



FOS jurisdiction
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As we reported in our previous [blog post](#) in November 2018, from 1 April 2019 the jurisdiction of the FOS has extended to include a new category of complainants. Prior to this date, only individual consumers and micro-enterprises (i.e. SMEs with fewer than 10 employees and an annual turnover or balance sheet total of less than €2m) could refer disputes to the FOS. Now, SMEs with an annual turnover below £6.5m and with a headcount of fewer than 50 employees or a balance sheet total of less than £5m will be able to use the FOS (as well as charities with income up to £6.5m, trusts with net assets up to £5m and personal guarantors of loans to businesses in which they are involved). Further to the FCA's [policy statement PS18/21](#) published in October 2018, the [final rules](#) were published in December 2018 and will appear in the FCA's Dispute Resolution sourcebook (DISP).

According to data in the [FOS Strategic Plans and Budget 2019-20](#), the extension will bring approximately 210,000 SMEs within scope of the FOS resulting in an additional 1,300 complaints each year. The FOS has created a ring-fenced, specialist unit to handle complaints from SMEs which will include a dedicated team of SME investigators and ombudsmen with specialist knowledge and skills, who will have access to additional expertise and technical advice (e.g. forensic accountants or experts on novel or complex financial products and services) and a dedicated microsite and phoneline for SME complainants.

Why extend the FOS's jurisdiction?

Stories of banking misconduct in the SME market in recent years, including misselling of interest rate hedging products and mistreatment of distressed SMEs by banks' business support units, was a key driver behind the need for a free, independent, dispute resolution service. Based on research undertaken by the FCA, SMEs of the size which now qualify to use the FOS appear to lack access to financial management and legal expertise and are therefore likely to struggle to resolve disputes with financial services firms without recourse to the courts, the cost of which can be prohibitive. Although their characteristics are more akin to consumers than large commercial businesses, SMEs cannot bring a breach of statutory duty claim under s138 FSMA based on a breach of FCA Rules – and, as most commercial lending (apart from lending under £25,000 to sole traders/small partnerships) falls outside the regulatory perimeter, the FCA cannot take regulatory action against any financial services firm which mistreats an SME.

It is also thought that allowing SMEs to use the FOS may have the added benefit of improving standards across the commercial lending industry, revealing trends in complaints, which can help identify issues before they become wide-scale problems. And it may also promote effective competition, with SMEs feeling braver about using lesser known firms or new products.

So, it is clear that the extension has admirable intentions - but has the FOS bitten off more than it can chew?

Resources

The FOS is in the process of implementing the wide-ranging recommendations of the [Lloyd Report](#) (July 2018), commissioned as a result of a Channel 4's Dispatches programme in March 2018 which alleged bias within the FOS in favour of financial services firms. The Report did not find bias but did raise concerns about training and expertise, and risks that certain complaints could have been incorrectly decided.

In addition to effecting change as a result of the Lloyd Report, the FOS is busier than ever in a variety of ways. From 1 April 2019, the FOS's jurisdiction expanded to receive complaints about claims management companies (CMCs) (see FCA [press release](#)). The FOS is taking over this role from the Claims Management Regulator which is part of the Department of Justice. And from 31 January 2019, the FOS's jurisdiction was extended in respect of authorised push payment (APP) fraud, allowing victims to complain not only about their bank, but also about the procedures of the receiving bank. The deadline for the submission of PPI complaints (which accounted for 55% of FOS complaints in 2018) is in August 2019, which might mean a final surge in complaints. And the increase in the FOS's award limit from £150,000 to £350,000 - which took effect on 1 April 2019 and was implemented in order to cater for the needs of new complainants – is likely to result in an increase in complaints across the board – and particularly an increase in more complex complaints, on the basis that higher value claims are likely to be less straightforward to resolve.

In a nutshell, the FOS has a lot on its plate, and extending its jurisdiction to include SMEs from 1 April 2019 is potentially a stretch too far, and will place a strain on resources. In its [December 2018 Budget and Plan](#), the FOS recognised that resourcing levels were already an issue – and that upcoming changes would place a further need for more resources, saying *"We explained [in chapter 1] that we've needed to divert resources in the current financial year to handle growing demand for our help – and there's no indication the trends we've identified will slow or reverse in the coming year. At the moment, we're maintaining levels of customer satisfaction in line with our strategic commitments. However, keeping our service resourced at its current levels will put sustained pressure on our ability to investigate and resolve complaints as quickly as the parties involved need and expect... Our 2019/2020 resourcing plans and budget will also need to account for our ongoing programme of change – including the investment we're making in responding comprehensively to the recommendations of Richard Lloyd, which our board accepted in July 2018...At the same time, we will be investing in and running two significant new jurisdictions. And we'll need to continue to manage our PPI casework"*.

