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Case No: CO/10619/2010

IN THE HIGH COURT OF JUSTICE
QUEEN'S BENCH DIVISION
ADMINISTRATIVE COURT

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 20/04/2011

Before :

MR JUSTICE OUSELEY

- -

Between :

THE QUEEN on the application of BRITISH BANKERS ASSOCIATION	**Claimant**
- and -	
(1) THE FINANCIAL SERVICES AUTHORITY **(2) THE FINANCIAL OMBUDSMAN SERVICE**	**Defendants**
- and –	
NEMO PERSONAL FINANCE LTD	**Interested Party**

- -
- -

Lord Pannick QC and Mr C Flint QC
Mr J Herberg and Mr S Pritchard (instructed by Freshfields Bruckhaus Deringer LLP) for the **Claimant**

Mr M Brindle QC and Miss M Carss-Frisk QC
Mr R Coleman and Mr J McClelland (instructed by SNR Denton UK LLP) for the **First Defendant**

Mr Hodge Malek QC and Mr J Strachan (instructed by Russell Cooke LLP) for the **Second Defendant**

Mr M Fordham QC and Mr P Luckhurst (instructed by Herbert Smith LLP) for the **Interested Party**

Hearing dates: 25th, 26, 27th and 28th January 2011

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Judgment

Mr Justice Ouseley :

Introduction

1. This case concerns part of the regulatory response to the misselling of Payment Protection Insurance policies, PPI. PPI policies provide insurance against the risk that a borrower will be unable to maintain loan repayments for example when unable to work; they may include life cover. The premiums may be paid regularly or as a single premium. The policies may be sold with or without advice, face to face, over the telephone or in writing. PPI is a profitable and widely purchased product. Its sales have generated tens of thousands of complaints by customers.

2. The Claimant, the British Bankers Association, is the leading association which represents the banks. Banks are among those who sell PPI policies. Nemo Personal Finance Ltd, the Interested Party, supports the claim. It sold over 15,000 PPI policies, directly and through brokers, between 2005 and 2009.

3. The First Defendant is the Financial Services Authority, FSA, the statutory regulator for the financial services industry. Its powers are governed by the Financial Services and Markets Act 2000, FSMA.

4. The FSA has a statutory power to make rules and to issue guidance. It has issued rules called Principles; these are general statements of the conduct required of the providers of financial services. The FSA has also made rules which deal with the manner in which insurance policies including PPI policies can be sold. These are brought together in the FSA Handbook which also contains its guidance.

5. The Financial Ombudsman Service, FOS, set up by the FSA pursuant to powers in the FSMA, handles complaints by consumers. It is the Second Defendant. Since 2006, a rapidly increasing and now very large part of its workload are complaints by customers about the way in which PPI policies were sold to them. It upheld 89 percent of the PPI complaints made to it in the year ended 31 March 2009. Its concern about the way in which PPI policies were sold was formally communicated to the FSA in July 2008.

6. On 10 August 2010, the FSA published Policy Statement 10/12 "The assessment and redress of Payment Protection Insurance Complaints." It comprises what the FSA describes as a "package of measures" stemming from its "serious concerns about widespread weaknesses in previous PPI selling practices" to the detriment of many consumers. The package includes amendments to the Handbook rules, guidance about how PPI sales complaints should be handled and the basis on which they should be decided, and an Open Letter identifying what the FSA sees as common failings in the selling of PPI policies; these failings have inaccurately been termed Standards by the BBA. The measures also include guidance on "root cause analysis", a mechanism whereby those who have not complained may also receive redress for losses suffered.

7. The Claimant challenges the lawfulness of that Statement. The Policy Statement is said to be unlawful because it treats the Principles as giving rise to obligations owed by firms to customers, leading to compensation being payable for their breach, when those Principles are not actionable in law. The FSA says that the fact that breach of the Principles does not of itself give rise to a cause of action in court has no impact on their relevance as obligations, breach of which can lead to compensation.

8. The BBA's main alternative argument on the lawfulness of the Policy Statement is that, since the FSA has made specific other rules governing the manner in which PPI policies are sold, designed to incorporate in their ambit the implications of the Principles to the extent that the FSA chose to do so, it was unlawful for the FSA to provide in its Policy Statement that a customer might be entitled to redress by reference to Principles which conflicted with or augmented those specific rules.

9. The FSA denied creating any conflict, but said that it was entitled to rely on the Principles as well as the specific rules when telling firms and customers on what basis firms should decide complaints about entitlement to compensation.

10. BBA contended that, to the extent that either of its two main arguments were correct as a matter of statutory construction, the Ombudsman was acting unlawfully in publishing and maintaining since November 2008 guidance on its website, the Online Resource, which stated that the Principles would be taken into account in its decisions as to whether compensation would be "fair and reasonable". The Ombudsman submitted that it was obviously entitled to have regard to the Principles in that way.

11. BBA's third main argument, on which Mr Fordham QC for Nemo made the main submissions, was that the FSA's Policy Statement was designed to address what it perceived to be widespread misselling of PPI policies. The FSMA had prescribed a specific statutory procedure in s404 for dealing with this, providing redress for non-complainants, but with safeguards for the firms affected. The informal procedure in the Policy Statement, the guidance on "root cause analysis", was therefore unlawful. The FSA's Policy Statement could not be used with the intent or effect of circumventing that specific statutory procedure with its safeguards or limitations. Moreover, the specific statutory scheme, which was what the FSA had to follow, could not be based on breaches of the Principles since they were not actionable.

12. The FSA submitted that there was no obligation to follow that specific statutory procedure, and circumstances permitted it to proceed as it had done.

Ground 1: The relevance of actionability

The statutory framework: the FSA

13. The Claimant's first submission concerns the relationship between the powers of the FSA to make rules and to prevent them being actionable, and the reliance by the FOS on those non-actionable rules in determining compensation claims.

14. The duties of the FSA are set out in s2 of the Financial Services and Markets Act 2000. Its regulatory objectives include market confidence, public awareness and consumer protection. Its general functions in s 2(4) are making rules, preparing and issuing codes, giving general guidance, and determining the general policy and principles by reference to which it performs particular functions.

15. S138 provides the general rule-making power, which covers regulated activities such as the selling of PPI policies by authorised persons such as the members of the BBA. The s138 rules are known as general rules. S155 requires the FSA to consult on draft rules, the publication of which must include an explanation of their purpose and a cost benefit analysis. Representations must be taken into account, and the FSA must publish a general account of the representations and its response to them. The rules are denoted in the FSA Handbook by an R.

16. An important consequence of contravention of a rule is provided for in s150 as follows:

> "150. – Actions for damages.
>
> (1) A contravention by an authorised person of a rule is actionable at the suit of a private person who suffers loss as a result of the contravention, subject to the defences and other incidents applying to actions for breach of statutory duty.
>
> (2) If rules so provide, subsection (1) does not apply to contravention of a specified provision of those rules."

17. S150(2) is significant in the case since the Principles are FSA rules but the FSA has provided that s150(1) does not apply to them. Other consequences which apply to contraventions of the rules, including Principles, are public censure under s205, and financial penalties under s206. Those consequences are appealable to the Upper Tier Tribunal. The FSA may also seek from the court an injunction to prevent repetition of a contravention, s380, or a restitution order where someone has profited from a contravention or another has suffered loss in consequence; ss382 and 384.

18. S149 enables a rule to be made, known as an evidential rule, contravention of which does not give rise directly to any of the statutory consequences that follow contravention of other rules. Instead, contravention or compliance may be evidence of contravention of or compliance with some other provision of the rules. These evidential rules are denoted by an E in the Handbook.

19. The FSA may also give guidance consisting of information and advice about the operation of the Act and the rules, any matters relating to its functions, and for the purposes of meeting the regulatory objectives. It has to consult about guidance on rules as it would if it were issuing rules, unless urgency makes delay undesirable; s157. Guidance is denoted by a G in the Handbook.

The statutory framework: the Ombudsman

20. The FSA was required by s225 to set up an Ombudsman scheme: *"under which certain disputes may be resolved quickly and with minimum formality by an independent person";* s225 (1). The Financial Ombudsman Service Ltd is the company set up by the FSA to perform that function. It has a compulsory and a voluntary jurisdiction; I am concerned with the former. The effect of s226(1) and the compulsory jurisdiction rules made under it is to bring a complaint relating to an act or omission of an authorised person, such as a BBA member in carrying on the activity of selling PPI, within the scope of the compulsory jurisdiction of the Ombudsman. Under the procedural rules made under Schedule 17 paragraph 13, the complaint must not be entertained unless the complainant has previously communicated the substance of the complaint to the respondent firm and given it a reasonable time in which to respond.

