

## Consultation Response

### **Which? response to Financial Ombudsman Service's *2022/23 Plans and Budget Consultation***

#### **Summary**

- **Which? welcomes the Financial Ombudsman Service's consultation on its plans and budget for 2022/23.** The Ombudsman plays a vital role in the financial services industry, providing redress for consumers and working with industry and regulators to prevent consumer detriment from arising. The upward trend in the volumes of complaints to the FOS supports the need for further investment in the service.
- **We support the Ombudsman's priorities to enhance its service, prevent complaints and unfairness from arising, and build on its capabilities.** We are particularly supportive of the FOS' preventative work, including the sharing of insight on consumer issues and the causes of complaints. Which? recommends that the Ombudsman should regularly publish comparative, firm-by-firm data on more detailed and relevant areas including authorised push payment (APP) scams.
- **The FOS should ensure that offers made in proactively settled complaints are fair to consumers.** We appreciate the urgency at which the FOS is working to address the backlog of complaints. For the most part, the backlog is the result of wider trends and poor firm practices. Under the FOS' temporary changes to reporting the outcomes of proactively settled complaints, the FOS should continue to deliver on its commitment to review the fairness and reasonableness of any proactive offer made by firms.
- **We continue to support a budget that provides a free, high-quality service and fair outcomes for consumers.** The funding system should ensure that the FOS can invest in its key priorities and provide strong incentives for financial services firms to get things right the first time.
- **We expect significant levels of financial disputes between consumers and firms in the areas of scams and general banking provision, and a growing number of complaints in buy now, pay later (BNPL).**
  - The growing complexity of scams is leading to widespread consumer harm, while the inconsistent implementation of the Contingent Reimbursement Model (CRM)

Code by firms is likely to lead to more APP scam victims challenging banks' decisions on reimbursement.

- As a result of a reduction in the availability of bank branches and free-to-use ATMs, we expect to see a significant rise in the number of complaints made to the FOS from consumers being underserved by banks or facing financial exclusion.
  - We are concerned that the risks associated with the way that BNPL products are currently being used by consumers could persist even once the sector becomes regulated, resulting in a considerable number of complaints to the FOS once the sector falls under its jurisdiction.
- **The FOS should consider the impact of cost of living challenges on levels of demand for its service.** We are concerned that current cost of living challenges will put substantial pressure on people's finances, driving greater use of credit, increasing debt levels, and leaving consumers vulnerable to fraud. We anticipate a rise in complaints to the FOS as a result, including a rise in people in more vulnerable circumstances seeking redress and support.
  - **We expect to see the Financial Conduct Authority's (FCA) New Consumer Duty (NCD) influence FOS caseloads.** With effective implementation and supervision, the proposed Duty could prompt firms to devote more attention to delivering good consumer outcomes and, in so doing, reduce the volume of complaints made to the Ombudsman. However, immediately following implementation of the Duty, there may be a rise in complaints to the FOS as consumers and firms adapt to the new rules.

### **Which? welcomes the Financial Ombudsman's plans and budget for 2022/23**

The financial services market continues to change, as does the volume and nature of complaints made to the Ombudsman. The fact that in 2022/23 the FOS expects to receive approximately 177,000 new complaints and resolve 210,500 cases underlines its pivotal role in providing redress for consumers. While cases involving payment protection insurance (PPI) may now represent a smaller proportion of the cases handled, it is clear that the FOS will see a considerable rise in the number of non-PPI complaints it receives over the coming years. This expected increase in demand emphasises the need for further investment, enabling the FOS to continue to reduce waiting times whilst handling more extensive and challenging caseloads.

**We support the Ombudsman's priorities to enhance its service, prevent complaints and unfairness from arising, and build on its capabilities**



As retail financial markets develop, complaints are likely to become more complex and take longer to resolve. We therefore support the FOS' plans to unlock capacity and capability in its service. Consolidating expertise and investing in technology will not only improve the efficiency of the service it provides, helping to reduce waiting times and tackle caseloads, but could also increase accessibility for consumers and enable the FOS to adapt to changes in financial services both now and in response to future regulatory changes. This will require investment, further reiterating the need for a budget that will support the FOS in making such changes.

