HOUSE OF COMMONS

Treasury Committee

Oral evidence: SME Finance, HC 805

Tuesday 23 Oct 2018

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Watch the meeting

Members present: Stephen Hammond (Chair); Rushanara Ali; Mr Simon Clarke; Charlie Elphicke; Stewart Hosie; Alison McGovern; Catherine McKinnell; Wes Streeting.

Questions 358-432

Witnesses

I: Simon Walker, CBE, Independent Chair of the UK SME Complaints and Resolution Review, and Professor Christopher Hodges, Professor of Justice Systems, University of Oxford.

Examination of witnesses

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In the absence of Nicky Morgan, Stephen Hammond took the Chair.

Chair: Good morning, Professor Hodges and Mr Walker, and thank you for coming to give evidence. As a way of starting, and so that everybody is clear who you are, I wonder if you could both briefly introduce yourselves.

Simon Walker: I am Simon Walker. I chair the independent review of the alternative dispute resolution and SME environment.

Professor Hodges: Good morning. I am Christopher Hodges. I am Professor of Justice Systems at the University of Oxford.

Q358 **Chair:** Thank you both very much for coming to give evidence this morning. The Chair, the right hon. Nicky Morgan, sends her apologies. Surprisingly, both for you and for me, I find myself in the Chair this morning.

Your report, Mr Walker, has been published this morning, along with some commentary from the all-party parliamentary group on fair business banking and finance and others. I wonder whether both of you could briefly set out what you believe to be the review's primary conclusions and recommendations.

Simon Walker: I was asked to chair the review by UK Finance because I strongly believe in the importance of small and medium-sized enterprises to our economy. They employ 60% of all employees and generate roughly half of GDP. Lending matters enormously to them, and a good banking system is enormously important. I also believe that, at the time of the global financial crisis, there was very poor behaviour by a number of banks towards their SME customers. A lot of the putting right in the global financial crisis impacted very heavily on them. A big part of the project was looking at what happened then and seeing how the situation is now. There is a significant aspect of the report that covers that territory.

Our major recommendations are for a significantly beefed-up ombudsman system directed at small and medium-sized enterprises, but within the overall framework of the existing Financial Ombudsman Service, with new skills and expertise added. As I have said, I think the FOS lacks some of the skills that it needs.

We also recommend a voluntary ombudsman scheme that the banks would have to agree to and that would support larger businesses that are not eligible complainants under the proposed changes that the FCA has recommended—that are somewhat bigger than that—as well as a scheme that would look at legacy SME disputes that have not been adjudicated, and that is quite an important qualification, from the financial crisis era.

The third recommendation, to which I attach great importance, is for real-time data links between the banking ombudsman facility, the Financial Conduct Authority and relevant Government Departments so that there is a constant flow of data about what people are complaining about and how those disputes have been resolved.

The fourth key recommendation is for a formal process attended by the most senior representatives of major banks that tries to achieve reconciliation and closure between the people and businesses who suffered most—a lot of whom I have met—at the time of the global financial crisis. In that process, they would tell their stories, and senior bankers would listen to them, respond and acknowledge the hurt that was done.

If we commit to a new system of dispute resolution that looks forward, rather than back, I hope we can future-proof against a recurrence of this kind of issue, but my chief concern is to provide a fast, fair and inexpensive way of resolving disputes between SMEs and banks, and in that way to rectify to some extent the power imbalance that exists between the two.

Q359 **Chair:** Professor Hodges, is there anything you would like to add to that?

Professor Hodges: Two short things. First, my function is to try to assist Mr Walker by setting out a wide range of options. My paper, which is an annexe to his, tries to do that in relation to dispute resolution options, regulatory options and emotional closure options, without particularly indicating my own views. Secondly, having looked at all the evidence that has been produced, including that of Professor Robert Blackburn from Kingston University—he is also here, and he conducted an extensive data survey—and the data that the FCA published in its consultation last week, I entirely support Mr Walker's conclusions that this is the right way forward.

Q360 **Chair:** Thank you. In your answer, Mr Walker, you highlighted the recommendation about creating a business banking facility under the technical and budgetary aegis of the FOS to handle SME banking disputes. The FCA announced last week that it is making changes to the FOS's eligibility criteria to give more SMEs access. Is your primary recommendation doing something different from that? In what ways does it differ from what the FCA is already suggesting?

Simon Walker: No, I think it is entirely supportive of what the FCA is proposing. It goes a little bit further than the FCA does, in terms of suggesting that the compulsory jurisdiction or award capability of the new entity should be slightly higher and that the range of businesses that could be included could include some slightly larger SMEs, perhaps with a turnover of up to £10 million a year. I am entirely supportive of the measures that the FCA proposed last week.

I suppose that I do propose a greater detachment of the business pillar of the FOS. When I started this exercise, the first thing I did was go on the FOS website. It seemed to me that if I was a businessperson, I would not feel it was aimed at me; I would feel it was aimed very largely at consumers, and that is understandable and natural. What needs to be created is something that has a kind of branding and a presentation that aims very squarely at SMEs and companies with business issues, rather than consumers with individual issues. That needs to be accompanied by a considerable enhancement of its expertise.

Q361 **Chair:** I would like to come back to the business pillar later. At the start of that answer, you said that you support the FCA and that you see it as complementary. In your report, you also say that the FOS lacks the skills and specialisation to deal with complex financial disputes, yet the FCA is proposing extending the jurisdiction from next April. Is it really feasible for the FOS to develop those skills in that time?

Simon Walker: It is extremely ambitious, but getting something in place quite quickly is very much my aim. I think the FOS could start the process now with a fair wind—and the FCA's paper last week has given that fair wind. It could start the process of enlisting people who will bring those skills. At the moment, something like 60% of all the FCA's work is about payment protection insurance, which means that, from the end of next year, there will be a drying-up of much of what it does at the moment. I am saying that it should really get its skates on and work on bringing in business expertise to provide a complementary facility.

Q362 **Chair:** I hear that, but the FCA talked about creating a panel of external experts—a professional practice group. You talk about reviewing the governance structure, an expert special advisory body and legal practitioners. You just said that it is a fair wind, but some might think that it needs a hurricane to achieve that by April 2019. How long do you think it will take for your recommendations to be introduced?

Simon Walker: My hope is that, by the middle of next year—I am talking about eight months or so—one could have a functioning division of the FOS that would be capable of dealing with larger SME complaints. One is not talking about a vast number at the moment, because I don't think that SMEs are complaining about issues that would go to the FOS to nearly the extent that they were at the time of the financial crisis. There is a huge load of legacy issues from that period, but at the moment most complaints to the banks are of a fairly mundane character and would not actually end up with the FOS.

Q363 **Chair:** To be clear, you are hopeful that, by the end of the second quarter—the end of the first half—next year, there will not only be a business pillar properly established but a functioning element to it.

Simon Walker: That would be my ambition.

Q364 **Chair:** That is the recommendation and ambition.

Simon Walker: Yes, indeed.

Q365 **Chair:** In your review, you would obviously have been aware that Richard Lloyd, in his review, concluded that the previous large-scale reorganisation was performed at too great a pace. Given your hope and ambition for this, where do you differ from him? Are you saying that, although this is important, it is a smaller pillar, or are you saying that the FOS just needs to get its act together rather faster?

Simon Walker: I think it does need to do that, but it is aware of that. In fact, it has been thinking about this and considering the need to beef itself up in the business area for some time. The FCA's consultation paper has been out for almost a year, so the FOS is aware of this. It knows that this kind of demand is likely, and it has been gearing up already. Would I like to see that happen more quickly? Absolutely, but I think it is aware of that need. It is particularly aware of the need to bring in specialist skills. It has been so dominated by PPI claims over the last few years that it needs a kind of repositioning.