21. S228(2) is crucial:

> "(2) A complaint is to be determined by reference to what is, in the opinion of the ombudsman, fair and reasonable in all the circumstances of the case."

22. Where the complaint is determined in favour of the complainant, the determination may include, at s229(2):

> "(a) an award against the respondent of such amount as the ombudsman considers fair compensation for loss or damage…suffered by the complainant (a "money award");
>
> (b) a direction that the respondent take such steps in relation to the complainant as the ombudsman considers just and appropriate (whether or not a court could order those steps to be taken)."

23. A money award can compensate for financial loss or any other loss, or any damage of a specified kind; s229(3). The maximum which can be awarded is £100,000; but the Ombudsman can recommend that the respondent pay a larger sum. He may also make a direction to the respondent. The money award is enforceable through the County Court, s229(8), and a direction is enforceable by injunction. The Ombudsman can also make an interest award and a costs award.

24. If the complainant notifies the Ombudsman that he accepts the reasoned written determination, it is binding on both parties and is final. Otherwise he is treated as having rejected it, and can pursue a claim by other means or by judicial review of the Ombudsman's decision.

25. Schedule 17 to the Act sets out details of the Ombudsman Scheme. Paragraph 8 permits the FOS, as scheme operator, to *"publish guidance consisting of such information and advice as it considers appropriate…"*. Paragraph 14 provides for the scheme operator's rules, made by the FOS with the consent of the FSA. These rules may specify the *"matters to be taken into account in determining whether an act or omission was fair and reasonable"*. Where legal proceedings have been brought in relation to the subject matter of the complaint, the Ombudsman may dismiss the complaint without consideration of the merits if he considers that the complaint is better dealt with in those proceedings.

The FSA Handbook

26. The FSA Handbook contains the Rules, Guidance and background information covering the whole gamut of its functions. The Handbook includes both FSA and FOS rules in the section entitled "Dispute Resolution: Complaints", DISP in the jargon.

27. The eleven Principles, denoted by an R as rules, are in Chapter 2 of the section of the Handbook entitled "Principles for Businesses". Chapter 2 is referred to by its shorthand title as PRIN; the Chapter applies generally to all businesses, not just to those undertaking the sale of PPI policies. I cite the more relevant ones:

> "R. The Principles
>
> | | |
> |---|---|
> | 1. Integrity | A *firm* must conduct its business with integrity. |
> | 2. Skill, care and diligence | A *firm* must conduct its business with due skill, care and diligence. |
> | 6. Customers' interests | A *firm* must pay due regard to the interests of its *customers* and treat them fairly. |
> | 7. Communications with clients | A *firm* must pay due regard to the information needs of its *clients*, and communicate information to them in a way which is clear, fair and not misleading. |
> | 9. Customers: relationships of Trust | |

> A *firm* must take reasonable care to ensure the suitability of its advice and discretionary decisions for any *customer* who is entitled to rely upon its judgment."

28. PRIN R3.4.4 contains the limitation permitted by s150(2), and states that:

> "A contravention of the rules in PRIN does not give rise to a right of action by a private person under section 150 of the Act (and each of those rules is specified under s 150(2) of the Act as a provision giving rise to no such right of action)."

29. The commentary on the role of the Principles is in chapter 1.1 of PRIN. G denotes it all as guidance. Their stated purpose is to reflect the regulatory objectives and to be *"a general statement of the fundamental obligations of firms under the regulatory system"*. It sets out the consequences of a breach. Although breach of a Principle does not give rise to a cause of action for breach of statutory duty, paragraph 1.1.7G states that breaching a Principle makes a firm liable to disciplinary sanction. In deciding whether there has been a breach of a Principle, the FSA would look to the standard of conduct required by the Principles. It would be for the FSA to prove fault on the part of the firm. The Principles were also relevant to the FSA's powers to gather information, to vary certain permissions, to its powers of investigation and intervention, and to possible injunction or restitution proceedings. This guidance says nothing about their relevance to redress or compensation under the Ombudsman Scheme.

30. The FSA placed reliance on 1.1.9G:

> "Some of the other rules and guidance in the Handbook deal with the bearing of the Principles upon particular circumstances. However, since the Principles are also designed as a general statement of regulatory requirements applicable in new or unforeseen situations, and in situations in which there is no need for guidance, the FSA's other rules and guidance should not be viewed as exhausting the implications of the Principles themselves."

31. Paragraph 1.2.1G specifically states that certain Principles, including 6 and 7, *"impose requirements on firms expressly in relation to their clients or customers."*

32. The FSA Rules in Chapter 1, DISP 1, include complaints handling, and in particular what is known as "root cause analysis", to which I shall return in connection with Mr Fordham's submissions. DISP 1.4.1R contains the Rule that a respondent must investigate complaints *"competently, diligently and impartially; assess fairly…whether the complaint should be upheld [and] what…redress…may be*

appropriate…taking into account all relevant factors;…". Guidance spells out what may be relevant: the evidence and circumstances, similarities with other complaints received by the respondent, *"(3) relevant guidance published by the FSA, other relevant regulators, the Financial Ombudsman Service or former schemes; and (4) appropriate analysis of decisions by the Financial Ombudsman Service concerning similar complaints received by the respondent."* There is a duty to co-operate with the FOS where a complaint is referred to it.

33. Chapter 2, DISP 2, sets out the FOS Rules in relation to various jurisdictions. It embodies the requirement that the FOS can only consider a complaint if the complainant has already complained to the respondent and either the respondent has sent its final response or eight weeks have elapsed since it received the complaint.

34. Chapter 3 sets out the FOS complaints handling procedures. The Ombudsman's powers include dispute resolution by mediation or investigation. There may or may not be a hearing, depending on what is fair; it may or may not be in public; and he can give directions as to how evidence will be presented. DISP R3.5.9 enables him to exclude evidence which would be admissible in a court, or to include evidence which would not be admissible in a court. He can accept evidence in confidence with only a summary or edited version being shown to the other party.

35. DISP R3.6.1 repeats the statutory duty to *"determine a complaint by reference to what is, in his opinion, fair and reasonable in all the circumstances of the case."* R3.6.4 states:

> "In considering what is fair and reasonable in all the circumstances of the case, the *Ombudsman* will take into account:
>
> (1) relevant:
>
> (a) law and regulations;
>
> (b) regulators' rules, guidance and standards;
>
> (c) codes of practice; and
>
> (2) (where appropriate) what he considers to have been good industry practice at the relevant time."

The regulator's rules, guidance and standards include the Principles, as well as the FSA's more detailed rules and guidance governing the sale of insurance policies and the resolution of disputes.

36. By DISP R3.7.2, a money award is such amount as the Ombudsman considers to be fair compensation for one or more of:

> "(1) financial loss (including consequential or prospective loss); or
>
> (2) pain and suffering; or
>
> (3) damage to reputation; or
>
> (4) distress or inconvenience;
>
> whether or not a court would award compensation."

37. A direction may require the respondent to take such steps in relation to the complainant as the Ombudsman *"considers just and appropriate (whether or not a court could order those steps to be taken);"* DISP 3.2.11R

38. In this context, it is worth noting the breadth of the definition of "complaint" in the FSA Handbook. It is:

> "any oral or written expression of dissatisfaction, whether justified or not, from, or on behalf of, a *person* about the provision of, or failure to provide, a financial service, which:
>
> (a) alleges that the complainant has suffered (or may suffer) financial loss, material distress or material inconvenience; and
>
> (b) relates to an activity of that *respondent*, or of any other *respondent* with whom that *respondent* has some connection in marketing or providing financial services or products, which comes under the jurisdiction of the *Financial Ombudsman Service*."

The factual background

39. The Principles were not new in 2010, and there had been very similar provisions since the passing of the 2000 Act, as envisaged during the passage of the Act, and indeed they had been preceded by broadly similar statements from earlier bodies which laid down standards for various aspects of the financial services industry. Principles, in like or identical form, had been in place in 2005 when the FSA took over the regulation of insurance selling.

40. However, the step on the part of the FSA, which precipitated this application for permission to apply for judicial review, was its issuing of Policy Statement 10/12, in August 2010. This Statement was preceded by two consultation papers in 2009 and in 2010, as required by the Act since it was to lead to Rule changes.