We are particularly supportive of the Ombudsman's plans to step-up its preventative work, to help prevent consumer harm before it occurs rather than subsequently relying on redress mechanisms to resolve issues. It is vital that the FOS shares its insight on the issues behind complaints with consumers, firms and regulators to prevent consumer detriment. This can have considerable benefits for both consumers and firms: for consumers, there are limits to a complaints-led system of enforcement, which requires consumers to engage with what can be a daunting process; and for firms, preventing issues arising can help them to better serve their customers and to avoid damaging trust in their brand. Which? therefore welcomes the Ombudsman's recent announcement of the Wider Implications Framework, where it will play an important role in sharing insight, data and trends on salient consumer issues and the causes of complaints with members of the regulatory family.

To improve its preventative work, Which? recommends that the Ombudsman should regularly publish comparative firm-by-firm data on more detailed and relevant areas. The publishing of comparable FOS data alongside data on how they have handled complaints is essential to provide a comprehensive view of how firms are treating their customers and how effective complaints procedures are.

In particular, the FOS does not currently publish aggregate data specifically for APP scams, and does not regularly publish firm-by-firm data for the broader category of authorised fraud. We have called on the PSR to include FOS data as part of its proposals to require firms to publish data on levels of APP scams and reimbursement. We agree with the PSR that firm-level data could be used by consumers to make decisions about which firms they bank and make payments with. We also agree that firm-level transparency will provide strong incentives for firms to do more to prevent APP scams from taking place and to protect customers when they do fall victim.

### **The FOS should ensure that offers made in proactively settled complaints are fair to consumers**

We appreciate the urgency with which the FOS is working to address its backlog of complaints, and commend its continued efforts in almost halving this caseload from 90,000 cases to just under 50,000 cases. Which? acknowledges that, for the most part, this backlog is the result of wider trends such as the pandemic and the poor practices of many financial firms. We therefore understand that through making temporary changes to reporting the outcomes of proactively



settled complaints, industry can help the FOS to tackle this caseload and reduce waiting times for consumers.

Which? responded to the FOS' consultation on proactively settled complaints with a letter outlining our views and initial concerns. We recommended that the FOS should review and assess the offers made by firms to help to lead to fairer decisions, while balancing the need to incentivise firms to change their approach to cases. We appreciate that the FOS has since revised its proposals and has now committed to reviewing the fairness and reasonableness of any proactive offer made by firms to ensure that consumers will be fairly compensated for their financial losses.<sup>1</sup> Which? welcomes and strongly supports this change in approach from the FOS. This is particularly important for victims of fraud, as losses can be life-changing and there is a considerable emotional impact. The FOS should ensure that it continues to deliver on this commitment, and has factored the sufficient time and resources to be able to do so within its plan.

### **We continue to support a budget that provides a free, high-quality service and fair outcomes for consumers**

The Ombudsman's funding system should provide strong incentives for financial services firms to get things right the first time. Appropriate financial incentives must be maintained to encourage firms to tackle the causes of complaints and improve the way they handle complaints. This could, in turn, improve consumer outcomes and reduce the number of disputes received by the FOS. Moreover, the FOS' budget should be able to invest in its service to support its aims for 2022/23 of reducing wait times for consumers, handling increasing demand without allowing queues to grow, and investing in a programme of operational change.

### **We expect significant levels of financial disputes between consumers and firms in the areas of scams and general banking provision, and a growing number of complaints in by now pay later (BNPL)**

#### ***Scams***

Which? continues to see a growing number of scams. In 2021, we received 26% more cases of scams and fraud via the Which? Money Helpline than we had in 2020. UK Finance figures show that there were 106,164 cases of APP fraud in H1 2021, with losses amounting to £355.3 million.<sup>2</sup>

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<sup>1</sup> Financial Ombudsman Service (Nov 2021) Temporary changes to reporting the outcomes of proactively settled complaints Consultation feedback statement, p.8. Available at: <https://www.financial-ombudsman.org.uk/files/316823/Financial-Ombudsman-Service-Feedback-statement-Temporary-changes-to-reporting-the-outcomes-of-proactively-settled-complaints.pdf>.

<sup>2</sup> UK Finance (2021) 2021 Half Year Fraud Update, p.8. Available at: <https://www.ukfinance.org.uk/system/files/Half-year-fraud-update-2021-FINAL.pdf>.