Expertise

In addition to a lack of resource, there are concerns that the FOS will lack the necessary expertise to deal with disputes between financial services firms and SMEs. The FOS has set up and trained a specialist unit to handle complaints from SMEs under its extended jurisdiction with individuals recruited internally and externally, but will they have the tried and tested expertise necessary for such complaints? SME disputes are likely to be more complex than those handled to date by the FOS as they will involve more sophisticated financial products concerning commercial lending and investment, and in particular given the diverse range of industries that SMEs cover. The end of PPI in August 2019 will free up resources, but these case-handlers are likely to have handled nothing more than PPI disputes for the last few years. SME complaints will present a very different, more complex and more diverse caseload to PPI. Casehandlers' expertise is also being stretched in other new directions – such as handling disputes concerning CMCs and against receiving banks for APP fraud.

Suitability

While there is clearly a need for a mechanism to help more SMEs resolve disputes with financial services firms, there are concerns that the FOS is not the solution and the proposals are insufficient to meet their needs. The potential strains on resources and expertise could result in lengthy cases and incorrect results.

Decision making at the FOS is made on the basis that it is "fair and reasonable" (s.228(2) FSMA) – taking into account relevant law and regulation, guidance and standards and good industry practice – but the decision does not have to be in accordance with common law or contract. There are few rules in the FCA Handbook which cover SME treatment and the relationship with their bank (The FCA Banking: Conduct of Business Sourcebook Rules (BCOBS) only apply to individual consumers, micro-enterprises and certain charities). Against what standards would the FOS decide what is "fair and reasonable" in the context of the SME-bank relationship?

Given the FOS's wide discretion when deciding disputes, this could lead to uncertainty for financial services firms – whose legal team might be well placed to advise on the legal position, but more in the dark as to what the FOS might decide, which ultimately might make firms more risk-averse in lending to SMEs. On the other hand, financial services firms with their own in-house and/or external legal teams are likely to be well equipped to present their case to the FOS, not to mention having the greater understanding of the product or service in dispute. SMEs who lack these resources may not find themselves on an equal playing field. SMEs involved in complex, high-value disputes would be well-advised to instruct a legal team and perhaps a forensic expert – in which case they might as well take their case to court, where they will be before a judge with financial expertise (in particular if it is a Financial List case) who will apply law and legal precedent, and have no fetter on the amount (s)he awards.

Is there another solution?

There is support for a reform of the wider regulatory framework so that all commercial lending to SMEs is a regulated activity making SMEs able to sue for breaches of FCA rules - hence getting rid of the current restriction to "private persons". However, this is a matter for parliament, which would need to make legislative changes (unlikely at the moment given the government's preoccupation with Brexit).

Alternatively, a separate tribunal, providing a more formal process for financial services disputes, could be set up. The FCA sees a role for both an extended FOS service and a tribunal working alongside it. Again, such a set-up would need government support and legislative change. As a result of the independent [Walker Review](#) in 2018, UK Finance and seven major banks are planning on launching an ADR scheme for larger SMEs (with a turnover between £6.5m-£10m, and a balance sheet up to £7.5m) and an award limit of £600,000 – potentially higher in deserving cases - which is due to come into force on 1 September 2019 (see UK Finance [press release](#)). UK Finance is also exploring a dispute resolution service for SMEs with a turnover less than £6.5m for uninvestigated claims potentially as far back as 2000 (the current proposed cut-off is 2008 but this may be extended to 2000). There may therefore be multiple routes for SMEs to deal with complaints, but might this lead to a fragmented system with SMEs receiving different treatment and achieving different results for the same, or similar, types of dispute?

What is clear is that SMEs need an alternative mechanism for resolving disputes other than having to go through the costly court system. At present extending the FOS jurisdiction seeks to do this, but, for the reasons set out above, one wonders if this was a quick and easy solution to a far deeper problem with the risk that the FOS could develop into a service which falls below the standard expected by all parties before it.

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