Q366 **Chair:** I accept that, but we are obviously looking at the SME financing today and your recommendations on that. You recommend that the eligibility criteria for the FOS should be reviewed again. You talked about potentially looking at the increase of business size. You recommend that in two years' time. Why wait? As you rightly said, they have been considering this for a period of time. Why don't we just make the change now?

Simon Walker: Well, the FCA's change would put its jurisdiction up to £350,000 from £150,000 from next April.

Q367 **Chair:** You are suggesting up to £600,000.

Simon Walker: I am suggesting £600,000. Had I been in the FCA's position, I think I would have gone for a £600,000 upper limit now. I am not wildly critical of the FCA. It has a consultation paper at the moment that is looking at where that figure should end up. My suggestion would be that it should be higher than the £350,000 that it envisaged.

Q368 **Chair:** Although you say it is being reviewed in two years' time, you would be happy if there were pressure on the FCA to introduce a £600,000 limit now.

Simon Walker: Yes, I would. I stress that I do not think the FCA envisages that a vast number of cases would fall into that category. Specifically, it envisages that between five and 50 a year from larger SMEs will be in that above-£150,000 jurisdiction category. Yes, it needs to gear up, but that is not an insurmountable task once one considers what the FCA is going to be dropping back on.

Q369 **Stewart Hosie:** Mr Walker, it is fair to say that throughout this inquiry the FOS has been pretty roundly criticised. Lawrence Tomlinson described it as "a complete waste of time"; the Economic Secretary said he was "concerned" and "keen to be reassured" about its effectiveness; an SME dispute resolution lawyer said the FOS was not "fit for purpose"; and even your own report states that the FOS "board and senior management need to…get a grip on the organisation." Given that you are recommending significant new responsibilities for the FOS, can you explain why this Committee should have any more confidence in its ability to take on those important roles than in its ability to fulfil its functions in the past?

Simon Walker: This Committee and other people have rightly put pressure on the FOS to up its game considerably, and that needs to be maintained. The Financial Ombudsman Service employs 3,500 people, which makes it the largest ombudsman service in the world. It has a budget running into hundreds of millions of pounds. I do not think it makes sense just to write it off. The question is: can it be re-geared quickly to provide a system that is fast, fair and inexpensive for this important category of businesses? That ought to be the first option, since that is its statutory role. Should it have its feet held to the fire? Yes it should, but Richard Lloyd's report, although it is critical—in some areas very critical—does not say it is completely unfit for purpose. It does say it needs to be improved.

Q370 **Stewart Hosie:** So what practical steps does the FOS need to take to rebuild and command confidence among the UK's SMEs?

Simon Walker: It needs to bring in people who have adequate expertise at a professional level. It needs to set up an expert panel with strong legal and banking knowledge that can help them. And it needs to redirect its whole focus, at least for this new pillar, away from purely consumer-related work and towards small and medium-sized businesses, so that businesses think of it as a practical place that they can go that will not involve the cost of going to court, which is the principal thing I am trying to avoid.

Q371 **Stewart Hosie:** Of course, the other argument is that a completely new, separate dispute resolution mechanism specifically designed to handle more complex disputes would be an alternative, would it not? Would you see that new resolution regime being within the FOS but operating separately? How would that work?

Simon Walker: I suppose my primary feeling is that an ombudsman-type facility is what is needed. There are a number of reasons for that, but they are fundamentally around the basis of decision making of an ombudsman as opposed to a court or a legal tribunal process. Since the FOS is there, since it is actually quite well resourced in terms of people and money, and since it is funded by the financial services industry, it seems to me the right place to start. Frankly, I do not think—from a taxpayer perspective aside from anything else—it makes sense to write off an organisation that has statutory responsibility and has that many employees and that kind of budget.

Q372 **Stewart Hosie:** I am sure that bit of the debate will go on, but let's just leave that aside for the moment. The FOS will soon be undertaking a review of cases considered during the early stages of its reorganisation in 2016, following concerns about its decision making. Notwithstanding this Committee's concerns about the design of that review, if it were to uncover serious flaws, do you think that your recommendations might need to be reconsidered?

Simon Walker: I still think that the statutory body that has responsibility for dealing with business complaints and that falls under the FCA—and the FCA has just raised the limits—ought to be the first port of call. I suppose that what I am saying is that I do not think that the FOS is in such bad shape that it should simply be written off and closed down. That would be unwise. I do think that it needs a major adjustment to its focus and, as PPI winds down as an issue, that this is the right time to do it.

Q373 **Stewart Hosie:** Okay. May I just check? Is that review of cases during the early stages of reorganisation the same review as that of legacy SME disputes which you spoke about earlier—ones that have not yet been adjudicated—or is that a separate exercise?

Simon Walker: That is very much a separate exercise. I am suggesting that the banks, on a voluntary basis, should review claims dating back to the global financial crisis that have not been adjudicated—that have not had the opportunity for adjudication—whether through the courts, the FOS or ad hoc processes.

Q374 **Stewart Hosie:** This is where I have some difficulties. I have a case—we have cases, and I have many cases—but it has been adjudicated. The first adjudicator found in favour of the constituent. A subsequent adjudication produced a very detailed and accurate assessment of the case. Another ombudsman, however, appeared and changed the whole basis of that thinking and, I am told, suggested that he would conclude what he concluded and that new evidence would not alter his decision. This has been adjudicated, but in my view and that of many others, it has been adjudicated wrongly.

Simon Walker: Is this by the FOS?

Stewart Hosie: Yes, it is—by the FOS. Where do we go with this? If he happens to fall into the adjudication being around the restructuring in 2016, he will have his case reopened, but because it has been adjudicated, if the timings do not work, it will not be. You are going to have two categories of businesses—one that, finally, may get justice, and another, simply because of the serendipity of timings, that won't. Would it not be better, if you are going to look at these legacy cases, to take out the caveat about adjudication, unless of course businesses are happy that they got a fair hearing, and to look at them all again?

Simon Walker: I suppose my concern is limits—one has to set them at some point. My concern would also be for the businesses that have settled through existing processes. I think it is unfair to them to allow others to have a second bite of the cherry. I obviously don't know about your constituent's case, although I would be happy to take a look at it if that were necessary, but one has to strike a balance between what is actually practical and going ahead. To me, something that reviews cases that have not been assessed—of which there are some going back a long way, way beyond the current jurisdiction of the FOS, which I think is three years or, in some circumstances, six years—seems a sensible compromise.

Q375 **Stewart Hosie:** Can I just challenge you there? You said it would be unfair on those who have settled for another case to be reopened, but there is nothing inherently unfair to someone who has settled a case and is happy with the outcome about a case where there is still dispute—adjudication or otherwise—being reopened and reinvestigated. It is a false argument to say that it is unfair to someone who is quite content to look at a case where there may still be a very serious dispute.

Simon Walker: I understand. There are many tragic cases, an awful lot of which I came up against, but I do not think that one should set up an open-ended mechanism. I just do not think that it is practical to set up an open-ended mechanism that re-weighs issues that have been considered. I do not know your constituency case. I completely understand—it may be in that category, but my suggestion is that there should be an arrangement for cases that have had no adjudication, of which there are a number. Otherwise, it gets very difficult to delve into matters that go back beyond a decade. I am not quite clear and do not know the situation, but if your constituency case is from 2016, it is still within the current jurisdiction of the FOS, because it is within a three-year timescale.

Q376 **Chair:** Professor Hodges, before we move on, can I ask you this? You will have seen the report that says that the ability to make decisions based on what is fair and reasonable is a good candidate for resolving SME disputes. Can you set out why you think that might be a better way of resolving disputes rather than using English common law, for instance, which is widely regarded as a gold standard?

Professor Hodges: If I may say, the common law is not entirely on the point. The courts decide disputes based on "the law". In financial services, the law is primarily Parliament and statutory guidance or instruments made by the FCA, so in this situation, the common law does not actually play much relevance statistically. The major point is that the courts decide law. We have extended consumer protection over the past 50 years to allow disputes to be decided on the basis of what seems fair and reasonable to the ombudsman. Of course the law is taken into account, and the substance of consumer law has extended very considerably. There are quite a few ombudsmen in different sectors in this country at the moment. I think that that is the gold standard internationally.