Low reimbursement rates and consistently high FOS uphold rates suggest little change in how firms are treating scam victims. In H1 2021, just 49% of total losses to APP scams were reimbursed by CRM Code signatories, a slight increase from 38% in the previous year.<sup>3</sup> Moreover, since 2019/20, FOS uphold rates for complaints involving authorised fraud have remained relatively constant at around three-quarters.<sup>4</sup> This compares to an uphold rate for all types of FOS complaints of 32% in 2020/21. FOS uphold rates for individual firms for authorised fraud vary significantly, but are as high as 86%.<sup>5</sup> Given the rising levels of scams and continued, low rates of reimbursement for consumers, we expect the scale of authorised fraud to be reflected in the levels of scam-related complaints the FOS receives in 2022/23.

Fraud is becoming increasingly more sophisticated and complex, with fraudsters taking advantage of emerging digital technologies to commit fraud that is harder to detect and more challenging for the FOS to resolve. We have seen the following trends become more common, reaching a wider demographic of people and leading to significant harm for consumers:

- Cases involving remote access software, particularly with fraudsters impersonating banks
- Cases involving number spoofing
- SMS scams (smishing)
- Multigenerational scams
- WhatsApp-based scams, where scammers can pretend to be a close family member or friend of the victim to convince them to disclose financial details or make an authorised payment to the fraudster's account
- Cases involving money sent to cryptocurrency exchanges (though we appreciate most crypto-related cases fall outside the FOS' current jurisdiction)

Therefore, it is vital that the FOS considers complex scams when planning and budgeting: it should ensure that it keeps on top of trends in scams, has sufficient resources to tackle scam-related complaints, and works to develop its expertise to best resolve fraud cases. This is crucial if the FOS is to build its capabilities for the future.

Moreover, the continued inconsistent implementation of the voluntary CRM Code by industry is leading to more APP scam victims challenging the reimbursement decisions made by banks through the FOS. The Ombudsman has previously observed that, overall, firms are applying the reimbursement provisions of the CRM Code inconsistently and in some cases incorrectly, failing

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<sup>3</sup> UK Finance (2021) 2021 Half Year Fraud Update, p.26, and UK Finance (2020) 2020 Half Year Fraud Update, p.24. Available at: <https://www.ukfinance.org.uk/policy-and-guidance/reports-publications/2020-half-year-fraud-report>

<sup>4</sup> In 2019/20, the FOS upheld an average of 75% complaints involving authorised fraud. In 2020/21, this figure was 73%. In Q2 2021/22, the FOS reports that it upheld around three quarters in the consumers' favour. See Financial Ombudsman Service (2021) Annual complaints data and insight 2020/21, available at: <https://www.financial-ombudsman.org.uk/data-insight/annual-complaints-data>, and Financial Ombudsman Service (2021) Quarterly complaints data, available at: <https://www.financial-ombudsman.org.uk/data-insight/quarterly-complaints-data>.

<sup>5</sup> Which? (2021) Banks wrongly denying fraud victims compensation in up to 8 in 10 cases, available at: <https://www.which.co.uk/news/2021/11/banks-wrongly-denying-fraud-victims-compensation-in-up-to-8-in-10-cases/>



to reimburse consumers in circumstances anticipated by the Code.<sup>6</sup> We agree with this view, as Which? continues to be involved in cases of APP fraud where some banks have applied the provisions incorrectly, leading to significant consumer detriment.

Which? is seeing more consumers challenging banks on the effectiveness of their warnings and challenging banks' reasoning and rationale behind decisions not to reimburse victims. While HM Treasury's works to deliver on its commitment to legislate to make reimbursement mandatory for all victims of APP scams, we strongly expect the FOS to receive high levels of financial dispute cases from consumers seeking to challenge banks on their reimbursement decisions.

It is important to acknowledge the ongoing distress experienced by fraud victims, especially for those who have lost life-changing sums. We support the approach that the FOS has taken in holding firms to the commitments they have made under the CRM Code and their wider responsibilities to their customers, and its guidance to individual firms to help them understand the FOS' approach to APP scam complaints where the CRM Code is a relevant consideration. This is important in preventing further consumer detriment.

