville & another v Central Capital Limited* [2014] CTLC 97 show how similar Handbook cases can be to discrimination cases: they involve extremely detailed textual analysis of the Rules and Guidance (eg paras 23–30), tightly nuanced counter-factual arguments on causation (eg paras 31–36). The incidence of the burden of proof is both controversial and extremely important (eg paras 49 and 66).

37 The Hon Mr Justice Browne-Wilkinson 'The Role of the Employment Appeal Tribunal in the 1980s' (1982) 11 Indus L J 69, 70: as a result of the EAT's work '. . . in a short time a very large body of so called ''law'' built up, laying down what was to be treated as fair industrial conduct'.

Thirdly, an inquisitorial element. In contrast to common law courts, Employment Tribunals operate a mixture of an adversarial and an inquisitorial system.[38] The adversarial system gives the parties a sense of their day in court and drives up the quality of tribunal decision-making. The inquisitorial element adds value at both ends of the process.

At one end, an inquisitorial element is necessary when employees are unrepresented, so the tribunal ensures the right issues are aired. At the other end, the inquisitorial element means specialized tribunals can run with the issues that interest them in the light of their employment experience and the development of the law. It avoids the need to pre-identify all factual or legal issues in statements of case and in particular it reduces the need to adduce expert evidence in advance of a hearing. It also helps tribunals interpret expert evidence. Market practice issues can be explored more flexibly and at a reduced cost. Issues are less likely to be missed because a party did not raise them early enough.

Fourthly, the Employment Tribunals' dispute resolution function was a central mechanism in Parliament's culture-building programme—but not the only one. It is a regular feature of employment-related legislation that stakeholder bodies are given a consultative role—and are even created for that purpose where necessary. The BSB and the BRSC, therefore, have come into existence at an appropriate moment.

The aim of such consultation was to create statutory codes of practice[39] which Employment Tribunals take into account when determining cases, as do employers when managing employees. Those codes are aimed at establishing norms of behaviour arrived at by experts from all sides through dialogue. They are effective in shaping culture, as breach of the code is evidence in support of breach of a legal duty.

The FCA has already adopted a system of 'evidentially significant' breaches and guidance in its Handbook to supplement its rules.[40] The point about such consultation around a dispute resolution system, however, is that it achieves broader-based acceptance for the guidance as a result of it being overtly the product of all stakeholders rather than being imposed by a hostile regulator.

Moreover, members of a specialist tribunal system are more likely to engage readily in a broader culture-building than judges of the County or High Courts: such common law judges would tend to view such consultation as impinging on their key duty of independence from the legislature. However, when they and their practitioner colleagues are appointed under a statutory regime, they are not to be so inhibited; then, they can

38 The Employment Tribunals (Constitution and Rules of Procedure) Regulations 1993 sch 1, r 9(1), now superseded by the Employment Tribunals (Constitution and Rules of Procedure) 2013 sch 1, r 41.

39 See, eg ACAS Code of Practice 1 Disciplinary and Grievance Procedures (2009) under authority granted by s 199 Trade Unions and Labour Relations Act 1992 (to which ACAS added a Guide, the latest version of which is from 2014, which does not have statutory force); the Disability Discrimination Act 1995 Code of Practice of 2008 under s 14 of that Act, issued by the Equality and Human Rights Commission (EHRC), along with its Code of Practice on Equal Pay (2011 edition) now under Equality Act 2010 Codes of Practice (services, Public Functions and Associations, Employment and Equal Pay) Order 2011. The EHRC has extensive powers of inquiry and investigation listed at paras 3–6 of that Code of Practice, not dissimilar to the FCA's. The EHRC's Code of Practice on Employment (2011) under the same Order covers all aspects of discrimination in employment. There are numerous others.

40 See FCA's *Readers' Guide: An Introduction to the Handbook* (2015) ch 5.

make a valuable contribution to the development of norms as a result of their direct experience of resolving disputes.