In relation to an earlier point, if you go round Europe or the rest of the world and talk to other ombudsmen—there are not that many, although there are more in financial services than in other sectors in most other countries—they all regard the British ombudsman model as virtually the gold standard. Secondly, they regard the FOS as the one to go and visit and learn from. The international standing of the FOS is extremely high. I was in one country last week—

Q377 **Chair:** Before you move on, is that international standing with regard to consumer cases as opposed to SME cases?

Professor Hodges: The extension that is now happening is moving into SMEs. As proposed by the UK, a number of foreign ombudsmen are extending their jurisdictions into SMEs—Australia and the Netherlands this year, and various others. Some of them, like Switzerland, already accept SME cases, but this is actually a move that is taking place. Therefore, in many ways, I regard the current proposals, whether by the FCA or Mr Walker as being part of a direction of travel that is entirely explicable and actually the right one.

On your original question, courts decide law, and tribunals decide law, subject to one proposal, but ombudsmen decide what seems fair and reasonable in the circumstances of the case, taking the law into account. That is a much wider jurisdiction. Therefore, for example, in the current ADR schemes, which were set up by RBS and Lloyds, and which are overseen by Sir William Blackburne, a High Court judge, and Professor Russell Griggs, they were empowered by the banks to make a decision on what seems fair and reasonable. We were told by Sir William that in a good 90% of the cases, if they had been in court, the SMEs would have lost. You can see the power of the extension of "fair and reasonable".

Chair: Thank you for clarifying that point.

Q378 **Charlie Elphicke:** Mr Walker, small businesses in my constituency of Dover and Deal think that the banks have taken them for a ride and ripped them off massively. Are they right to feel that?

Simon Walker: At the time of the global financial crisis, that was certainly right. That did happen—I do not think I pulled my punches on this—and the banks engaged in shameful behaviour at that time. That has largely stopped. By now, the situation is considerably better. That is partly a fact of better regulation and greater powers for the FCA. It is partly a sense of public pressure and a sense of shame that a number of the banks rightfully feel about their behaviour at that time. Yes, your constituents are right. I do not think it is happening to nearly that extent now, but I believe we need remedies so that, if it arises in the future, your constituents would have a fast and cheap remedy that would come up with a fair outcome.

Q379 **Charlie Elphicke:** Do you think that my constituents will have a better deal in future thanks to your review?

Simon Walker: Yes I do. I believe that your business constituents will benefit from a system that offers them fair and reasonable judgments rather than strict legality. I can give a fairly typical example that was brought to me in a number of cases. Before the global financial crisis, if a bank gave a loan on a property with a covenant—a loan-to-value ratio of 60%—and the value of that property dropped to 55%, undoubtedly in terms of the contract the bank was entitled to demand its money back the next day, or to put up interest rates massively on that loan even if the payments were being met. Was that behaviour legal? The answer is yes, it was within the contract. Was it fair and reasonable? That is highly questionable. I would like the judgment to be made by an entity that has the ability to say, "That may have been in the contract, but the provision was not fair and reasonable, and the way in which the bank enacted it was not fair and reasonable." That seems to me to be in your constituents' interests.

Q380 **Charlie Elphicke:** Prior to the beginning of your review, UK Finance, that well-known, forward-looking and reforming trade body of the banks, stated that it "does not believe a case has been established" for "further institutional change to handle SME banking disputes". It also said that it believes "the incidence of cases justifying redress on a scale that cannot be addressed by the FOS is low". Having given that Panglossian viewpoint before your review started, it then paid you to do the review. Do you think it was appropriate for UK Finance to make that kind of statement before you did your work?

Simon Walker: Well, they commissioned me to do an independent review and I have no responsibility to endorse their previous statements, and I do not. They gave me no steer on what I was to come up with. They helped me to contact banks, but no more than that. There was no pressure on me and, as you can see from the report, I absolutely have not pulled my punches in my descriptions of the past behaviour of the banks. That is really over to them. I am not justifying those previous statements.

Q381 **Charlie Elphicke:** Do you think that was broadly unhelpful and that a period of silence from them would have been welcome?

Simon Walker: That is very much a matter for them.

Q382 **Charlie Elphicke:** Did knowing UK Finance's position—there is nothing to see here and we should just move on—cause you to be less radical in your recommendations, or did you just do what you thought was right anyway?

Simon Walker: I did what I felt was right anyway. I think I have been fairly radical, but I have been tempered by a belief that I should come up with something practical that could mean we had a system working within a year, rather than something that would require legislation—I do not see the likelihood of getting that through the parliamentary process in short order. To me, coming up with a remedy that could be put in place rapidly was quite important. That was the only thing that tempered my radicalism.

Q383 **Charlie Elphicke:** Your report has just been published this morning. It is strikingly similar to the changes announced by the FCA last week. Is that an incredible coincidence, or have you been working with the FCA quietly as well?

Simon Walker: No, I haven't. I think anyone who read the original FCA consultation paper would have known what the FCA was likely to come up with, so I was aware of that, but I hope I go rather further than the FCA in some important areas. As you can tell, I have not pulled my punches, either about the FOS or about the banks. I have been critical where I felt it was necessary to be critical.

Q384 **Charlie Elphicke:** Where have you gone further than the FCA, and what are the areas where you think the FCA should go further themselves?

Simon Walker: I would have preferred, rather than having the ceiling for SMEs as a turnover of £6.5 million, to have gone a bit higher, perhaps to £10 million. I am influenced by the fact that the Legal Services Board thinks that a company that has turnover of more than £10 million ought to be able to look after itself legally. If you are going to make a judgment, that seems about the right position, so I would put it there.

Also, whatever the new business ombudsman service ends up being, I would like to give it a bit more clout than it has. The Australians, who have also been reviewing the financial ombudsman scene, have set it at A$1 million, which is roughly £600,000. That seems to me an appropriate upper limit. I would accept that once you get much above that you need a kind of legal imprimatur before a penalty can be levied, but I would prefer to see it that bit higher.

There are other things that I recommend that are beyond the FCA's remit, which include the rebranding and the very clear focus on business. Quite a number of the businesses that we talked to were not aware that they could go to the FOS, and just telling them that that facility is available seems to me terribly important.

Q385 **Charlie Elphicke:** The Economic Secretary has on many occasions noted that your review will be an important contribution to his deliberation on the subject of redress and regulation in the SME finance market. To what extent have you engaged with the Treasury as part of your review?

Simon Walker: I have kept in touch with the Treasury. I have let them know what my thinking was along the way. I have certainly been in touch with them. They obviously put no pressure on me to come up with a view. I have occasionally sought advice about what was and was not legally practical without legislation. I suppose that is the only sort of technical area where I have had to go to the regulator or to Government Departments and say, "What can one come up with that does not require primary legislation?"

Q386 **Charlie Elphicke:** Finally, your report does not actually recommend that the Treasury take any action. Have you let them off the hook?

Simon Walker: I don't think so. It is so clear to me that the Treasury and the relevant Ministers are looking at this and are going to come up with something.

Some of my recommendations, and some of the most important ones, are not really for the Treasury. The dataflow between the complaints procedure and the FCA is hugely important. One of the biggest shocks I had was finding out that the first PPI case was in 1994, but because it was sealed as a judgment it was more than a decade later that PPI was evaluated, a super-complaint was laid and the regulatory authorities decided that PPI was not permissible.

It is that sort of gap that I am trying to avoid, but that dataflow, which I think the FOS is conscious of the need for, is not really a Treasury matter. Nor, actually, is the reconciliation and closure procedure, which I think is terribly important, because a number of people represented by the all-party parliamentary group, including people who have actually gone bankrupt, said to me, "We've just never had our stories told. We've never had an opportunity for a hearing." I am very sympathetic to that view. These are people who are bankrupt anyway, and the money would not help them because it would just go to their creditors, but the chance to tell their story and say what happened seems to me quite an important right.

