Injustice in financial services disputes (Pt 3)

Michel Reznik reviews the principles of effective dispute resolution & endorses the introduction of a Financial Services Tribunal

IN BRIEF

- Specialist dispute resolution forums are necessary in markets in which David habitually fights Goliath.
- The Employment, Intellectual Property and Competition jurisdictions are examples where specialist disputes forums have proved essential to give David a chance at justice.
- Adopting the specialist Financial Services Tribunal suggested by Richard Samuel would bring justice within the reach of SMEs.

Since the financial crisis, banks and financial services institutions have been exposed by the Financial Conduct Authority (FCA) for mis-conducting themselves, and, in particular, for mis-selling financial products to their SME (small and medium-sized enterprise) clients on an industrial scale. This reputation has been galvanised in the minds of the public by widely-publicised outcomes of investigations into scandals and by enormous fines meted out by regulatory bodies.

Victims of misconduct have rightly expected compensation. The question has been and remains: how and where are they going to get it? The Financial Ombudsman Service (FOS) is not the right forum for disputes of real substance: it has a £150,000 cap on awards which is accompanied by basic processes. The High Court, on the other hand, has the credibility and expertise for such disputes—especially its Financial List, which is reserved to disputes in excess of £50m or those of significance to financial markets. However, litigation in the High Court is both expensive and time-consuming. The 'loser pays' rule puts High Court litigation beyond reach of the victims of misconduct, particularly SMEs.

The FCA (and its predecessor, the Financial Services Authority (FSA)) duly recognised that those two forums serve each end of the dispute resolution market well, but not the mid-market. So it attempted to bring into being such a mid-market dispute resolution forum to fill the gap; it created mass-redress schemes (or 'bespoke adjudication processes' as the FCA calls them).

In two seminal articles published in *Capital Markets Law Journal (CMLJ*)'Tools for changing the banking culture: FCA are you listening?': April 2016 Volume 11 Issue 2: 129-144 and 'Tools for Culture Change: FCA now you are listening!' (*https://doi.org/10.1093/cmlj/kmw029*) Richard Samuel, barrister at 3 Hare Court, observes that the FCA took a wrong turn. The schemes were technical and administrative, replete with conflicts of interest—as the banks were the investigator, judge, jury and executioner in actions against them—and, fatally, they were conducted behind closed doors. These schemes were so favourable to the banks that some are now voluntarily establishing redress schemes when their misconduct is exposed.

The victims, however, are dismayed. For example Mike Hockin, who ran a commercial property business, recently settled an interest rate swap mis-selling case in this way with RBS. On 18 May 2017 he was reported saying to the BBC: 'I was gutted, I didn't want to [settle] because I don't feel that justice has been done.' Having accumulated costs of £12m he said: 'I made the decision to call it a day but I wasn't happy. But I really had no choice with it.'

In 2016 Andrew Bailey, the CEO of the FCA, recognised that under his predecessor the FCA stepped outside its competence and these schemes failed to meet their intended objectives. He has also endorsed the solution Richard first proposed (see 'Injustice in financial services disputes' Pts 1 & 2 for a fuller briefing of the background *NLJ,* 28 April 2017, p 18 & 19; *NLJ,* 12 May 2017, p 15 & 16).

The right mid-market dispute resolution forum

Richard argued that the mass-redress schemes should be replaced by a permanent dispute resolution system that possesses four characteristics: that it is: (i) specialist; (ii) inexpensive; (iii) swift; and (iv) most importantly, that it operates the adversarial common law system.

The significance of the adversarial common law system is that public trust and confidence in its competence and independence is well established. Alas, the same cannot be said of the FCA, against which a motion of no confidence was debated in the House of Commons on 1 February 2016. That debate largely focused on the inadequacies of its mass redress schemes.

The adversarial nature of the common law gives the litigants their day in court and gives them a voice to have their say and test the other side's case. Mr Bailey, giving evidence to the Treasury Select Committee on 20 July 2016 acknowledged that the FCA's mass-redress schemes were not able to provide the essential sense of having had one's day in court.

As far as the broader public interest goes, Richard reminds us that the common law is a system of open justice that continuously evolves as each judgment adds to the sum of market knowledge: by determining questions of fact and law, the courts publicly work out the principles that guide norms of the market behaviour. Market participants are then able to observe the courts' reasoning and conclusions and adopt the principles and practices of which the court approves.

In his two *CMLJ* articles, Richard has pointed to three historical examples of the adversarial common law approach being adapted to create a specialist dispute resolution forum which works even where there are enormous imbalances between the parties.

Example 1: The Employment Tribunal

Historically, the common law courts were not able to provide employees with effective rights against their employers. Common law rights only extended to recovering an unpaid notice period, but the costs of recovering it outweighed any benefits. In the 1960s this became politically unacceptable so *The Donovan Report* of 1968 recommended that employees be given new statutory rights: the right not to be unfairly dismissed and later the right not to be discriminated against.

But those rights were of no use without an accessible forum where they could be enforced. The 1968 report also recommended for a specialist forum to hear the disputes: what since 1 August 1998 has been known as the employment tribunals. They had the four characteristics Richard identified.