10. Financial Services Tribunals

It appears to this author, therefore, that today a gap exists below the level of the High Court's specialist Financial List,[41] and above the level of s 404 schemes or the FOS. The FCA tried to extend its reach into that space when it created its ad hoc redress scheme, overseen by s 166 skilled persons, which would keep IRHP disputes out of the County Courts and general lists of the High Court. The FCA identified the right space to occupy with a 'mass dispute resolution system' but has not yet found the right system with which to occupy it. The FCA should not lose heart, but look at different ways of filling that gap with an alternative redress system. Such an alternative will need to possess the following characteristics: ie it must

(i) enjoy the confidence of the public as a robust mechanism for resolution of disputes too complex for s 404 CRSs;

(ii) provide for easy, low-cost access to justice for claimants[42] (who will normally be SMEs or private individuals suffering from an asymmetry of information, experience and resources as against a bank);

(iii) deliver substantive rights to banks' customers which go beyond the common law remedies available in the Courts (to include the private law rights created in consumers' favour to be found in the Handbook); and perhaps most importantly

(iv) be capable of making a significant contribution to delivering an overall change in retail financial market culture (ie from *caveat emptor* towards responsibility and accountability to consumers).

A Financial Services Tribunals (FSTs) system modelled on Employment Tribunals would have those characteristics. Such a system should not be difficult to create: there already exists in the Tribunals, Courts and Enforcement Act 2007 a widely used framework for operating tribunals systems.[43] In fact, Employment Tribunals predate this statute and so enjoy their own statutory platform, but that makes little difference.

If it proved difficult to establish such a scheme in short order, the FCA might simply design a suitable set of arbitration rules under the Arbitration Act 1996. It could persuade

41 The new High Court cause list, before judges specialised at trying cases concerning complex financial products requiring particular financial expertise or valued over £50m or raising issues of general importance to financial markets. It includes a Financial Markets Test Case Scheme, which excludes costs shifting.

42 Employment Tribunals and the Employment Appeals Tribunal operate no costs shifting absent unreasonable behaviour. There are numerous other solutions which protect claimants from the full effect of costs shifting. Since the Jackson reforms were introduced on 1 April 2013, the common law courts now operate a system of 'qualified one-way costs shifting', under which personal injury claimants (effectively suing well-funded insurers) are protected from costs shifting unless their behaviour is in various ways unreasonable. The Intellectual Property and Enterprise Court is designed to allow small businesses to protect their IP, often from established competitors; it caps costs shifting at £50,000. The parallel with SMEs suing banks is clear. Other jurisdictions listed at CPR45 also cap costs shifting.

43 The Upper Tribunal (Tax and Chancery Chamber), which already hears appeals against appeals from regulatory and disciplinary decisions of the FCA, is constituted under the 2007 Act.

the banks that it is a good idea to offer those dispute resolution terms to customers by way of submission agreement instead of relying on the dispute resolution terms in the standard terms and conditions they forced on the customer at the point of sale. How either of these two first-instance solutions might look in practice and the respective advantages of each is a matter for another article.

The essence of any such tribunals system, however, would be specialist[44] Financial Services Judges drawn in large part from the common law Bar and judiciary, plus a wing member drawn from the banking sector and a wing member from the small business sector. Each would be able to bring his expertise to the resolution of SME disputes against banks.

11. Financial Services Appeals Tribunal

A temporary solution under the Arbitration Act 1996 would have the disadvantage of the very limited right of appeal to the High Court permitted under s 69.[45] On any view that threshold would be an impediment to building a body of authority guiding tribunals and market participants on how to apply Handbook rights.

The Employment Tribunals system stands at the other end of the spectrum: for it a specialist Appeals Tribunal was created—as an additional, 'third' appeal court to the existing two from first-instance litigation decisions: the Court of Appeal and Supreme Court. In commercial arbitration, there is widespread support for a very limited right of appeal; indeed, England and Wales is exceptional in granting any right of appeal at all in international commercial arbitration. Would a Financial Services Appeal Tribunals system add value to a tribunals system, or would it just add cost?

In 1982, Mr Justice Browne-Wilkinson felt obliged to defend the work of the recently established Employment Appeals Tribunal, of which he was then President, in response to certain restrictive decisions[46] of the Court of Appeal. Those decisions had reminded the Appeals Tribunal that its jurisdiction was limited to correcting errors of law, and of the dangers of issuing guidance to the proper factfinders in the Industrial Tribunals.