Q387 **Wes Streeting:** There is obviously a huge amount of political interest in all of this. The chair of the APPG on Fair Business Banking and Finance is here with us this morning, as is the shadow Economic Secretary to the Treasury. That is largely because all of us through our casework have seen many examples of small and medium-sized businesses being treated terribly and the remedies falling far short of expectations. I am therefore quite surprised that, in your report on page 22, you acknowledge, and I think you have done again this morning with your evidence to us, that: "There has been a gap – a failure to provide a (metaphorical, if not actual) 'day in court' where victims' stories can be told, wrongs acknowledged, remorse articulated, and assurances given of behavioural and cultural change." That sounds to me like a compelling case for a public inquiry. Why didn't you make one?

Simon Walker: There have now been four or five inquiries into what happened, particularly if one looks at RBS, which is perhaps the principal case. I think it is actually all out there. There may be people who disagree with me on this, but I think the material is there. I fear that a public inquiry would take four or five years. The Lloyds/HBOS inquiry which Dame Linda Dobbs is leading is not likely to come out until the end of next year and it has been going for three years.

Postponing coming to conclusions on this—postponing arriving at closure—is not in anyone's interests. To me, the important thing is to settle on a way forward, a way of dealing with complaints now, a way of future-proofing, so that next time any of this type of issue comes up, it is spotted immediately and acted on rapidly, rather than saying: "Let's put it in the public inquiry format", which enables a lot of people to say: "Well, we are waiting for the outcome of the public inquiry". That is why I have not recommended it.

Q388 **Wes Streeting:** I can see the argument that says to historic victims of injustice: "Well, there have been some lessons learned, there is a new complaints mechanism in place", which I will come on to very shortly, "and therefore you can take some comfort that were you or other people to be victims in the future there would be a better way of remedying it". I can see how that argument might be posed, but you acknowledge in your report that victims have not had what has been described as something akin to a day in court.

What I find difficult about this in the context of your report is that you say: "It is highly desirable that Britain's banks show a willingness at senior level to meet with those who suffered most from the excesses of 2008-10, to hear their stories and acknowledge their hurt."

This Committee finds it difficult to get a straight answer from Ross McEwan about what happened with GRG. Isn't it naive to expect after everything that has happened, after the miserable excuses that we hear in front of this Committee and the failure of banks to still respond properly to victims of injustice that they are going to read your report and think: "Actually, may be now is the time to sit down and give victims some sense that we have understood and are seeking to put right what has gone wrong"?

It seems to me that they hope that the passage of time will stop the difficult questions and that they can fudge and prevaricate their way through hearings like this and that people forget about it. I imagine they will treat your report in the same way. Why are you not being tougher in your recommendations so that they are properly held to account for the injustices experienced by our constituents?

Simon Walker: I have a lot of sympathy for what you are saying, and I understand the problems and the way in which people have suffered. I just do not think that a public inquiry is the way of achieving that. Frankly, they will all be gone by the time that a public inquiry comes out.

Q389 **Wes Streeting:** You have made that point. I get from your report that you have made an argument about public inquiries that I think has a lot of merits to it, incidentally. But what I see here is a proposal to sit down over tea and biscuits. There must be somewhere between the two.

Simon Walker: It is not over tea and biscuits. I envisage a serious major public event, perhaps chaired by someone who was a previous Chairman of this Committee or someone who had been a Minister, something like that, that confronts the banks with the consequences of their actions at the time of the global financial crisis, which were often disgraceful, but which were generally not illegal and were not generally a breach of regulatory standards which they absolutely would be now.

That is part of the problem with this. We cannot go back retrospectively and put heads on spikes for activity that was not criminal at the time. Frankly, it was mean, cavalier and callous, but it was not against the law. I am not excusing that behaviour in any way: I am just saying there are limits to how much you can act against it. My top priority is to get a system that is fair, fast and affordable for businesses that are faced with this situation in the future.

Q390 **Wes Streeting:** All right. Let us turn to your proposals for the future. How many victims of GRG would have been covered under the expanded access to the FOS that you propose?

Simon Walker: I don't know the answer to that, because, inevitably, I don't know the size of all the 5,000 or so cases that came to GRG—I suspect it is a good number. The critical thing is that under the senior managers regime that the FCA now has, all that GRG activity would be actionable if it took place now. That is a big change since the global crisis.

I am not excusing the behaviour that took place then; I think the banks should be ashamed of how they acted in many cases, but I don't think that should stop us devising a system that works for the situation we face now. Most importantly, that system should pre-empt any bad behaviour next time there is a financial crisis—the one thing we know is that there will be one. I want to get a process in place in time to ensure that it is not SMEs that suffer first—because they are the easiest targets—the next time there are problems of this sort.

Q391 **Wes Streeting:** Okay. Notwithstanding the lack of detail on how many businesses would be covered by expanded access to the FOS, your report acknowledges that even after expanded SME access to the FOS there would still be a gap in the market for dispute resolution. You propose that banks create a voluntary scheme for businesses, but you do not propose a great deal of detail on how that scheme might operate. Could you elaborate further on how you would imagine that scheme to work in practice?

Simon Walker: The simplest thing to me would be for the business end of what I am proposing to have its jurisdiction raised to £10 million in turnover, and to possibly, in time, move up to the EU definition of SMEs, which is considerably higher. If you have confidence in the system as it evolves, the aperture should be as wide as possible, because—

Wes Streeting: I am asking how the voluntary scheme would work in practice.

Simon Walker: That has to be a decision for the FCA and the FOS, but my preference would be for the new business wing of the FOS to take it on and to operate up to £10 million, with that expanded compulsory award capability. That has to be a matter for other people; I cannot just order that.

Q392 **Wes Streeting:** So you don't wish to see a voluntary redress scheme in place.

Simon Walker: The banks would have to say, "We will observe this power for companies with turnover of up to £10 million." They would have to do that on a standardised basis. In practice, they do that anyway quite often.

Q393 **Wes Streeting:** Forgive me for pressing on this point, but I want some clarity. It may be because this is hot off the press that I have misunderstood, but my understanding was that you propose in your report that banks create a voluntary scheme for businesses with a turnover of between £6.5 million and £10 million. You are saying that your preference would actually be for the FOS to cover up to £10 million. There appears to be a discrepancy between what you are saying and what is in the report.

Simon Walker: I don't think so.

Q394 **Wes Streeting:** I just want to understand how you would envisage the voluntary scheme working.

Professor Hodges: The FOS currently operates under two bases: one is the statutory scheme and the other is a voluntary jurisdiction to which the banks already subscribe. The process of how the FOS operates is the same, but the rules are different. Mr Walker is simply saying that you expand the rules of the voluntary process, because it takes too long to get legislation, and the banks should voluntarily subscribe to that.

Q395 **Wes Streeting:** May I ask, then, why you have focused coverage of the scheme on the turnover of the business rather than on the size of the claim? You can understand why, for claims of certain values, even low millions, there would not actually be huge incentives to take this to a legal process, where the costs are remarkably high and the risk is higher. Why have you not instead taken an approach that looks at the size of the claim and makes decisions about where it might be appropriate to take such a claim?

Simon Walker: If there is a very large company that has its own legal capability and legal advisers, then legal remedies are available to it. I suppose my attention is really around businesses that can't afford expensive legal advice, where it is either too expensive or it's such a distraction of time for the business that they can't engage in it. That is my principal focus; the number of employees is also relevant here.

Boundaries are always very difficult but one has to have them and this seems to me to be the best shot. Ultimately, you could go to the EU definition, which is €43 million or 250 employees, if you wanted to raise it higher. I would say let's get a system working first before we consider that expansion.