To improve transparency for APP victims, we reiterate our recommendation that the FOS should regularly publish firm-by-firm data on APP scams. The publishing of this data, alongside data from payment service providers on how they have handled complaints, is vital to provide a more comprehensive understanding of how victims are being treated by firms and in helping to drive better outcomes.<sup>7</sup>

### ***Changes to general banking provisions***

The UK's cash infrastructure is under severe strain: the rapid rate of bank closures since the pandemic and ongoing cuts to the ATM network has contributed to the depletion of the cash network. Which? analysis shows that 736 UK bank branches closed in 2021, with over 220 more planned for closure this year.<sup>8</sup>

This has led to substantial levels of consumer harm. Which? research has shown that more than half (57%) of consumers have experienced one or more issues with accessing cash or a bank branch in 2021, and four in ten (43%) respondents said they had experienced bank branch issues, including the closure of a bank branch they used to visit or reduced opening hours.<sup>9</sup>

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<sup>6</sup> Financial Ombudsman Service (Oct 2020) Lending Standards Board Review of the Contingent Reimbursement Model Code for Authorised Push Payment Scams: Financial Ombudsman Service response, pp.2-3. Available at: <https://www.financial-ombudsman.org.uk/files/289009/2020-10-02-L-SB-CRM-Code-Review-Financial-Ombudsman-Service-Response.pdf>.

<sup>7</sup> See Which? (Jan 2022) Which? response to The Payment Systems Regulator's consultation 'CP21/10 Authorised push payment (APP) scams consultation paper'. Available at: <https://www.which.co.uk/policy/money/3552/consultation-responses-payments>

<sup>8</sup> Which? (Dec 2021) Which? calls on banks to pause branch closures to protect access to cash. Available at: <https://www.which.co.uk/news/2021/12/which-calls-on-banks-to-pause-branch-closures-to-protect-access-to-cash/>

<sup>9</sup> Which? Press Office (August 2021) Crunch point for cash. Available at: <https://press.which.co.uk/whichpressreleases/crunch-point-for-cash/>

While the speed and convenience of digital payments has been welcomed by many, millions of people continue to rely on cash as their sole payment method, with consumers' financial inclusion and independence reliant on maintaining access to cash. Hence, as a consequence of the reduction in the availability of bank branches and free-to-use ATMs, we expect to see a significant rise in the number of complaints made to the FOS from consumers, including vulnerable consumers, being underserved by banks and in many cases, facing financial exclusion.

Recent initiatives from the retail banking industry, such as the commitments made by the UK Finance Access to Cash Action Group are welcome, since they offer support to customers who continue to rely on cash. We continue to maintain that legislation is required to provide a statutory underpinning to such voluntary initiatives, and urge HM Treasury to take prompt action to deliver on its commitment to introduce legislation to protect access to cash. While the scope and format of legislation is still to be determined, it may well provide consumers with a means to challenge banks over the extent to which they make access to cash available. The FOS should keep abreast of developments in this area to consider the potential implications for its service which may arise from new legislative obligations.

### Buy Now Pay Later (BNPL)

Unregulated BNPL products, which currently sit outside the FOS' jurisdiction, continue to gain mass popularity with consumers, with more than 17 million people in the UK having used BNPL services.<sup>10</sup> The industry is growing at a rapid rate, with a proliferation of products being offered to consumers.

BNPL has many potential benefits for consumers. Users cite the affordability, clarity and ease of using products, and that paying in installments can better suit their financial situations. However, through our in-depth research with BNPL users, we are also aware of the considerable risks in the way these products are currently being used by consumers. We have found that consumers lack understanding of BNPL products: most participants did not see BNPL as a form of borrowing, rather a 'way to pay' and a 'money management tool,' and did not conceptualise it for themselves as a form of credit.<sup>11</sup> Furthermore, we found that BNPL users are more likely to be experiencing other challenges, including the expenses associated with raising a family and other life events.<sup>12</sup> While we understand that BNPL products may help smooth costs through these challenging times, these circumstances may also increase the risk these products pose to consumers.

HM Treasury recently proposed the proportionate regulation of the BNPL market and is currently determining an appropriate regulatory scope. However, even once these products become

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<sup>10</sup> BBC News (Nov 2021) More than 17 million have used buy now, pay later services. Available at: <https://www.bbc.co.uk/news/business-59433904>

<sup>11</sup> Which? (Jan 2022) Buy now pay later: understanding and addressing the risks to consumers, p.18.