In defending the practice the Appeals Tribunals had adopted, he described the unique nature of the Employment Tribunals' and Appeal Tribunal's work in contradistinction to the common law courts. The article[47] repays reading in full, but the essence of what he said is this:

> What is needed [from the Employment Appeals Tribunal] is to build up, and from time to time modify, general principles of fair industrial conduct by reference to which Industrial Tribunals should approach the facts of each case . . . .[48]

44 See Lord Nicholls writing the Foreword to the second edition of *McMeel and Virgo* in May 2006: 'To many lawyers the law relating to financial markets is still largely unexplored territory.' In the Preface to the third edition the authors state certain English cases '. . . throw up surprising results, which betray judicial unfamiliarity with the legal and regulatory background in this field'.

45 The threshold is: the appeal point must substantially affect the rights of a party, the point must be one the tribunal was asked to determine, and the decision of the tribunal must be obviously wrong or the point one of general public importance. The challenge procedure under s 68, on the other hand, although more widely used, would not contribute to the case law on Handbook rights because it is limited primarily to irregularity of procedure in the arbitration.

46 *Retarded Children's Aid Society v Day* [1978] ICR 437 and *Bailey v BP Oil (Kent Refinery) Ltd* [1980] ICR 642, 648.

47 'The Role of the Employment Appeal Tribunal in the 1980s', see n 37 above, first given as a talk to the Industrial Law Society on 9 March 1982.

48 ibid 73. At 74, he continued:

> In my view, the Appeal Tribunal, if it still has jurisdiction to do so, has an important role to play in declaring uniform principles of good industrial practice by reference to which employers and employees can regulate their conduct . . . .[49]
>
> I do not think that conventional law can be applied lock, stock and barrel to industrial relations cases . . . . There are therefore two sets of principle to applicable to these cases: the principles of strict law (in a lawyer's sense) and the principles of good industrial practice . . . .[50]
>
> . . . it should be made quite clear that the Appeal Tribunal is not laying down rules of law, departure from which by an Industrial Tribunal automatically involves an error of law . . . statements of industrial practice should not be treated as principles of law which can only be changed by being overruled by a higher court or by a statute. Industrial relations practices change with circumstances and any principles laid down must change with them: there is no room for the doctrine of binding precedent in industrial relations practice.
>
> I would like to end by suggesting that, only if it is accepted by traditional lawyers that these and other special features have to be taken into account in dealing with industrial relations cases, will the law ever have an effective role to play in labour relations . . . . It would be sad if the experiment [of establishing norms of good industrial practice through a specialist Industrial Tribunals and Appeals Tribunal system] were to be aborted by the over-stringent application to this new field of traditional legal thinking.[51]

In the 1980s, therefore, it was necessary to make a case from scratch that the Employment Appeals Tribunal had to be more than just an appellate court of law to achieve its objective of establishing good industrial practice. In the 2010s, we have the benefit of Mr Justice Browne-Wilkinson's lucid arguments, and the luxury of needing only to substitute 'good banking practice' for the phrase 'good industrial practice' to have a complete argument made for a specialist tribunals system—distinct from the common law courts—to help the FCA achieve its work of delivering culture change.

12. Making the banks pay—funding Financial Services Tribunals

The time is, of course, ripe for the FCA to consider establishing FSTs because of the review it is beginning into the difficulties it has experienced with its ad hoc IRHP redress scheme. But it is also ripe because of developments in the common law courts.

The most recent in a short series of Lord Chancellors who are not lawyers has decided that the judicial system to finance itself by levying fees on claimants from March 2015. This year the first wave of fee increases is capped at £10,000. That is about a 600% increase. It is a fee levied simply for issuing a claim—as if access to justice in our common law courts were the same thing as resolving a dispute between multi-nationals by

> In the context of industrial relations, the answer to the question 'was it fair' often depends on knowing and understanding what is regarded as good industrial practice in industry and commerce. It is for that reason, amongst others, that the lay members sit on Industrial Tribunals so as to form an industrial jury . . . This is, I think, a unique feature of Industrial Tribunals. Unlike any other judicial body, the are making the crucial judgment —was it fair'— not on the basis solely of the views of the ordinary man in the street, but in part on the basis of principles of fair industrial behaviour which are unknown to lawyers and others without experience in that field . . . '.