Q396 **Wes Streeting:** Finally, Professor Hodges, your contribution to the report states that SMEs "may be confused by having too many options in dispute resolution". I have already had an exchange with you this morning about my understanding and clarity around what you mean when you talk about voluntary schemes.

Do the proposals that have been outlined by Mr Walker satisfy your concerns around simplicity and having channels that are easily understood, so that SMEs are able to access the right complaints or disputes resolution mechanism, or do you think there is a case for further simplicity?

Professor Hodges: No. I think that this is the right solution. The comment that you quoted was my response to a suggestion that we should have courts, the FOS—which already exists, so it just expands that bubble—but also a tribunal. It seems to me that that confuses things too much. There are various other reasons as well.

You then have too many sources of law—or sources of precedent, if you like—being created. There is confusion between the decisions and between the pathways. My major concern on confusion is actually the very considerable number of ways in which SMEs can get advice and assistance, or the number of regulators that they have to deal with.

It seems to me that focusing effectively a new business FOS will help with wider rationalisation on the side of too much advice. I would like to see that rationalised very considerably in order to provide much clearer support, bearing in mind that one of the reasons that the ombudsman system as a whole is regarded as being internationally leading is that it provides not just dispute resolution but provides data, which is a point that Mr Walker has already made.

Where does the data go? At the moment, from the Financial Ombudsman it goes to the banks, the public and the FCA. On the business side, it could go all over the place, so I would like to see that support and regulatory landscape reviewed quite significantly.

Q397 **Rushanara Ali:** Good morning. I want to focus on the idea of tribunals. Both you and the FCA concluded that even with an expanded Financial Ombudsman Service, there remains a gap in the market for larger SME disputes. The FCA has repeatedly stated that it supports the creation of a financial services tribunal to fill that gap, whereas you recommend that the banks create a voluntary redress mechanism.

I read through some of your thinking behind it and an inherent aversion, perhaps, Simon, to tribunals. You have talked about how the balance falls in favour of complainants rather than institutions—the employer or, in this case, the banks—and some of the rationale for why you think that is not a good idea. Can you say a bit more about that? You seem to have had a predisposed view on this, as opposed to really thinking about the fact that many of the customers are small businesses. You have documented here the experience of the RBS scandal and others, and also more recent cases such as the TSB technology failure that has led to 100,000 complaints in the space of days. There are still tens of thousands of outstanding complaints and people do not feel confident that the FOS can cope with the additional demands that will come, even with the things you are saying. The tribunal idea presents a credible alternative; why are you so averse to it?

Simon Walker: I don't think I am opposed to tribunals per se. I am hesitant about anything that will require the employment of lawyers and the engagement of lawyers in court processes, just because of the expense and the likely delay that all that will lead to. Being able to do things quickly and with a minimum of legal input seems to me an asset. If I could say so, there are already cases from the FCA, as Professor Hodges points out, that go to tribunals. The average length of time for those to be sorted out is just over four years and the average cost is nearly three quarters of a million pounds, or £712,000. That is an awfully expensive way. The indications are not good in that sense, and that is my first concern.

My principal feeling, however, is actually a positive one about the ability to make a judgment on what is fair and reasonable, as opposed to having to go on the strict legality of what a contract says. That seems to me an enormous plus for the business. From my previous example, the fact that a court or a tribunal would have to rule in favour of a bank that had ruthlessly enforced a loan-to-value ratio that had fallen marginally below what was required seems to me quite decisive. Those were practical examples. Very few people I met suggested that the banks had broken the law, but they often said to me that the banks had behaved in an unreasonable fashion. A tribunal can only weigh up the law—that is important—but also, tribunals, like courts, are not there to provide data. Ombudsmen are there to provide data. That is what they do: they feed data through to the regulator.

Q398 **Rushanara Ali:** But, with respect, the regulator is saying that this idea of a tribunal should be considered and you have ruled it out. How does that fit? I don't really understand. Secondly, "reasonable and fair" is not what has been going on. The APPG has recommended a tribunal. You are coming up with a solution—and it sounds as if it is a pragmatic solution—to addressing the other complaints that fit within the framework and parameters set by the FCA for the FOS. It might work—I say "might" given some of the issues raised so far by colleagues and what we have heard over the last year about the FOS's troubles and how it copes with more responsibility—but even if that were the case, you have suggested some recommendations to try to bolster what it does. Why could you not explore properly what a tribunal approach might look like, taking into account some of the points you are making about fair and reasonable versus the more legalistic approach to tribunals? Why didn't this inquiry look much more at, and investigate much more, what would be feasible that would redress the power imbalance that you talk about in this report at the moment, that is still tilted in favour of banks? It is just not good enough.

The problem is that we have spent years addressing the historic problems. There are a whole series of other problems that have already emerged and are probably going to grow—for instance the implication of technology failures. Some of them will be for businesses, small businesses—we have already seen some of those examples—and large amounts of money. With respect, what you are proposing feels quite timid and I just want to know why it is that you didn't look at this much more thoroughly as a potential option and set out how you might mitigate some of the concerns you are raising.

Professor Hodges: Perhaps it would help if I set the scene. At the moment we have courts that decide on law. We all know they are expensive and slow. That is in many ways why, in the consumer area, ombudsmen came into effect. The ombudsmen have a different jurisdiction—a wider jurisdiction, which is "fair and reasonable". The other facet of the ombudsmen is that unlike courts and, indeed, unlike tribunals, ombudsmen collect data and feed it back, and we are getting better at doing that. So they are part of the regulatory system as well as the dispute resolution system.

It is said that there is a gap for companies that do not have the money to go into the court system and have lawyers. It is difficult to find data on exactly how much the court or the tribunal system would cost, but it is not cheap, whereas the ombudsman system is free to applicants, because the banks pay. So that is one advantage, and it is much quicker as a process. In the gap, it is also clear that extending the idea of the protection of "fair and reasonable" is a good idea, and the APPG came out with a proposal that proves the point that you don't want a tribunal that applies the law; you want a tribunal that applies the "fair and reasonable" test. A slight concern, which is mentioned in my report, is that if you have a tribunal it is going to involve lawyers. The banks are going to have lawyers. You are on the back foot if you don't have lawyers. You haven't got the money to pay for them, and it is going to take some time, but also the lawyers are going to argue about the extension of section 138D of FSMA, which is only going to complicate things, whereas you can't if you are in the ombudsman system.

What we have at the moment is the FCA are saying, "Let's extend"—or they will extend—the ombudsman system. Mr Walker is saying, "Let's extend it even further," so the question is: what are you left with? Frankly, one would expect that any SME in the current gap would opt for the ombudsman route. It would be quite illogical, for reasons of cost, delay, finance and "fair and reasonable" to go the tribunal route. So the question is: what is the size of the remaining gap? As Mr Walker said at the start of this session, it is probably very small. So what is the justification for doing it? That is not off the table, but equally it is also true that although the FCA said "We are not against a tribunal," they have not proposed what it would look like.

Rushanara Ali: You talk about a halfway house approach. Can you say a bit more about that? What would a halfway house between a tribunal and the ombudsman route look like? You talk about legal costs. We have heard in evidence sessions with victims of the GRG scandal and others that they didn't have confidence in, or were not eligible in many cases to go to, the ombudsman because of the limits, so a process that is clearly independent and in which they trust would be much more significant for them. And is there not also a care for looking at how those fees are paid? Did you explore that?

Let's go back to look forward. Shouldn't the victims of the GRG scandal have had recourse to some sort of legal aid equivalent for their fees, given that it was clear that there was something systemically wrong with the provisions that were made to them? Have you explored how that would be financed so that the risks are not as high, and so on? Has there been much thinking behind that? We had an advance copy of the report, or a summary of it—I do not know how much that is reflected in the overall report. Could you say a bit more about that?

Professor Hodges: I am having difficulty working out exactly what you are asking me, because there were a number of different points there.