<sup>12</sup> For more information on our research, see our Policy Report here: Which? (May 2021) Under Pressure: Who uses BNPL?. Available at: <https://www.which.co.uk/policy/money/7601/buynowpaylater>



regulated, we expect to see the risks associated with BNPL persist, at least in the short term, and particularly issues with consumer understanding. Subsequently, we anticipate that this may result in a considerable number of complaints from consumers to the FOS once the sector falls under its jurisdiction.

We strongly support HM Treasury's proposal to give BNPL customers access to the FOS. We acknowledge that this may require the FOS to expand its capabilities and reallocate its resources, but this further reiterates the need for a budget that enables the FOS to invest in its service. The FOS will have a crucial role to play in resolving individual complaints, and more broadly in helping the BNPL industry to treat customers fairly.

### **The FOS should consider the impact of cost of living challenges on levels of demand for its service**

Recent surges in inflation, energy prices and food costs are exacerbating financial hardship for consumers. Our research shows that 2.5 million households missed at least one payment in January 2022. This marks a significant increase on December 2021, when 1.7 million households were estimated to have defaulted on or missed a payment.<sup>13</sup> 56% of people told us they had been affected by higher energy price rises, and 58% had been affected by increased food prices. Of those who had experienced higher food prices, 10% said they had skipped meals.<sup>14</sup>

Which? is concerned that current cost of living challenges will put substantial pressure on people's finances, driving greater use of credit, increasing debt levels and exposing individuals to a higher cost of borrowing. Moreover, financial difficulties could leave consumers more vulnerable to financial fraud, leading to considerable harm.

As a result, we anticipate an increase in complaints to the FOS in 2022/23, including a rise in complaints from people in more vulnerable circumstances seeking redress and support from both the Ombudsman and financial services firms.

### **We expect to see the FCA's New Consumer Duty (NCD) influence FOS caseloads**

Which? welcomes the FCA's proposals for a New Consumer Duty which offers the potential to deliver a step-change in the way consumers are treated by financial services firms. The NCD proposes to set clearer and higher expectations for firms' standard of care towards consumers.

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<sup>13</sup> Which? Press Office (Jan 2022) 2.5 million households missed payments in January as cost of living crisis bites, Which? research suggests. Available at: <https://press.which.co.uk/whichpressreleases/2-5-million-households-missed-payments-in-january-as-cost-of-living-crisis-bites-which-research-suggests/>

<sup>14</sup> Which? Press Office (Jan 2022) 2.5 million households missed payments in January as cost of living crisis bites, Which? research suggests.



Underpinning the Duty is a focus on good consumer outcomes: the FCA expects firms to be continually assessing whether the financial products and services they deliver are meeting the diverse needs of consumers, and to use this as a basis for continued improvement. Firms will need to ensure that their products and services are fit for purpose and offer fair value, and that their communications and customer service enable consumers to make and act on well-informed decisions. Furthermore, the Duty will require firms to ensure that consumers get prompt and appropriate redress when things do go wrong.<sup>15</sup>

It is the poor conduct of many financial firms that is driving FOS caseloads. Therefore, with effective implementation, supervision and, where necessary, enforcement, we believe that the proposed Duty could prompt firms to devote more attention to delivering good consumer outcomes and, in doing so, reduce the volume of complaints made to the FOS. However, immediately following the implementation of the new Duty, there may be an initial rise in complaints to the FOS as consumers and firms adapt to the new rules.

Which? anticipates the Ombudsman will play a vital role in holding firms accountable against the higher standards of the proposed Duty. The early decisions it makes will be influential in the behaviour of firms and crucial to the effective implementation of this far-reaching framework.

### **About Which?**

Which? is the UK's consumer champion. As an organisation we're not for profit - a powerful force for good, here to make life simpler, fairer and safer for everyone. We're the independent consumer voice that provides impartial advice, investigates, holds businesses to account and works with policymakers to make change happen. We fund our work mainly through member subscriptions, we're not influenced by third parties and we buy all the products that we test.

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<sup>15</sup> Financial Conduct Authority (Dec 2021) A new Consumer Duty: Feedback to CP21/13 and further consultation, 1.13, p.5. Available at <https://www.fca.org.uk/publication/consultation/cp21-36.pdf>