41. Of major importance to the process which the FSA had embarked on was a letter from the Chairman of the FOS to the Chairman of the FSA dated 1 July 2008. It was written in line with an agreed working practice, the "wider implications process", whereby the independent FOS would alert the FSA to what its complaints handling experiences showed could be of interest to the FSA. Its detailed terms are more important in connection with the third submission, but it is convenient to set it out when it first arises.

> "Under the wider implications process we agree to draw to each other's attention complaint issues that appear to us to have wider implications and where there may be a need for you to consider regulatory action to ensure that consumers who have suffered widespread detriment do not lose out. My board considers it is appropriate now to draw formally to your attention under the wider implications process the issues arising from past payment protection sales.
>
> FSA's own thematic work and that of the Competition Commission suggest that large numbers of consumers who have (or have had) PPI policies may have been missold. There is evidence of widespread and regular failure on the part of many firms to comply with FSA's rules and insurance law. In order for these consumers to receive redress it is inappropriate for them to have to make complaints individually to firms or ultimately to the Financial Ombudsman Service. Complaints may not be pursued by less confident customers, whilst large numbers of other complaints may be raised by customers who in practice have little prospects of success. Significant issues for customers and firms would need to be determined by the ombudsman dealing with large volumes of disputes and acting in a manner some might perceive as quasi-regulatory. While the number of consumers who have made complaints about PPI to the Financial Ombudsman Service constitutes a substantial part of our caseload, it is apparent to us that this number constitutes a tiny fraction of those who would be entitled to redress.

> You are presently assessing the need for wider regulatory action in the light of the latest information about present practices.
>
> We intend to provide you with further information about our experience so that regulatory action can be designed to ensure that firms take appropriate and proportionate remedial action. It is of course for FSA, together if appropriate with HM Treasury, to decide exactly what regulatory tools should be used to bring about the required outcome. But my board is in no doubt that simply allowing consumers individually to bring complaints is not the right way to tackle what is a systemic problem."

42. The FSA's first consultation paper 09/23 contemplated that its proposals would lead to an increase in justified complaints about the selling of regular and single premium policies, and that there would be an increase in the compensation paid on single premium policies.

43. The two components of the Policy Statement which matter for this submission are the amendments to the DISP section of the FSA Handbook and the Open Letter, covering the approach which firms should use in handling and assessing complaints about the sale of PPI policies and determining redress when a complaint is upheld. Guidance is given not only on the manner in which complaints are dealt with by firms as a matter of procedure, but also on how the Principles and other rules should be considered in determining the substance of the complaints.

44. Appendix 1 to the Policy Statement contains the amendments to the Handbook which are introduced by the Dispute Resolution: Complaints (Payment Protection Insurance) Instrument 2010, and are in a new Appendix 3 to DISP.

45. Appendix 3.1.2G to DISP says:

> "The aspects of *complaint* handling dealt with in this appendix are how the firm should:
>
> (1) assess a *complaint* in order to establish whether the *firm's* conduct of the sale failed to comply with the *rules*, or was otherwise in breach of the duty of care or any other requirement of the general law (taking into account relevant materials published by the *FSA*, other relevant regulators, the *Financial Ombudsman Service* and *former schemes*). In this appendix this is referred to as a "breach or failing" by the *firm*;

(2) determine the way the complainant would have acted if a breach or failing by the *firm* had not occurred; and

(3) determine appropriate redress (if any) to offer to a complainant."

46. The Appendix, at 3.6.2E, an evidential rule, deals with how the effect of a breach or failing is determined: *"In the absence of evidence to the contrary, the firm should assume that the complainant would not have bought the payment protection contract he bought if the sale was substantially flawed…"*. A series of examples of substantial flaws follows: pressuring the purchaser into buying the policy; not disclosing to the purchaser, in good time before concluding the contract, and *"in a way that was fair, clear, and not misleading"* that the policy was optional; not disclosing in a way that was fair, clear and not misleading the significant exclusions and limitations in the policy; not taking reasonable care when giving advice to ensure that the policy was suitable for the customer's needs, or to ensure that he was eligible for the benefits; not disclosing in a way which was clear, fair and not misleading the parts of the policy that did not apply to the customer, or what the true cost of the policy was; and recommending a single premium policy where the refund for early termination would not be pro rata to the length of term expired without taking reasonable steps to establish whether the customer might want to repay early. Thus evidence of a substantial flaw was rebuttable evidence that the policy would not have been bought and that would form the basis for compensation and other action.

47. Appendix 4 to the Policy Statement contained what described itself as an "Open Letter" to the BBA among others. It listed common failings in the sale of PPI policies, relating the failures, "mapping" them in the jargon, to the Principles and other rules in the Handbook. Some of these common failings are the same as the substantial flaws. The FSA had become concerned that those handling complaints about the selling of PPI policies were *"not applying the appropriate standards for the sale of this product"*, despite many reminders in various forms. So to remind the recipients of the letter of these standards, the common failings were set out, and the recipients were told that they should have regard to the list of failings when considering their obligations in relation to sales which had already taken place including in assessing complaints about them. The letter reiterated that the Principles had applied to sales of PPI policies since 2005, when the FSA became the regulator.

48. The major concern underlying this claim was that, through the Handbook changes and through this Open Letter mechanism, the FSA was using the Principles to impose obligations on firms towards customers to treat failings in sales procedures, as breaches of the Principles, even though they complied with or did not breach the

"Insurance: Conduct of Business", or ICOB, Rules in the Handbook. This would lead to compensation for breaches of the Principles. Thus the non-actionable Principles, according to the Claimant, were unlawfully being made actionable. In turn, the Ombudsman's substantive decisions may and the prior complaints to the firms would be affected by the contents of this Policy Statement. That is not disputed.

49. The BBA had made representations about this during the consultation process. The FSA responded that the BBA was wrong to regard the other rules and guidance as exhausting the implications of the Principles themselves; they could be relied on even where there were detailed rules. (This latter point goes to the second ground of challenge). Breaches of the Principles gave rise to liabilities, and firms had to pay redress where the conduct in question breached the Principles. This was consistent with the obligation on firms to resolve complaints on the basis of the wide and flexible test of what was fair and appropriate. They had to have regard to all relevant factors which clearly included the Principles of the FSA. The Ombudsman scheme envisaged that decisions by companies on complaints and subsequent decisions by the Ombudsman would be made on the same basis. The Ombudsman took account of his own previous decisions, to reach his decision on what was fair and reasonable, taking into account the Principles. The Ombudsman did not simply act on the basis of what was legally actionable. The Principles were vital to enabling the complaints rules to support the Ombudsman's jurisdiction to decide cases on the "fair and reasonable" basis.

50. The FSA's consultation response on this point concluded:

> "We consider it right and important to see the Principles as creating obligations on firms to comply with them, and as vital to delivering fair consumer outcomes.
>
> As we have repeatedly set out, the essence of the Principles-based approach is that the focus is on setting out the purposive 'what' that needs to be achieved (in the retail context this is typically a particular outcome for a consumer), not the 'how'. This approach lets firms and us focus on what is important, and it gives appropriate responsibility to firms to deliver and comply in a way that best fits their business. This view is fundamental to our being a Principles-based regulator. It has formed the basis of numerous supervision and enforcement actions, which in many cases entailed the payment of redress to consumers.
>
> In the PPI context, omitting failings from the open letter because of industry criticisms of their relationship to the Principles could undermine our efforts to address many acts or omissions by which firms have potentially caused detriment to consumers and may continue to do so. If, as we believe, too many firms selling PPI have failed to live up to the responsibility for delivering fair and appropriate consumer

> outcomes under the Principles at the point of sale, then we need to hold them to account for this.
>
> To step back from the Principles would be bad for current and future consumers because it weakens their protection against poor outcomes, and bad for firms because we would need to be more prescriptive in rules and thus leave them less scope for flexible approaches in light of their own evolving business models."

51. After the commencement of these proceedings, the FSA made a statement saying that it feared that the Open Letter was being misinterpreted. This was seen as something of a climb down by the BBA. The statement of 24 November 2010 said that the BBA thought that the Open Letter meant that a sale which involved one of the common failings would necessarily breach the Principles or rules or the general law, without there being any need to consider all the particular circumstances of the sale. The FSA said that that was not the position.

> "Rather, it has been the FSA's experience, based upon the thematic and enforcement work mentioned above, that sales in which one or more of the Common Failings occurred usually involved, on a proper consideration of all the circumstances of the sale, a breach of at least one of the FSA's Principles for Business, or other FSA rules, or the general law."

52. The common failings were not a substitute for a full assessment of the claim and were intended to help firms comply with their obligations.