First, they were specialist as cases were heard before an employment judge often accompanied by two wing-members: one appointed via nomination of Trade Union Congress and one via nomination by Confederation of British Industry. Second, informality and simplicity of rules made the cases progress swiftly. Third, low fees, the lack of the need for a lawyer and exclusion of the loser pays rule meant they were inexpensive. Fourth they operated the adversarial system but blended it with an inquisitorial element to assist employees representing themselves.

Employment tribunals provide the context for thousands of disputes each year to be resolved by settlement or judgment (even after erosion of those four principles in recent years for example by the introduction of fees and a reported 70% fall in cases). In the 45 years of its operation this carefully calibrated adaptation of the adversarial common law system has created a body of case law which has moved the common law and industrial relations on from 'master and servant'. Doing so has transformed civil society as a whole.

Example 2: Intellectual Property and Enterprise Court (IPEC)

Small businesses developing intellectual property rights need to have the ability to protect themselves against infringement by other start-ups and against oppressive actions by tech or pharma giants. Such industries, with regular disputes between David and Goliath, need a specialist forum to allow each party an effective day in court.

Until 1990 the only forum for such disputes was the Patents Court, which is part of the Chancery Division of the High Court. Its specialist judges heard adversarial argument from the specialist Bar and delivered quality judgments. But it was ineffective to satisfy the needs of the SMEs because it did not respect two of the principles Richard identifies: it was slow and expensive.

In 1990 a low-cost Patents County Court (PCC) with limited jurisdiction was created to hear small cases. It did not fully meet the needs of the SMEs. So, after consultation, the Intellectual Property Court Users Committee published a report in 2009 in which it made a series of recommendations that focused on expanding the PCC's jurisdiction to all forms of intellectual property.

The recommendations were adopted in *The Final Report of the Review of Civil Litigation Costs* by Lord Justice Jackson on 1 October 2010. Finally, on 1 October 2013, the PCC was reconstituted as a specialist list of the Chancery Division of the High Court and renamed to IPEC. The reforms brought into being a carefully-balanced set of rules to level the playing field which made the forum quick and inexpensive: for example by capping the loser pays rule at £50,000, by limiting damages to £500,000, unless litigants agreed otherwise, and trial lengths to two days.

The IPEC has been a great success: *Evaluation of the Reforms of the Intellectual Property Enterprise Court 2010-2013* (22 June 2015) found that there has been an general increase in claims filed—particularly by SMEs, so that 45% of cases in 2013 were filed by SMEs. That directly reflects previously suppressed demand among SMEs for IP dispute resolution services.

Example 3: Competition Appeal Tribunal (CAT)

In 2013 the Department of Business Innovation and Skills (now the Department for Business, Energy and Industrial Strategy (BEIS)) reviewed the progress it had made on its duty to ensure markets remain free of anti-competitive behaviour. It had been pursuing two means of doing so: first directly, by bringing enforcement actions against those who abuse market dominance and second indirectly, by encouraging victims of anti-competitive behaviour to bring actions on their own behalf.

In 2013 BEIS published its *Final Impact Assessment*, after a consultation. In it, BEIS recognised that its enforcement action necessarily focused on big-ticket cases and the two forums for private actions—the Chancery Division of the High Court and the CAT—failed to respect two principles of effective SME justice: low cost and high speed.

The *Final Impact Assessment* made a simple and obvious but crucial finding that the FCA missed: the regulator can't be everywhere. Accordingly BEIS advised the government that, rather than relying on more state enforcement in competition law, it needed to create a dispute resolution platform which allows individuals and SMEs to bring claims against abusers of market dominance. This led to the Consumer Rights Act 2015, which increased the rights of SMEs to bring such claims and introduced a 'fast track' procedure in the CAT, the speed and cost of which is designed for SMEs.

The future

Richard has proposed that the principles distilled from these three historic examples be used to establish a Financial Services Tribunal (FST), which brings justice within reach for SMEs while ensuring the system remains just for banks and financial services institutions. It should be:

- swift, by keeping the rules simple and tailored for speed;
- inexpensive, by: (a) focusing rules of procedure on lowering costs and in particular by modifying the loser pays rule; and (b) by introducing an inquisitorial element to assist those who cannot afford legal representation;
- expert, as judges will be drawn from the commercial bar and judiciary and the wing members from the financial services industry and the small business sector; and
- authoritative, as it will produce high quality, publicly reasoned judgments subject to appeal which explain how the law applies in practice.

A tribunal established according to these principles will provide the public with confidence that there is an independent, open and robust forum in which mid-market clients, including SMEs, can hold banks to account. In time, that forum will create a body of law to fill the lacuna left by the mass-redress schemes. The Hon Mr Justice Browne-Wilkinson observed in 'The Role of the Employment Appeal Tribunal in the 1980s' (1982) 11 Indus L J 69, that '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*'.

A FST will quickly develop a body of law determining what *fair business conduct* means in financial services and by doing so it will stimulate an overdue change in the culture of the financial services sector. **NLJ**

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