Q399 **Chair:** The first and key point was about the halfway house solution, which the report talks about—how that might differ and why it would not involve all the cost, procedure and legality of a financial services tribunal if you are not recommending that. What is the halfway house, and how on earth would that operate?

Professor Hodges: Forgive me, but I do not recognise the phrase "halfway house". What we are talking about is extending the existing ombudsman system.

Q400 **Chair:** Your report states that, "If ombudsman methods fail", you "would not rule out the creation of a new halfway house in terms of judicial processes simply to provide cheaper, quicker and easier alternatives to going to court". We are taking the phrase out of your report, and Rushanara is asking you what that is, how it would operate and how it is any different from not recommending a full financial services tribunal.

Rushanara Ali: With some financial back-up, because you raised that question about costs.

Simon Walker: I understand. That was my phrase, so I, rather than my colleague, probably need to take responsibility for it. I suppose what I am saying is that at the end of the day, if an ombudsman system fails, all options need to be looked at, including a tribunal. But I think that is quite a long way down the track. One reason it is a long way down the track is that it is going to require primary legislation, and I am not sure that that can happen for quite some time.

Rushanara Ali: I don't think so.

Simon Walker: To me, the fundamental point is this issue of fair and reasonable versus strict legality. That to me is the decisive feature. I do not think strict legality is going to help small businesses, because the banks are always going to have better lawyers.

Q401 **Rushanara Ali:** My understanding is that within the existing legal framework—the Tribunals, Courts and Enforcement Act 2007—it would be possible to introduce this kind of tribunal. Isn't it for Parliament to work out whether it should legislate? Perhaps you are overly concerned about our capacity to legislate. If there is the will—the FCA is saying there is and that it should be considered—why are you so averse to it? Why didn't you use this opportunity to set that out as an option, if you are saying it should have been an option, so we do not have do these piecemeal reviews and hear about story after story and scandal after scandal? They are not just historical—there is a new wave of problems coming our way. Only before the summer recess we dealt with the TSB scandal, and I suspect there will be many others. Why are we missing this opportunity to set out all the different potential ways forward, so a different way forward could be enforced straightaway if that were necessary? We could legislate if we needed to, but I do not think we need to.

Simon Walker: I am not crusading against a tribunal. I do not think the FCA is actually endorsing a tribunal—it says it is willing to consider it. I am saying that, of the options available, creating a separate pillar within the ombudsman structure is a better deal for SMEs, because it does not require lawyers.

Rushanara Ali: I accept that.

Q402 **Chair:** May I ask two questions following on from that? I think you just said that the FCA does not support the creation of a tribunal. I think they do, don't they?

Simon Walker: I said they are not campaigning—they say they are open to it—

Q403 **Chair:** They are not campaigning for it, but they do support it.

Simon Walker: I am not sure that they do. I think they are open to it.

Q404 **Chair:** I thought they had repeatedly stated that they support the creation of a financial services tribunal to fill that gap, but I will get someone to check the record. I do not know whether you have had the chance to see what was written by the All-Party Parliamentary Group on Fair Business Banking, who welcomed your report in recognising the "massive power imbalance" but are concerned as to whether you have reviewed their conclusions. Have you looked at them? As you mentioned, they have set out a proposal for a tribunal solution and then they say this: "Inexplicably, Mr Walker dismisses a financial services tribunal as simply being popular with politicians. It is also supported by senior members of the legal profession, many banks, the regulator and most importantly victims." What is your response to that phrase?

Simon Walker: I have not seen it. I did not dismiss it as simply being "popular with politicians". I said that one reason that employment tribunals were liked was that politicians like the feel of employer v employee representative with a lawyer in the middle. Employment tribunals are a proposed model. I think there is a lot wrong with employment tribunals, though that is not for this forum. I will not go to the stake on my opposition to tribunals, but I am saying that it is a much more practical remedy and it will benefit businesses. The advantage that I can see in tribunals is that there is not a "loser pays" principle, so if you lose your case you do not end up paying the bank's lawyers' bills as well. That seems a fairly marginal advantage for creating a superstructure that will cost many millions of pounds and will be a new bureaucratic facility.

Q405 **Catherine McKinnell:** The Chair slightly picked up on a few issues. I wanted to ask you a few questions about the response of the All-Party Parliamentary Group on Fair Business Banking to this report. They said that "It will provide a piece of the jigsaw but taken alone the recommendations are not enough." Do you agree with that summary?

Simon Walker: I think the proposals I am putting forward will take us a very long way forward. Will they solve everything? No they won't, and there is no system that is going to be perfect, and there is certainly a backlog of people who were shamefully treated where a remedy is very hard to arrive at. But I think they will deal with the overwhelming bulk of cases involving SMEs. To me, that is the advantage that they have. We could put this in place rapidly and it would not involve a further use of taxpayer expenditure, and the facility is there: it just needs to be redeployed and that can be done relatively easily. In many ways what I am talking about is a practical remedy. I keep going back to this point about being fair and reasonable, and that seems to me to be a huge advantage. So many people complained to me about how badly they were treated, but had to acknowledge that there was nothing illegal. I do not think a tribunal is going to be able to stop that.

Q406 **Catherine McKinnell:** On that basis, do you think that your recommendations will satisfy the groups campaigning for change in this area, such as the SME Alliance and the All-Party Parliamentary Group on Fair Business Banking? If so, why or why not?

Simon Walker: I do not think my proposals are going to satisfy any individual entity, and that is why I did it as an independent review in which I talked to a great many people with many different opinions.

Q407 **Catherine McKinnell:** So you do not think they are going to satisfy anybody?

Simon Walker: I would not say that. Everyone—if they look at it—will see that in the round my proposals would provide a viable system that could work in the short to medium term. How well will that work? Are we going to need something more? We are going to need to wait and see. That is probably only going to be tested next time there is a financial crisis, because that is what exacerbated the situation last time—but I do have confidence in what I am putting forward as something that is viable and that will help the sort of SMEs that at the moment just do not have the ability to go to expensive lawyers. I am afraid tribunals are going to need that as well.

Q408 **Catherine McKinnell:** With all due respect, I have to say you do not sound entirely confident about your own recommendations. You talk about the short to medium term, but that is not going to actually make any of the people campaigning for change in this area happy or feel confident in the recommendations that you are making. How do you give the reassurance that this is a report that is going to bring some resolution for the people campaigning for change and for the constituents who have come to us? How do we sell this to them?

Simon Walker: I can understand that. I believe that my system offers very good redress now and into the future. You are never going to be able to put things right for many of the people who suffered at the time of the financial crisis. I am afraid that that simply is the case. They were treated very badly in many cases, and there is not much that can be done about that. I have said how disgracefully I think the banks acted at the time. I am afraid I am producing a legacy remedy for people whose cases have not been adjudicated. For people whose cases have, there is not much I believe that can be done, because there was no illegality.

I am sorry to sound equivocal on that case, and I take the point that Rushanara made about why there was no redress for people who were so poorly treated at the time of GRG and RBS and that there wasn't legal aid or anything else. I understand and sympathise, but you cannot retrospectively create an ad hoc system for that situation, partly because there was no law broken. People were just badly treated and I am anxious to make sure that they are not badly treated again. I do believe that the remedies I am proposing would help enormously if SMEs are faced with the consequences of technology failures, for example, and the current problems that the banks face. As I have said and as the statistical outline says, there are an awful lot of complaints about banks now.

Q409 **Catherine McKinnell:** You put a fair amount of weight on banks expressing regret and committing themselves to an era in which they do not repeat the behaviour and the mistakes. I think many victims will feel that they have heard that all before. I want to put a question to you, Mr Hodges. The report says: "Victims who feel that an apology is insincere or formalised will not accept it, and it may deepen their motivation to continue to fight." Do you have concerns that Mr Walker's proposals could actually make things worse?