53. The action of the FOS which is challenged is the publication of its version of its "Online PPI Resource" in November 2008, or now it appears some 6 pages of it which deal with Principles and their use. This 2008 version was not the first version of its online PPI resource. This resource provided, among other items of assistance to someone contemplating using the scheme, an overview of the FOS approach to some of the common issues raised in disputes about PPI, including how it assessed complaints and approached redress. It took account of "*the relevant regulatory, legal and other standards at the time of the sale*". It normally needed to consider whether the supplier gave to its customer information "*that was clear, fair and not misleading*" so that an informed choice could be made, and whether in giving advice, the firm "*took adequate steps to ensure that the product it recommended was suitable for that customer's needs.*"

54. Its description of the relevant regulatory rules included the FSA Principles, including Principles 1, 6, 7 and 9. In addition to those, it said, were the more detailed rules in the Insurance Conduct of Business, ICOB, section of the Handbook. It is sufficient for the first submission that the FOS intended to make decisions which relied in whole or in part on the non-actionable Principles. It is clear from the formulaic part of the

FOS decisions which were also part of the online resource that the Principles were taken into account in its decisions.

The Claimant's submissions

55. Lord Pannick QC's oral submission for the BBA refined somewhat the way the case had been put in the Skeleton Argument. His submission was that s150(2) prevented any obligation arising from the Principles between a firm and its customer; the FSA was wrong in law to use those Principles in advising firms how they should handle complaints and assess failings in that context, and the FOS was wrong to take them into account in ruling on redress for complaints. S150(2) was not just a procedural bar to reliance on the Principles in a court action for breach of statutory duty but prevented any substantive obligations arising from them in any other sphere of redress for customers. This was because Parliament had appreciated that the FSA might wish to produce statements of principles with a high level of generality, as earlier regulators had done and to whom similar statutory provisions had applied, which were not suitable for actionability in court.

56. This was an issue of statutory construction not of estoppel or legitimate expectation. But it was not a crude issue to be resolved by contrasting the language of legal liability in s150(2) with the language of "redress" in the handling of complaints under DISP. The question was whether, where legal actionability did not apply because of s150(2), redress under DISP was also excluded for breach of the same Principles. Redress and actionability had so much in common that the two were the same for this purpose. This did not mean that the Ombudsman was obliged to ignore the Principles in reaching his decisions on complaints; he had to understand their legal limits, which is that they cannot give rise to redress obligations. Lord Pannick did not identify any purpose for which the Ombudsman could consider them other than as an aid to interpretation.

57. Lord Pannick supported this submission with references to materials which he said explained how Parliament and the FSA saw the role of Principles when the FSMA was being enacted. He referred me first to the Explanatory Notes to the Financial Services and Markets Bill, which treated as one basis for the exception to the principle of actionability in s150(1), rules which might be drawn at a high level of generality, to which it might not be appropriate to attach a right of action. The Notes did not in fact say why that made them inappropriate to be actionable. Lord Pannick asserted that it was the very fact of their high level of generality.

58. Next, Lord Pannick placed reliance on an FSA consultation paper published in September 1998, after the draft Bill had been published for pre-legislative scrutiny. It was available to Parliament. It proposed a very similar set of Principles to those with which I am concerned. These "*succinct high-level precepts*" would state "*the fundamental obligations of regulated businesses*", within the overall context of the FSA's approach to regulation, which would be able to specify the legal consequences of their breach.

> "We do not expect the Principles to function in a vacuum, but in harmony with the other materials making up the framework within which firms must operate. The implications of the Principles will be elaborated in binding rules, 'evidential' provisions, and guidance. Wherever detailed provisions and guidance can be regarded as expressions or illustrations of the high-level Principles – as will often be the case – we will make that clear. The implications of the Principles will be evident throughout the Handbook.
>
> We envisage that, in supervisory contexts, the new Principles will function in much the same way as do the current models. Thus routine supervisory monitoring will rest on the Principles *coupled with amplificatory rules, evidential provisions and guidance*, rather than on the Principles alone. However, the Principles may be relevant in situations for which no rule or guidance yet exists. In such situations firms and supervisors alike need to be prepared to make judgments based on the values embodied in the Principles. "

59. The Principles would also be relevant to judgments of fitness and propriety, the use of investigatory and intervention powers, disciplinary proceedings, obtaining injunctions and restitution orders. By contrast, as Lord Pannick pointed out, there was no reference there to the Principles imposing obligations on firms towards customers.

60. The FSA intended that the Principles should not give rise to a cause of action, as is in fact the case, and gave this reason in that consultation paper:

> "We propose that it should not be possible for private persons to found an action for damages on the Principles alone. We have designed the proposed Principles as a statement of *regulatory* expectations, not as a set of legal rights at large. The high level at which they are expressed makes it important that their interpretation and application should be in harmony with the overall body of FSA rules and guidance and declared authorisation, supervisory and enforcement policy. This might be put at risk if civil litigation between private parties were to become the engine driving the interpretation of the Principles. The investor protection need can be amply met (as it is at present) by providing for civil actionability below the level of Principles in more specific rules.
>
> Since the Principles are not designed to create rights or liabilities in civil law, they will not provide a basis for payments under the compensation scheme."

61. Lord Pannick submitted that they were therefore intended to deal with the relationship between FSA and firm, not between customer and firm.

62. Third, the FSA addressed the role of the Principles in a Supplementary Memorandum of April 1999 to the Parliamentary Joint Committee on the Bill. Principles had been introduced ten years previously to respond to criticism from the industry about the high level of costs incurred in complying with a very long and detailed regulatory regime. Principles provided the industry with flexibility in determining how firms should meet regulatory standards; Principles could be applied to new circumstances and could prevent the exploitation of technical loopholes in detailed Rules. But they would need to be enforced effectively. Lord Pannick said that this meant enforcement through disciplinary measures.

63. What the Memorandum went on to say was this:

> "25. We recognise that the practical application of the Principles needs to be reasonably predictable, for those to whom they apply. We will therefore amplify the Principles through a combination of rules, evidential provisions and guidance. The FSA Principles should not therefore be viewed in isolation, but in the broader regulatory context"

Mr Brindle QC for the FSA highlighted "amplify".

64. The next paragraph referred to disciplinary action for a breach of a Principle; but it did not suggest that that was to be the only form of enforcement. It continued:

> "27. If the Principles are to achieve their purpose, it is important the FSA should be able to take action to enforce them where:
>
> - it is clear that the conduct in question violates the Principles, regardless of whether any detailed rule, code or evidential provision has strictly been breached;
>
> - the behaviour in question breaches the Principles because it is closely analogous to behaviour which would constitute a breach of a detailed rule, and would breach the spirit, though not the letter, of the rule;
>
> - there is evidence of systematic and repeated breach of detailed rules. For example, repeated breaches of rules about recommending suitable products may indicate wider problems, such as a lack of due skill, care and diligence, breaching Principle 2."

65. Lord Pannick submitted that there was therefore no example of any statement to Parliament which reflected a wider role for the Principles by way of affording redress

for consumers. Nor indeed was there any such statement in the Guidance about the Principles in the FSA Handbook, in the PRIN Section, as I have set out earlier.

66. This material was all relevant, submitted Lord Pannick, since where there was uncertainty as to the meaning of a statutory provision, here s 150(2), the court should, within the permissible bounds of interpretation, ascertain and give effect to the true meaning of what Parliament had enacted, to its true purpose: controversial provisions should be read in the context of the statute as a whole, which itself should be read in the historical context of the situation which led to its enactment; see Lord Bingham in *R (Quintavalle) v Secretary of State for Health* [2003] UKHL 13, [2003] 2 AC 687, at p695. It was therefore, he submitted, legitimate for that purpose for the Court to look at the sort of materials which he had invited me to look at, whether addressed to Parliament or not, since it all could help explain what the FSA and hence, in this type of legislation, Parliament had in mind. It would not have wanted to create obligations which the FSA had disavowed. He relied by way of example on *Black-Clawson International Ltd v Papierwerke Waldhof-Aschaffenburg AG* [1975] AC 591. I accept that that certainly helps on the use of a report by a Parliamentary Committee, with draft Bill attached, to identify the mischief to which an Act might be directed, which is not the case here. Mr Brindle QC for the FSA did not take strenuous issue with Lord Pannick's reliance on those materials as a matter of principle, but contended that they were neither direct nor reliable as guides to the meaning of the Act.

