



# Financial Services Bill: an update on collective redress and regulator-led redress

This is an update to our briefing of December 2009, which considered the provisions in the Financial Services Bill (the Bill) relating to collective redress and regulator-led redress. These provisions have now been debated in parliament by the House of Commons Financial Services Bill Committee (the Committee). This update sets out the key issues raised before the Committee and the government's response.

## Introduction

A number of concerns were raised before the House of Commons Financial Services Bill Committee (the Committee), including questions as to the lack of detail in the provisions and whether they contain sufficient safeguards against abuse. The Committee did not amend the Financial Services Bill (the Bill) in light of the concerns raised. The Bill, however, is still to be debated in the House of Lords and there is likely to be significant further debate before the Bill is passed or rejected. The collective redress and regulator-led redress provisions remain highly controversial.

## Collective redress

The Bill would give the court the power to permit a collective action, on either an opt-in or an opt-out basis. The action would be brought by a representative claimant on behalf of a class of customers or other claimants.

### Opt-in or opt-out?

The Committee considered whether it was right that a collective action could be brought either on an opt-in or an opt-out basis. The government's view was that, although there was strength in the argument that collective actions should be brought on a pure opt-out basis, the court should have the flexibility to determine whether the action should be brought on an opt-in or opt-out basis depending on the circumstances of each case.

## Should collective actions be limited to claims brought by consumers?

Under the Bill, a collective action could only relate to a 'financial services claim', which, broadly, is defined to encompass claims against authorised firms relating to regulated activities or dealings with firms in the conduct of their regulated activities. Collective actions would be available to any claimants whose claims fell within this definition. The Committee considered whether collective actions should be confined to claims brought by consumers (defined as 'any natural person, who in the matters to which the claim relates, is acting for purposes which are outside his trade, business or profession'). The government's position was that it would not be right to limit collective actions in this way and that collective actions should be available to businesses, especially small businesses, as well as charities, the self-employed and individuals acting in a professional capacity. None of these entities would fall under the proposed definition of 'consumer'.

## Lack of detail in the Bill

The Bill is drafted in broad terms and leaves a number of detailed provisions to be made under subsequent statutory instruments. This has led to concern that implementation of the Bill would lead to the use of secondary legislation to amend primary law (in particular, as to the limitation period and allowing aggregate damages claims). The government, however, considered that it was important for the Treasury to retain the power and flexibility to introduce detailed provisions by way of secondary legislation and to be able

to tailor collective proceedings to the features of financial services.

### **Safeguards against abuse**

The Committee considered whether the Bill contained sufficient safeguards to protect against abuse including, for example, speculative claims and vexatious litigants. The government agreed that such safeguards were necessary and noted that some were already provided for, including the 'loser pays' principle<sup>1</sup> and the fact that only cases that cannot be settled by the regulator will proceed to the court. The government emphasised, however, that the detailed provisions as to safeguards should be contained in the secondary legislation and court rules rather than in the primary legislation. This is because secondary legislation and court rules require full consultation and can, via such consultation, be tailored to the financial services sector. In addition, secondary legislation is easier to change and update than primary legislation. The government intends to spend a significant amount of time talking to stakeholders and other interested parties to make sure that their views are properly taken into account when it comes to developing the new provisions.

### **The role of the Ombudsman**

The Bill provides that regulations enacted by the Treasury may require that the Financial Services Authority (FSA), the Office of Fair Trading and the Ombudsman Scheme Operator are entitled to be heard on an application for a collective proceedings order. It was proposed to the Committee that it was not appropriate for the Ombudsman Scheme Operator to be heard because the Financial Ombudsman Service has no regulatory function. The government explained that the role of the Ombudsman Scheme Operator would not be as a regulator but as an information provider. The Ombudsman Scheme Operator would provide information to the court, which would help the court determine if collective proceedings, rather than a regulatory solution, are a suitable means of dealing with the case.

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<sup>1</sup> Since this debate, Lord Justice Jackson has published his report on costs. In this report, he recommends that the loser pays principle 'should remain for collective actions (with the exception of personal injury collective actions), but that the court should have a discretion to order otherwise if this will better facilitate access to justice'. If Lord Justice Jackson's proposals are implemented, therefore, the loser pays principle may not continue to be a safeguard in the manner currently envisaged by the government.

## **Regulator-led redress**

The Bill would permit the FSA to impose, after consultation, redress schemes requiring firms to investigate particular books of business and to determine whether they had breached their obligations to their customers and, if so, whether the customers had suffered loss and what redress should be paid.

### **The role of the FSA**

This has led to a concern that the FSA's *ex post facto* view of what standard of conduct was required at a particular time in the past could, in effect, be imposed upon firms so as to establish their legal liability to pay redress to customers. The FSA would be able to establish a firm's liability in this way without any of the safeguards that exist under the Financial Services and Markets Act 2000 (the FSMA) to ensure that the FSA's procedures are compliant with the Human Rights Act and to avoid it being 'judge, jury and executioner'.

The government explained that the FSA's power under the FSMA to deal with groups of complaints and order reviews of past business is limited in scope and has a high threshold for action, meaning that it has never been used. There is, therefore, a gap in the regulatory system that needs to be closed.

The Bill would introduce an extension of the FSA's normal regulatory remit. The decision to establish a redress scheme should be taken by the FSA rather than the courts because:

- the FSA has a higher degree of specialist knowledge;
- the role of the courts is to assess whether the FSA has exercised its powers lawfully and in line with FSMA responsibilities, not to assess the merits of regulatory action; and
- involving the courts is likely to be burdensome and slow.

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