Professor Hodges: No, I do not think that this is going to make things worse. What we are trying to do is to attempt to provide a solution, first, for the future. Secondly, in relation to the past, there are people who may feel that they will never feel better. Looking at a great deal of research on the process of mediation or other ways of solving emotional harm, as I have set out—there are quite a lot of examples of that—it does seem to me that the process such as Mr Walker has recommended is capable of helping. It may not help everyone, but it ought to help quite a lot.

Q410 **Catherine McKinnell:** Help in what way?

Professor Hodges: It is one thing for a bank to take out a full page ad in the *FT* to say, "We're terribly sorry." It is another thing to look people in the face who are saying to you, "I've really been hurt. I've lost my business, my family, my home. I'm feeling terrible. I am bankrupt," and so on—to allow them to express that and to look them in the face and say, "I'm really sorry." That is the process.

Q411 **Catherine McKinnell:** There is another issue for an awful lot of people who have suffered misconduct. Yes, they are hurt; yes, it has hurt their family. For many of them, it has completely changed their life, and for many, it has affected their health as well. But somebody made a lot of money out of that suffering, and I think that is what is very hard to reconcile. For many people, listening to that and acknowledging it is not enough.

Professor Hodges: I cannot think of many legal systems in which you then select particular victims for money remedies over and above what the law requires.

Q412 **Catherine McKinnell:** I am not necessarily talking about money remedies. I am talking about being very sorry, but also acknowledging that there were victims of that misconduct, and there were also people who made a lot of money out of it.

Professor Hodges: Absolutely. That is part of the "really sorry" process. One says, "Yes, really bad things happened and various people benefited, and we want to set up a system where that does not occur again." One of the exemplars for this situation comes from NHS patients, where it is very clear that they may not be particularly interested in money, but they want facts, they want to know what happened, and they want a genuine, look-you-in-the-eyes apology. They also say quite regularly, "We don't want it to happen to anyone else."

Now, we are not good at that, but this is an opportunity to put in place a system that can identify problems and is accessible. You can go there quickly and it will sort out problems, but it will also create data and send it back within the behavioural and regulatory system to say, "We are going to try to identify problems much more quickly in future, and respond to them." That ought to give quite a considerable amount of reassurance that this is an integral element.

Q413 **Catherine McKinnell:** I understand that analogy, and I did note that in your report. However, the point I am making is that in an NHS inquiry, there will have been dreadful failings that need to be addressed, apologised for and accepted, and changes will need to be made so that those failings never happen again, but somebody did not make a lot of money out of the suffering of others. It is not necessarily about giving money as a redress, but I think what makes it very difficult to move on from these cases is that those banks made a lot of money out of the suffering that was caused. That is what makes a more open, transparent tribunal service much more appealing. People can put their trust in that proposal more than they can trust more of the same, which they have already seen.

Simon Walker: With respect, we could not have a tribunal that goes back and looks at the incidents of that era, terrible though they were. We have to try to come up with some sort of remedy; something that will help. You are absolutely right that a lot of people lost a lot of money, and most of all, the taxpayer lost an enormous amount of money. My particular concern is that SMEs suffered grievously in that period, because they were often relatively easy targets, and that is what I want to stop happening in the future. It is really important that the relationship between banks and the SME community is normalised. SMEs need to be able to borrow and get working capital to be able to fund themselves for growth, and not a lot of that is happening at the moment.

While it is terribly important that we say how terrible those events were and try to put them behind us, I am keen that we move on to a situation where we have a remedy vehicle built for the future, not for these past misfortunes—these past tragedies—which I fear often cannot be put right. I very much regret that situation, but because laws were not broken, I cannot see a way around that, and I do not think anyone else can either. This country rightly does not like retrospective legislation, and I do not think anyone would see that as appropriate.

Q414 **Mr Clarke:** I want to focus on the viability of what you have been recommending regarding the expanded role of the FOS. On page 51 of your report, you note, "The Service does not currently provide a viable forum for an expanded volume of financial business complaints…It needs reshaping and reinvigorating". I think everyone the Committee has heard from would say that that is a very British understatement about the nature of the current lack of grip, which the FOS is being criticised for. What specifically do you want to see change, and what is the timetable by which you would expect that to be in place for us to have confidence that it is able to step up in the way you are recommending?

Simon Walker: I suppose point 1 would be bringing in the legal and banking expertise in the advisory group that I propose setting up to try to infuse that into the FOS.

The second pillar of the FOS, which I would aim at business, would be to bring in new people. Instead of winding up the FOS in staff terms and reducing it significantly, as is planned when PPI closes down—that is the current planning—my suggestion is to maintain those staff levels and that resource input, but move it into business-related expertise, where you have got people who can sort out often highly complex problems.

The third thing is the FOS website—I recommend that you go on to it and just looks at it—which is not geared to people who are running businesses. That needs to be done. We need something that says, "This is for you if you have got a dispute with your bank." That would be stage 3.

I think the FOS recognises some of its failings. I am conscious that Richard Lloyd, who is potentially a harsh critic, didn't say, "Wrap the whole thing up." I am also conscious that there is an awful lot of money and resource there, and I think it could do much better.

Q415 **Mr Clarke:** Is the leadership there? In the end, all these organisations rest on whether they have got the requisite drive from the top.

Simon Walker: I think there is leadership there. I have talked to the chief executive, and I think she is very conscious of what we are talking about. I know that they are, in any case, enhancing hugely their data abilities at the moment. Do I think it needs more? Yes, of course. Do I think that the current chief executive and the senior leadership can provide that? Yes, I do. I think they need help, guidance and expertise in what are often highly technical areas that, frankly, any of us would have difficulty grasping.

Q416 **Mr Clarke:** Would you recommend that there be some kind of periodic review of whether the expanded FOS is, for example, delivering against a series of metrics that business might reasonably expect? It seems to me that we are taking an awfully big punt on this organisation being able to transform its standing in the eyes of people who really will rely on it.

Simon Walker: I completely agree. I think there should be a body set up to monitor it, and I think it should include people from the all-party parliamentary group. It should include the leading critics of the institution as it stands at the moment.

Q417 **Mr Clarke:** Is that a formal recommendation in your report? Forgive me—it is so hot off the press that I have not had a chance to go through it.

Simon Walker: I think I do recommend a regular review body that would meet six-monthly. If people want to turn that around and make it report three-monthly or whatever, I am perfectly happy with that. Does the system need close monitoring? Absolutely, and on quite a technical level that pursues questions such as whether it is actually reaching the business community, because they need to know about it.

Professor Hodges: Just one point, which to some extent draws on Ms McKinnell's point. The FOS has the ability to establish its own procedure. Indeed, the oversight committees of various sorts that Mr Walker is talking about could influence that. If one is looking at trust in the process, one shouldn't imagine that exactly the same internal procedure that is entirely appropriate for consumers would apply to SMEs. There are a number of ways within which that can be developed. That may go to the issue of trust, transparency, visibility, etc.

Q418 **Chair:** May I just ask Professor Hodges to qualify that? You said that it can set its own procedural eligibility criteria and how it operates, but there are some restraints to its procedure, aren't there? Could you set those out? It is right, isn't it, that despite the fact of transparency, it would have no power to compel witnesses to attend.

Professor Hodges: It does already. It can give directions—

Q419 **Chair:** It can give direction, but it cannot compel.

Professor Hodges: —as to what evidence is required and the extent to which that is oral or written. It does not usually do that in straightforward consumer complaints because it does not think it needs it, but it has the power to do that. So you can envisage a slightly different process, which is designed for the type of problems we are looking at here.

Q420 **Mr Clarke:** In terms of the FOS's fitness to administer its role on the basis of your recommendations, a second aspect would be the binding award limit. On page 49, you set out how you broadly endorse the FCA's strategy of moving to a £350,000 threshold from 1 April 2019. The all-party parliamentary group on fair business banking suggests that 90% of the complaints it deals with fall outside the Australian threshold, which you set as the long-term goal, of £600,000. Is it not the case that, almost by definition, your solution will not catch a lot of the cases that are attributed? Is that a fair criticism?