67. Lord Pannick further supported his submission on statutory construction by reference to the overall scheme of the Act. He submitted that there were good reasons why Parliament would have intended that s 150(2) should be limited in the way suggested. It made for a more coherent statutory scheme. Were the Principles to yield redress through the Ombudsman, where no specific Rule in ICOB had been breached, the only effect of a Principle not being actionable under s 150(2) would be to make claims over £100,000 not actionable, (and the extra could still be the subject matter of a recommendation). The vast majority of the claims were for very much smaller sums up to £1-2000.

68. As part of this analysis of the overall statutory scheme, Lord Pannick pointed to s404 of the 2000 Act. S404, to which I shall come in the context of Mr Fordham's submissions, deals with a situation of widespread failure on the part of firms to comply with rules as a result of which *"private persons have suffered loss in respect of which authorised persons are…liable to make payments ("compensation payments")"*. A scheme can be set up to deal with it. But this, as was common ground, does not apply where there have been widespread breaches of the Principles alone, since it only applies where the requisite loss is actionable in court. The language of s404 is similar to that of s150(2). The redress provisions should be construed in the like manner, submitted Lord Pannick, and not so that individuals could obtain redress under the complaints scheme for breach of the Principles alone, where the mechanism for dealing with widespread failures could not apply to them.

69. It was made even clearer in the replacement provisions of s404, with effect from 12 October 2010, that a scheme under s404 could not be made in respect of non-

actionable breaches of Rules. Lord Pannick treated this as clearer support still for this aspect of his submission. In addition to widespread failures to comply with applicable requirements, the making of what is now called a "*consumer redress scheme*", requires the loss suffered by consumers to be loss "*in respect of which, if they brought legal proceedings, a remedy or relief would be available in the proceedings*"; s404(1)(b). S404 (1)(c), a new provision, also requires the FSA, before it can make a "consumer redress scheme" to consider it desirable to make rules to secure that redress is made to consumers in respect of the failures, having regard to other ways in which consumers might obtain redress. By s404B(4), where a consumer redress scheme is in force to deal with widespread failures, and a complaint is made which falls within its scope, the Ombudsman must determine it by reference to what the determination under the consumer redress scheme should be. Since the latter cannot provide compensation for breaches of the Principles, as non-actionable Rules, the Ombudsman cannot provide for such compensation either. There is no logic for the position of the consumer, vis a vis the Principles, to change once a consumer redress scheme is in place, submitted Lord Pannick.

70. Mr Flint QC, also for BBA, pointed to the statutory Financial Services Compensation Scheme established by rules made by the FSA to compensate persons where the authorised person against whom a successful claim has been made cannot meet it; s213-4. The FSA decided on the basis for payments under the Scheme. The Scheme only paid out in respect of legal liabilities, that is in respect of claims which were legally actionable against the failed firm. It did not therefore regard claims based on the Principles alone as enforceable, even when embodied in an Ombudsman's award. It would decide the issue based on the nature of the underlying claim. Mr Flint also submitted that since the FSA had made actionable rules in the ICOB part of its Handbook, to which I will come in the context of the second main submission, which were restatements with minor changes, as the FSA saw them, there was clearly no need for the Principles to be actionable.

Conclusions on the relevance of actionability

71. I do not find the Claimant's submissions persuasive, preferring instead those of the FSA and FOS. The statutory provision being construed is s150. S150(1) deals with contraventions of rules by making them actionable as breaches of statutory duty. "Actionable" means giving rise to a cause of action in a court of law. S150(2) removes that actionability. S150(2) does nothing else. "Actionable" in s150(1) simply does not mean "capable of giving rise to obligations or compensation". So s150 does not apply to the Principles. It does not alter their function in any other way. It leaves intact any other function or effect which a non-actionable rule might have. The clear words of the section are wholly inapt to prevent rules which are not actionable giving rise to obligations as between firms and customers.

72. The words which would have to be imported into the section to give effect to Lord Pannick's submissions are not there by necessary implication either. If the Ombudsman can take the Principles into account in construing other rules but not as free standing sources of obligations, (even where using them in that way did not fall foul of BBA's second main submission that they cannot apply where specific rules have been made), an exclusion of unclear effect yet of some legal sophistication would be required. It is clearly not possible let alone necessary to imply such words.

73. There is nothing in the provisions dealing with the Ombudsman's scheme which contain the sort of limitation on the operation of non-actionable rules for which Lord Pannick contends. It might have been expected that such a consequence would feature in the legislative language somewhere along the line, and its absence shows beyond any reasonable doubt that it was not intended to exist.

74. Indeed, such an interpretation would run counter to the statutory role of the Ombudsman scheme, to the operation of which the intended effect of this submission is in reality directed. I accept Lord Pannick's contention that s150(2) should be interpreted in the context of the Act as a whole, but that does not help him. The FOS has a very broad statutory basis in s228 of the Act for reaching its decisions: what is in the opinion of the Ombudsman, fair and reasonable in all the circumstances of the case. The case begins with a complaint, and that is broadly defined in the Handbook Glossary. It can cover financial loss, and material distress and inconvenience. The Ombudsman's procedures are not limited to those of a court, nor is the evidence which he can admit. This is not surprising since the statutory purpose of the scheme is to provide a quick, informal, non-legalistic method of dealing with complaints. The remedies include compensation but it is not limited to those heads of loss to which a court would be confined, and he can give directions which a court could not. Redress may include or be limited to a finding or the obtaining of an apology.

75. Above all for the purposes of this issue, Schedule 17 gives a very broad power to the Ombudsman to decide what to take into account, as its rules in DISP 3 make clear. These include regulators' rules, guidance and standards, and good industry practice, as well as law and regulation. There is not and could not be a challenge to the Ombudsman's Rules and powers thus expressed. It cannot be argued that previous decisions of the Ombudsman Service are immaterial. I would have thought it obvious that the Principles were relevant rules, subject to the argument about their relationship to specific rules, and that the Guidance about the role of the Principles and the Open Letter common failings were relevant guidance.

76. All that the FSA decision under s150(2) does is to prevent a cause of action for breach of statutory duty arising in respect of the Principles; that is the only limitation on their role. That fact cannot make them irrelevant to the Ombudsman's duty to reach a decision as to what is fair and reasonable in all the circumstances of the case. Nor is there a justification for treating Principles, which cannot give rise to legal action, differently from those other relevant materials which by their nature cannot do so: regulators' guidance, codes of practice and good industry practice.

77. Indeed, it is my view that it would be a breach of statutory duty for the Ombudsman to reach a view on a case without taking the Principles into account in deciding what would be fair and reasonable and what redress to afford. Even if no Principles had been produced by the FSA, the FOS would find it hard to fulfil its particular statutory duty without having regard to the sort of high level principles which find expression in the Principles, whoever formulated them. They are of the essence of what is fair and reasonable, subject to the argument about their relationship to specific rules.

78. Mr Hodge Malek QC submitted that the BBA's argument about the role of the Principles, although directed at, was largely irrelevant to the FOS. Its obligation was to decide complaints by reference to what was fair and reasonable. Schedule 17 and the guidance in the Online Resource were necessarily expressed in wide terms. Whether the Principles had been formulated or not, and whether they could or could not be considered, the FOS would be bound to consider such essential points as whether the information given to a customer was clear, fair and not misleading, putting him in a position to make an informed choice, and whether the policy was a suitable one to be recommended for this particular individual. I accept that point. It is in reality unanswerable.

79. It is not in serious issue but when firms have to decide complaints, before they can go to the Ombudsman, they have to apply in reality and for fair complaints handling, the same approach as the Ombudsman would. DISP 1.4.1R, which is part of the FSA Rules on handling complaints, and which has been in force since 2007 in its present form and since 2001 in a very similar form, tells firms by way of guidance that in deciding complaints they should have regard amongst other matters to guidance published by the Ombudsman. This clearly contemplates complaints leading to firms deciding to offer redress or remedial action where the complaint would not be actionable. Any other approach would considerably reduce the value of this necessary stage of the scheme. Firms need to know and to be told what approach the Ombudsman will adopt. Complainants need to know the same to know whether to complain and how to do so.

80. Mr Malek also contended that the Principles in fact make very little difference to the position in relation to complaints since the crucial Principles were largely restated as actionable Rules, and embodied or reflected legal principles such as the duty of care, the duty of full disclosure by an insurer, and remedies for misrepresentation. He may well be right. But that does not help answer this question of statutory construction. It is a point which could cut both ways: either there is no reason why the Principles should have been excluded unless the exclusion also affects obligations in relation to complaints, or there is no reason to exclude the Principles from the Ombudsman's consideration given that he can consider them in a different guise.