49 ibid 75.
50 ibid 76.
51 ibid 77.

international arbitration under ICC rules. In July 2015, the Lord Chancellor began consultation on increasing that maximum to £20,000.

In short, the Lord Chancellor has tilted the playing field further in the direction of banks and away from banks' customers: it is the claimants/customers who will now be funding the defendants/banks through the common law courts. So the Lord Chancellor has magnified the problem of asymmetries between parties to the point where the common law courts are simply not the place where David can take on Goliath. If the common law courts were not the right place for the resolution of IRHP disputes between customer and bank in 2013, they are less so in 2016. If evidence were needed for this self-evident proposition, one only needs to look at the effect that increasing fees in the Employment Tribunals in July 2013 has had: there has been a 70% drop[52] in claims in that forum.

Unlike the Lord Chancellor, the FCA clearly had the problem of party asymmetry in mind when designing its ad hoc s 166 CRS: under s 166 the banks pay for the process. It is not cheap. In 2012–2013, the s 166 oversight of the IRHP redress scheme that they themselves were administering cost banks £141.5m.[53] By contrast, the Employment Tribunal system cost the Ministry of Justice about £80m to run per year.[54]

The FCA would have the political mood of the country on its side if it wished to carry the s 166 funding approach over into FSTs. The system could be financed by a levy on the banks, so there is no burden on the taxpayer and no fees would be payable by claimants. The FCA would also be assisting the Lord Chancellor in his thrift by taking a large and growing slice of the common law courts' workload out of the Ministry of Justice's budget, so it might make friends there. Indeed, the mood of the country is such that the banks would have difficulty resisting a proposal from the FCA that the banks should finance a legal aid fund for SME claimants before the FSTs. At that point, the FCA might experience morphing from everybody's whipping boy into popular hero.

13. Conclusion and postscript

The world finally agrees that banking has a culture problem, but no one yet seems to know what to do about it. And it is at just this moment that the FCA has decided it does not even want to know what to do about it: on 31 December 2015—a good day to bury bad news—it dropped its thematic review of the culture in banking.[55]

So to fill the policy vacuum, it is now time for all stakeholders—the FCA, Ministry of Justice, the Treasury and the bodies around those decision makers—to study a successful driver of culture change from the past: the employment law revolution of the 1960s,

52 Chartered Institute of Personnel and Development press release: 'CIPD research reveals employers are divided on employment tribunal fees as claims drop by 70%', 17 March 2015 <https://www.cipd.co.uk/pressoffice/press-releases/tribunalfees-research-170315.aspx>; see also, eg 'Employment Tribunal Cases Drop by 72%', *HR Magazine*, 17 September 2015 <http://www.hrmagazine.co.uk/article-details/employment-tribunal-cases-drop>.

53 Letter from FCA Chief Executive to Chairman of the Treasury Committee dated 7 July 2014.

54 Department for Business Innovation and Skills and the Tribunals Service, 'Resolving Workplace Disputes: A Consultation', January 2011, 49 fn 45.

55 'Banking Culture Enquiry Shelved by Regulator FCA' *BBC News*, 31 December 2015 <http://www.bbc.co.uk/news/uk-35204010>.

which took us from the old world of master and servant to the modern one of unfair dismissal and anti-discrimination.

That new world came about through giving employees a cheap and easy way to enforce their new rights outside the common law courts: the Employment Tribunals. The FCA has already given bank customers new rights in its Handbook—what it should be doing now is persuading the MOJ and the Treasury to create Financial Services Tribunals where customers can afford to hold banks to account.

The moment has arrived for the FCA to establish a dispute resolution system that will enable consumers of financial products to leverage the exceptional quality of the English judiciary to start the process of culture change in banks—just as Employment Tribunals enabled workers to leverage judicial and industry expertise in the 1960s.