Simon Walker: With respect, the APPG's cases are largely historic. That is not to say they ought to be downplayed or in any way criticised, but they are not the issues that are arising today. Most of the issues that arose as a result of the global financial crisis involved commercial property—loans that were taken out that simply would not be available today. So there is no prospect of small and medium-sized businesses borrowing, as they did, ahead of a property crash on a highly unsecured basis and then being pounced on by banks that need to clean up their balance sheets. That is why I understand and deeply sympathise with and have met a lot of the victims of that era. However, that is not happening now. I would be more inclined to go along with the FCA's judgment that we are really talking about 50 or so high-value complaints per year that would be getting to this body. Even if that rose somewhat, we need an organisation that can cope with it. My concern is next time rather than now, but we have got to have a system that is fit for purpose now.

Q421 **Mr Clarke:** Given that lending protocols and habits will fluctuate, there may well be a more risk-on approach in 10 years' time. It is hard to conceive at the moment, but potentially we could return to a much more adventurous lending mindset. Is it not better to have the threshold higher in case that were to materialise? Why limit yourself in that way?

Simon Walker: It is very much a matter of individual judgment. To me, anything above £600,000 feels as if it needs formal, legal imprimatur. You can argue where that point is, but there comes a point that requires a court behind it. I am just as worried as you are about adventurous lending practices in a few years' time. That is why this monitoring process is so important. A lot of what I heard was about businesses with a turnover of £30,000 a year being advanced loans of £250,000 in order to buy into commercial property at a time when that looked a good bet. I don't want to see that coming back and I hope we have regulators that will stop it from coming back. When I was at the Institute of Directors, which was the period from 2011 to 2017, a lot of my members would come to me and say, "Why are the banks being so mean?" "Why can't we party like it's 2006?" I used to say that there are very good reasons why we can't party like it was 2006, because look what that did. Having something that monitors and stops that happening is vital.

Q422 **Mr Clarke:** Why do you only use Australia as the benchmark, then, in terms of setting that £600,000 threshold? It is the only benchmark that you cite specifically in the report.

Simon Walker: Professor Hodges' section covers quite a few other countries as well. Australia has had a major scandal that is much analogous to ours, in many ways—except that it is about lending on farms as well as lending to businesses—where its banks behaved in a predatory way. It has reviewed the whole thing via a Royal Commission that reported back within a year; it was charged with doing that extremely rapidly and has come up with detailed recommendations. If we can borrow some of those—and I think I suggest borrowing some of the others as well—let's do it.

Q423 **Mr Clarke:** Professor Hodges, are you aware of other jurisdictions that do set a higher limit?

Professor Hodges: Yes; I am just looking at random at the new Netherlands approach, with the financial ombudsman in effect, which claims up to €1 million—

Q424 **Mr Clarke:** Without a court involved?

Professor Hodges: Yes, people don't use courts, they use the ombudsman system: that is the direction of travel.

Q425 **Mr Clarke:** So there is precedent that we could go higher still?

Professor Hodges: The number is a matter of judgment. There is no magic in any number.

Q426 **Mr Clarke:** That is helpful. Thank you very much.

The APPG report on fair banking for all also recommended including banks in the conduct of business rules, which would require you to treat your customers fairly. Do you think that that would have merit as a concept? Why was that not a recommendation that has been endorsed?

Professor Hodges: The point there was to what extent the conduct of business rules—as I understood it, the argument was to extend section 138D of FSMA so as to give someone who had suffered a breach of the conduct of business rules the right to bring a claim in a tribunal. The APPG would say the answer is a tribunal. That is as far as I understood it, without looking at the ombudsman system. Mr Walker—and I support him—is saying, "Actually, most of the answer is an ombudsman." That is for a number of reasons.

Where we absolutely agree and coincide is that the jurisdiction ought to be fair and reasonable. Their argument was that we can get "fair and reasonable" in by amending section 138D

Q427 **Mr Clarke:** And you consider that the ombudsman route allows the full factoring in of "fairness"?

Professor Hodges: If you wanted a tribunal and wanted it to have "fair and reasonable", that would be the mechanism for getting it in. As I said earlier, I actually think that doing that would open the door to more legal arguments, which would put up the cost and make things more complicated. That is not a technical issue that arises within the ombudsman system. But that is simply the point: senior management etc. rules apply holistically.

Simon Walker: If I may add to that, the senior managers' regime would now enable the FCA to act if, for example, a bank acted in breach of the Lending Standards Board to which it was signed up, which is one reason that I would like to see all institutions signed up to the Lending Standards Board's guidelines for lending, including the organisations to which debt is sometimes onsold. That is a serious problem. The senior managers' certification regime with the FCA has given the FCA an awful lot more power now to act if a bank behaves unfairly, and over matters not just of direct behaviour, but where senior managers ought to have overseen and spotted misbehaviour. That does give them powers that I hope they will be using.

Q428 **Chair:** Thank you both very much for coming before us today. I have two final points. One of the great joys of being in the Chair, albeit temporarily, is that when one seeks inspiration it arrives. The Financial Conduct Authority policy statement, "SME access to the Financial Ombudsman Service", on 16 October this year, says, "We have publicly stated our support for a tribunal". It goes on to say, "We see a role for both an extended ombudsman and a tribunal, as they meet different needs".

The FCA has been reasonably clear in its support for a tribunal to sit alongside an ombudsman system. I take it, Mr Walker, from what you have said this morning, that you still believe that an ombudsman system is a preferable route.

Simon Walker: That is my view. I am certainly not going to war against a tribunal. I just see it as a longer-range and, in my view, less useful vehicle for SMEs.

Q429 **Chair:** In response to one of your questions to Mr Hosie, I think you were saying that for practical reasons there had to be a time limitation to access to redress. Were you clear about that? Is that what you were trying to say?

Simon Walker: For the past or for current cases? The Financial Ombudsman Service at the moment operates a kind of six and three-year time limit, where something has to have happened within the past three years, but six years if the original cause of the complaint happened in the past six years and someone only became aware of it in the last three years—I think I've got that right. That sort of parameter seems sensible to me. There comes a point at which you cannot go back for decades.

Q430 **Chair:** The point that I suppose one would challenge you on is that the financial crisis was in 2008, which is now 10 years ago, and therefore if you are saying six years, there is a limitation to redress.

Simon Walker: Yes; that is why I am suggesting that limited exception to deal with legacy cases that have not been dealt with. There are quite a number of those, and I believe that the banks have an obligation to set that in place.

Q431 **Chair:** Finally. Professor Hodges, I found this quote: "It may be argued that tribunals, unlike ombudsmen, can summon witnesses and require documents to be presented. Ombudsmen can only request data and attendance, although they can draw an adverse inference from a refusal". Is that correct?

Professor Hodges: Yes, although one can go further because, as I said earlier, the ombudsman actually has power under the rules to, in effect, require people and documents to turn up. As I said, it incredibly rarely does that, but the power exists. Technically, although the powers between a tribunal and an ombudsman are expressed in different words, the function is pretty similar. Even under a tribunal or a court, the court would say, "I want you to produce these documents or this witness."

Q432 **Chair:** So it can definitely produce the documents, but it cannot compel a witness—is that the point? But it could draw inference if a witness refused to appear.

Professor Hodges: You can always do that. To some extent that quote was given to us by Sir William Blackburn within his ADR scheme about drawing adverse inferences. As far as evidence from the banks is concerned, if the ombudsman said, "I want to see this, or this person," it would be very difficult for the bank to wriggle out of that, because of the regulatory regime.

Chair: Gentlemen, thank you both very much for coming. Yet again, I extend the Chair's apologies for not being able to be here this morning. Thank you for your time.