81. Reliance was placed to a degree by Lord Pannick on *R (Heather Moor & Edgecomb Ltd) v FOS* [2008] EWCA Civ 642, [2008] Bus LR 1486. It was of greater importance for the second ground of challenge. But his reliance was misplaced: it supports the FSA and FOS. Although it is a case in which the passages relied on dealt with legal certainty, which is not an issue now pursued here, some observations relating to that

issue are of assistance. Paragraph 49, in the judgment of Stanley Burnton LJ, is clear that the FOS scheme lawfully permits a wide range of materials to be taken into account; the Ombudsman is permitted to reach a decision which departs, not just from the common law on negligence but from all the other materials to which he is entitled to have regard, if he thinks that that is necessary to reach the fair and reasonable decision. If firms comply with all the relevant materials, it would only be exceptionally that they could be found liable by the Ombudsman to provide redress. If he makes such a decision, he has to explain why. The judgment does not treat materials other than the law as relevant only exceptionally. Mr Malek referred me to a number of other decisions which make the same point.

82. What Rix LJ said at paragraph 89 is of importance, since it reinforces the argument that were the BBA to be correct, it would represent the sort of artificial legalistic narrowing of what the Ombudsman could consider under a scheme designed to avoid just such an approach:

> "In my judgment, the following values are all to be appreciated and brought into a pragmatic balance: that an efficient and cost-effective and relatively informal type of alternative dispute resolution should not be stifled by the imposition of legal doctrine; that the opportunity for the development of new ideas was fitting to financial service industries operating in consumer markets should be appreciated for the benefits they can bring; that on the other hand transparency, consistency and accessibility as to the principles which inform the ombudsman's determinations remain virtues in this new setting; and that publicity as to those principles and those determinations can assist in that regard."

83. Lord Pannick's strongest point was that, when s150(2) was read in the context of s404, it was clear that the wide limitation he contended for was exactly what Parliament had intended. His case was yet stronger when s150(2) was read with the new s404B. He was right that his opponents did not address this new provision in argument. Of itself, such a provision as s404 would not be strong enough to show that compensation and other FOS remedies could only apply to actionable complaints, in view of the breadth of the language used in relation to the Ombudsman's powers. Lord Pannick is right that s404B, which is new, means that the Ombudsman dealing with a complaint falling within the scope of a consumer redress scheme in force, cannot invoke the Principles, save perhaps to the extent that they are an aid to construction. I also accept that s404B cannot be regarded as changing the effect of the exclusion of the Principles under s150(2), from what it was before s404B came into force, so he can deploy this point in relation to s150(2) and the Policy Statement.

84. However, I do not accept that that assists Lord Pannick to the extent necessary in the light of the other provisions. First, this provision stands by contrast to the broad provisions in relation to the Ombudsman complaints. If this is merely giving effect to what the position always was in relation to non-actionable rules and the Ombudsman, as Lord Pannick must contend, it is curious that s404B was introduced into the new

s404 scheme provisions as clarification, without some other clarifying provision or references in s150 or in s228 and Schedule 17. In my judgment, that is because s404B is intended to have effect only in relation to the defined "relevant complaint". A relevant complaint is one falling within the scope of a consumer redress scheme which is in force. Had any wider effect been intended, declaratory or otherwise, in relation to any complaint, as must be Lord Pannick's case, there would have been no need for any limitation of its effect to "relevant complaints", as opposed to all and any complaints.

85. Second, there is some sense in such a limitation. One major purpose of the s404 scheme is to require firms to examine cases whether there has been a complaint or not, and if the failure has caused loss, they have to make redress to the consumers. The consumer may have made no complaint at all. They may complain only when they hear of the consumer redress scheme. The limitation to legal liability limits the liability of the firms in a situation when they are likely to be paying compensation to a number of people who did not or otherwise would not have complained. There is one class of consumer who could lose out, and that is the person whose complaint would fail under the s404 scheme but would succeed under the Ombudsman scheme as ordinarily applied. That is a form of trade-off for the consumer in general.

86. Lord Pannick's reliance on the general nature of the Principles and pre-legislative materials does not assist. The high level of generality in the expression of the Principles is not of itself the reason for their exclusion under s150(2). After all, they are no more in some instances than broad expressions of common law concepts, which do suffice for actionability. Breach of the Principles can give rise to significant legal consequences as between firms and the FSA; there is no logic in the degree of generality of expression inhibiting their use in complaints while giving rise to significant enforcement obligations including injunctions and restitution. But even if that were the reason for their exclusion, that could not assist in showing that they were incapable of giving rise to redress on a fair and reasonable basis. Nor does the fact that it is possible for the FSA to promulgate modified restatements of the Principles as actionable rules, as it has done, show that Principles were intended to give rise to no obligation between firms and customers. It may reduce the practical distance between the parties but the argument is neither logical nor a useful tool for statutory construction.

87. The Explanatory Notes are of no assistance since, although they refer to a high–level of generality as perhaps making actionability inappropriate, they give no reason why that could be so. I accept the evidence of the FSA that the thinking behind its decision to exclude the Principles from the effect of s150(1) was and continues to be that set out in the Consultation Paper on the Bill to which Lord Pannick referred. High level provisions were needed to provide the basic and enduring framework for financial services regulation; and it was thought undesirable to have to put in place rules which were highly prescriptive covering perhaps ineffectually all the circumstances to which every regulated activity gave rise. Indeed the industry did not want that. The FSA wanted to control the interpretation and application of those Principles, and their relationship to the more specific rules, rather than leave it to the courts to decide upon in the course of private litigation into which the FSA would not

wish to be incessantly intervening. The purpose of the exclusion does not therefore assist the BBA in showing that the rules excluded from the operation of s150(1) were also intended to give rise to no obligations between firms and customers.

88. The very next paragraph in the Consultation Paper states that, because the Principles would be excluded from s150, they would not provide a basis for payments under the industry's statutory compensation scheme. But that is saying no more than what the Financial Compensation Scheme operator itself says: that the scheme will only apply to legal liabilities and not to awards under the Ombudsman Scheme unless the underlying complaint itself gave rise to actionable liability. The "compensation scheme" does not refer to the Ombudsman scheme.

89. I accept Mr Brindle's submissions on the irrelevance of the compensation scheme to the true interpretation of these provisions. The FSA and not the Act set the terms for this Scheme; so it cannot be said that two sets of statutory provisions are in conflict. If the FSA has adopted a different approach in its application of s150(2) to the Principles and in setting the terms of the compensation scheme, that is irrelevant to an issue of statutory construction. In any event, there is no reason why there should not be a different basis to what the regulated industry has to fund in respect of the liabilities of firms which can no longer themselves meet their liabilities, from that which governs redress to be provided by individual firms which are alive and well, and can meet their full obligations. I see no reason why what is regarded as "fair compensation" for a complainant to be paid out of a common industry provided pot, should not be different from what is fair compensation from a firm which still exists and can meet its obligations.

90. I accept that the Consultation Paper on the Bill contains no reference to the Principles being used to create obligations as between firms and customers, although it does list ways in which the Principles would be used as between firms and the FSA. The reason for the omission is probably that it was thought obvious that Principles, while not creating actionability, would be relevant to the handling of complaints by firms and to the Ombudsman's task. I do not see any part of the Paper as suggesting that the Ombudsman should approach his task without regard to the Principles. The reference to investor protection being adequately dealt with by actionability below the level of Principles is not a reference to the role of the Ombudsman and the scope of his function, but deals with the value and effect of actionability for which the Principles are excluded. Taken literally, as is the Claimant's argument, the reference appears to suggest no need for the Ombudsman at all. The earlier Consultation Paper which included the Ombudsman provisions was clear as to the breadth of the materials to which he should have regard when ruling on complaints.

91. Lord Pannick is right that the FSA's Supplementary Memorandum to the Parliamentary Committee also omits reference to the role of Principles in creating obligations between firms and customers. While this is perhaps a potentially better source for guidance on the mischief and purpose of the legislation, it is less clear in what it says about the role of Principles than the Consultation Paper, and equally silent as to how the Ombudsman should approach his task - with or without reference

to them. In my view, as with the silence in the Consultation Paper, the more obvious explanation for this silence is that the notion that they should form no part of complaints handling or Ombudsman decision-making was simply never what the FSA had in mind and their obvious relevance to that task did not need spelling out. There is a limit to what can be gained from silence unless the context makes it clear that the omission was deliberate and significant. It is the exclusion of Principles from the decisions on complaints, despite being used to found all sorts of enforcement action by the FSA, which needed to be expressed, since that would be so much more startling a consequence of their exclusion from s150 than their continued use in complaints and the Ombudsman scheme.

92. The section in the FSA Handbook on the consequences of breaching the Principles, PRIN 1.1.7-1.1.9G gives rise to the same argument. It is not said that a consequence of breach of the Principles is that a complaint could be well founded. The only exclusion mentioned however is a private action for damages. But it is obvious that the DISP section of the Handbook requires firms handling complaints to consider a broad range of materials into which the Principles readily fall, and from which one would expect any exclusion of the Principles to be clearly expressed. The same applies to the Ombudsman. There is nothing new about this position.

93. Finally, I wish to express grave doubts about the use of the Consultation Paper and Supplementary Memorandum in this case as aids to interpretation. Lord Pannick submitted that they were useful in understanding the purpose of the legislation and the mischief to which it was directed. It is possible that such materials could be relevant to that. But the passages relied on refer to no mischief. They identify a legislative purpose only in the sense of explaining how the FSA intended to use its powers under the provisions, and with what expected effect. Such evidence goes rather beyond what I would regard as the identification of the purpose behind a provision. It is also quite a leap to say that Parliament must have intended its enactment to mean what was said by the shadow authority in its consultation paper issued to the general public, or what the authority told the Committee about its intentions. Parliament may have been persuaded thereby not to legislate to prevent a course of action or that no further change was necessary, but that is no real guide to what the words used mean. It is quite a distance from the mischief and purpose of the Act. No serious issue was taken with the admissibility of these documents. In referring to them however I do not wish to be regarded as having accepted that they were in fact admissible. They were also of no decisive help, and it is very dangerous for the supposed helpful tools of interpretation themselves to require speculative interpretation.

94. For those reasons I reject the BBA's first ground of challenge.

Ground 2: The Principles cannot conflict with or augment specific rules

The general contention of the BBA

95. This ground alleges that, if, as I have concluded on ground one, the non-actionable Principles in the Handbook can be relied on by the FSA and FOS as creating obligations owed by firms to customers, breach of which leads to compensation, it was nonetheless unlawful for the FSA and FOS to interpret or apply the Principles in such a way as to "contradict or augment" specific rules governing the sale of and handling of complaints about PPI. It was also unlawful for the Open Letter common failings, as reflected in the amendments to DISP in the Handbook, to be interpreted or applied so as to "contradict or augment" specific rules in the Handbook. This was the asserted effect of the new guidance, the Open Letter common failings and the required standards implied from them, and of the FOS' Online Resource.

96. The eventual difference between the FSA and BBA, as I saw it, lay in whether the specific could be augmented by the general, not in whether the specific could be contradicted by the general. The FOS position was different to a degree in theory, though much less so, it thought, in practice.

97. The "Insurance: Conduct of Business", ICOB, section of the FSA Handbook contained detailed rules and guidance on the sale of insurance polices. It is not confined to PPI sales. The FSA and FOS had significant concerns about the fullness and fairness of the information provided to potential purchasers of these policies, and about the way in which they were advised on the suitability of those policies to meet the customers' needs. That was where the arguments about the effect of the Principles, the new guidance and the Open Letter common failings were focused. So I shall concentrate on those aspects of the rules and guidance in ICOB, in force from 2005 to 2008. The ICOB Sourcebook, ICOBS, in place from 2008 has very similar provisions in relation to disclosure, suitability and appropriate information in form and content. I do not need to set out further provisions from ICOBS; they suffer from the same asserted vices, although the two versions had different requirements in specific rules governing the same aspect of a sale.

98. The Principles, submitted Lord Pannick, could be used as aids to the interpretation of specific but ambiguous rules. He accepted in this ground that where a regulated activity was not covered by a specific rule or detailed rules, the Principles could be used to impose obligations on firms. But he submitted that, as a matter of statutory construction and not of legitimate expectation, the scheme of the legislation was that where a regulated activity was governed by specific rules, the only obligation of the firm was to comply with those rules. If ICOB was complied with, a firm could not be held to have breached any provision leading to redress. The Principles could not be used to augment let alone to contradict those specific rules, which embodied the purposes of the Principles to the extent the FSA thought appropriate. Where specific rules were promulgated by the FSA "to occupy the field" and where the purpose of the specific rules was to implement specific Principles, the FSA could not additionally resort to those Principles. This would be to use the Principles in conflict with the rules or to augment them. But that only applied so far as material here to Principles 6,7 and 9. If Principle 1, integrity, were breached, the FSA could enforce that since the specific rules in ICOB were not intended to implement that Principle.

99. If that analysis was right, the FOS in its turn should not use the Principles to augment or contradict the obligations owed by firms to customers when deciding on complaints, and should not advise either side, as they did in the Online Resource, that that was how complaints should be handled. The FOS' duty to reach decisions on the basis of what was fair and reasonable could not permit it to misinterpret the role of Principles in that way. Fairness and reasonableness also required the FOS to apply the specific rules and not to augment or contradict them by relying on the high level Principles. In that context, Lord Pannick particularly relied on *Heather Moor & Edgecomb*, above.

100. The position of the FOS, however, was in one respect different from that of the FSA because, applying *Heather Moor & Edgecomb*, there might be exceptional circumstances, in view of the breadth of its jurisdiction, in which the FOS could uphold a complaint where a firm had complied with ICOB. It had to direct itself correctly in law as to the meaning and effect of the Principles, but it could still, exceptionally and on a reasoned basis, conclude that a fair and reasonable determination of a complaint required it to be upheld, and upheld by reference to the Principles as I understood the argument, even though the firm had complied with the specific ICOB rules. If the position were other than exceptional, it would frustrate the statutory scheme and make the FOS in effect the regulator, who could negate the regulator's s155 rule-making consultation process.

101. Lord Pannick adopted the same approach to the effect of a specific rule on the role of common law negligence. It would only be exceptionally that negligence could sustain a complaint when the specific rules, which that aspect of the common law addressed, were complied with. I was referred to the judgment of HHJ Waksman QC in the Mercantile Court on appeal in *Harrison v Black Horse Ltd* [2010] EWHC 3152 QB, in which damages were claimed for breach of the statutory duty in ICOB, and for damages for negligence. The bank faced a claim that it had assumed responsibility to take reasonable care in recommending the policy it did. The bank had relied on the content of a specific ICOB 4 rule to say that, as it was advising only on a single premium product, the extent of the advice it could offer on suitability was limited; it had met the requirements of the rules, which did not require it to advise on regular premium policies as an alternative nor on the products of other firms, the details of which it would not know. The claim in negligence was resurrected as an alternative. As I understand it, the claimant alleged that if the bank was entitled to avoid liability under the rules on that basis, a duty of care arose in the alternative to give that wider advice. But that did not assist the customer as HHJ Waksman held:

> "Given that ICOB prescribed a detailed code on how an intermediary in the position of the Bank should conduct itself when purporting to give advice in respect of a single product ie whether to recommend it or not, I see no reason why any co-terminous duty of care should extend more widely. Moreover, the fundamental point raised by rule 4.3.7 (1) above was that the question of cost can only sensibly be dealt with by a comparison with other products. If (as here) the Bank cannot engage in such an exercise because of its very limited advisory role, I cannot see how it could be expected to advise more

> widely on the question of cost under a common-law duty of care. Its inability to make a comparison remains, as does the difficulty of imposing some sort of obligation to pronounce nonetheless upon whether the PPI was expensive according to some other standard."

102. The BA submitted that S138 of the 2000 Act, with all its consultation procedure and cost/benefit analysis, would be frustrated if customers and firms could not rely on the rules, promulgated to implement specific Principles, as the statement of the obligations of the firms under those Principles.

The detailed analysis by the BBA

103. Lord Pannick's general submissions were exemplified in argument by Mr Flint. Mr Flint's first illustration concerned the introduction into a restatement of Principle 7 and other specific rules of a requirement to take reasonable steps to provide clear, fair and not misleading communications, instead of an unqualified obligation to provide such communications. ICOB Rule 2.2.3R(1), an actionable Rule, provides under the heading "Clear, fair and not misleading communication": "*When a firm communicates information to a customer, it must take reasonable steps to communicate it in a way that is clear, fair and not misleading*". The related guidance, 2.2.1G, says that the purpose of this Rule is "*to restate, in a slightly amended form, and as a separate rule, the part of Principle 7 …that relates to communication of information. This enables a customer…to bring an action for damages under section 150 of the Act…*" for its breach. The rule covers all communications with customers in whatever form: face to face, written and telephone. The slight amendment in the "*restatement*" of Principle 7 in ICOB is the inclusion of the words "*take reasonable steps to*". Guidance also explains that the prominence of relevant information in the context of the communication as a whole is important including, clarity of print including fonts, size of type and the use of different fonts and sizes.

104. ICOB 2.4.2R states:

> "R A *firm* will be taken to be in compliance with any *rule* in ICOB that requires a *firm* to obtain information, to the extent that the *firm* can show that it was reasonable for it to rely on information provided to it in writing by another *person.*"

105. 2.4.4R reads:

> "R (1) Any information which a *rule* in ICOB requires to be sent to a *customer* may be sent to another *person* on the instruction of the *customer*"
>
> (2) There is no need for a *firm* to supply information to a *customer* where it has taken reasonable steps to establish that this has been or will be supplied by another *person.*"

Mr Flint gave these as examples of where the specific rule required reasonable steps to be taken, as envisaged by 2.2.3(1)R.

106. Financial promotion is dealt with in chapter 3. Guidance at ICOB 3.5.2G states that the chapter "*amplifies*" Principles 6 and 7, for activities within its scope. ICOB 3.7.5R provides for circumstances in which communication of a non-investment financial promotion produced by another person will not contravene any rules in chapter 3; these involve taking reasonable care over establishing certain relevant facts. By ICOB 3.8.1(1)R, *"A firm must be able to show that it has taken reasonable steps to ensure that a non-investment financial promotion is clear, fair and not misleading."* Mr Flint gave this as a further example of where a particular rule developed the Principles for application to a particular activity, by requiring no more than reasonable steps to be taken.

107. ICOB 4 deals with standards of advising and selling. Again, guidance states that the chapter "*amplifies*" Principles 6, 7 and 9. The purpose of the chapter is explained in ICOB 4.1.7G: to ensure that customers are adequately informed about the nature of the service they have received from an insurance intermediary, and that where a personal recommendation is made it is suitable for the customers' demands and needs. Detailed rules then follow. ICOB 4.3.1R deals with suitability of a product for a customer:

> "R (1) An insurance intermediary must take reasonable steps to ensure that, if in the course of insurance mediation activities it makes any personal recommendation to a customer to buy or sell a non-investment insurance contract, the personal recommendation is suitable for the customer's demands and needs at the time the personal recommendation is made."

108. Mr Flint submitted on this first illustration there was no point in ICOB 2.2.3R and the other specific rules requiring reasonable steps to be taken if Principle 7, as unrestated, could lead to redress through complaints. And that is what customers were concerned about rather than actionability, since taking legal action was expensive and risky for them. Hence the Principle was subsumed into the many specific rules, which required no more than reasonable steps to be taken and Principle 7 could not then be used to augment or to contradict those specific rules. The Principles, and in particular Principle 7 in its unqualified version before restatement could not be used by the FSA or FOS to impose obligations to do more. Yet that was the effect of the amendments to DISP in the Policy Statement and of the Open Letter list of common failings.

109. All that dealt with "communication" in Principle 7: how information was presented. Mr Flint's next illustration came from ICOB 5 which covers product disclosure: what information had to be presented, the second "information" limb of Principle 7. ICOB 5 covered this in exhaustive detail. ICOB 5.1.9G is typical in the language of its guidance:

> "(1) This chapter reinforces *Principle 7* (Communications with clients), which requires a *firm* to pay due regard to the needs of its *clients* and communicate information to them in a way that is clear, fair and not misleading.
>
> (2) The purpose of this chapter is to ensure that *customers* have the necessary information to make an informed choice about whether or not to *buy* a specific *non-investment insurance contract* and whether a contract continues to meet their needs."

110. ICOB 5.2.9R lists the information which must be supplied to customers, which includes the policy summary, which is described in more detail in later rules. This policy summary is a key document. ICOB 5.5.1R specifies that the summary must contain "only" information tabulated in ICOB 5.5.5R, plus a limited amount of optional material. The ICOB 5.5.5R table includes *"(4) significant features and benefits"*, and *"(5) significant and unusual exclusions or limitations"*. Guidance says that the summary should properly describe the contract but should not overload the retail customer with detail. ICOB 5.5.2R requires the summary, if not set out in a separate document, to be "*in a prominent place within the other document and clearly identifiable as key information that the retail customer should read*", and to be separate from the other content of the document.

111. A core provision in ICOB 5 is ICOB 5.3.1R which requires certain information to be provided to retail customers before the conclusion of a contract which is not a "distance contract", ie not face to face. This was seen by Mr Flint as an important illustration of his point.

> "R If a *non-investment insurance contract* is not a *distance contract*, an *insurance intermediary* must, in good time before the conclusion of the contract:
>
> (1) provide a *retail customer* with the following information in a *durable medium:*
>
> (a) a *policy* summary (ICOB 5.5.1R to ICOB 5.5.13G);
>
> (b) a statement of price (ICOB 5.5.14R to ICOB 5.5.15G);
>
> (c) the relevant directive-required information set out in ICOB 5.5.20R (subject to ICOB 5.5.17G to ICOB 5.5.19R); and
>
> (d) draw the attention of the *retail customer* orally to the importance of reading the *policy summary*, and in particular the section of the *policy summary* on significant and unusual exclusions or limitations."

112. What is to happen after the conclusion of A non distance contract is covered by guidance:

> "5.3.2G Where the *retail customer* does not have the opportunity to read the information provided in accordance with ICOB 5.3.1R(1) before conclusion of the contact, for example, because it is provided in a sealed pack, the *insurance intermediary* should provide a specimen copy of all the information in such a way that the *retail customer* is able to read it before conclusion of the contract. For example, a stand with sealed packs could be accompanied by a copy of the *policy summary* and other required information, with a notice that they contain important information the *retail customer* should read before *buying* the *policy.* Oral disclosure at the point of sale must still be given in accordance with *ICOB 5.3.1R(2).*"

113. There are equivalent requirements with the same purpose in relation to distance contracts and telephone sales; ICOB 5.3.6R.

114. Mr Flint then turned to how the Policy Statement showed the FSA's intention to use unrestated Principle 7, other Principles and the Open Letter common failings to contradict or augment the specific rules and their limitations. The new provisions in DISP showed how the FSA intended to give effect to the new standards by way of evidential rules in relation to post January 2005 sales. Even for sales before that the rules are to be treated as guidance. New rule DISP Appendix 3.10.3E makes contravention of the new provisions evidentially relevant to establishing a breach of DISP 1.4.1R, which is the basic complaint handling rule, to which I have already referred, and to which this introduces substantive changes as to what justifies a complaint. I have already set out in paragraph 46 the provisions of new rule DISP Appendix 3.6.2E and summarised the 12 examples of substantial flaws, drawn from the Open Letter common failings and expressed in quite general language. These treat a substantial flaw in the sale, exemplified by the common failings, as evidence that the PPI policy would not have been bought. In that way, submits Mr Flint, the Open Letter common failings have been made a firm part of the rules whereby the actions of firms and complaints against them will be judged, rather than by compliance with the specific rules which the FSA has laid down for them to abide by.

115. I take for these purposes from DISP Appendix 3.6.2E examples 4 and 12, which treat as substantially flawed a sale in which the firm:

> "(4) did not disclose to the complainant, in good time before the sale was concluded and in a way that was fair, clear and not misleading, the significant exclusions and limitations, i.e. those that would tend to affect the decisions of *customers* generally to buy the *policy*, or…

> (12) in a sale of a single premium *payment protection contract*, failed to disclose to the complainant, in good time before the sale was concluded, and in a way that was fair, clear and not misleading:
>
> (a) that the premium would be added to the amount provided under the credit agreement, that interest would be payable on the premium and the amount of that interest, or
>
> (b) (if applicable) that the term of the cover was shorter than the term of the credit agreement and the consequences of that mismatch; or
>
> (c) (if applicable) that the complainant would not receive a pro-rata refund if the complainant were to repay or refinance the loan or otherwise cancel the single premium *policy* after the cooling-off period."

These contrasted with both the "reasonable steps" communication obligation in the restated Principle 7 and with the detailed information requirements of ICOB 5.

116. Mr Flint submitted that if the firm did not provide an explanation of the refund terms now required, that was a substantial flaw. There would be an assumption that the customer would not have bought the policy, and if not rebutted, compensation would follow. If compensation were refused, enforcement action would become possible for breach of the complaints handling requirements, since this was an evidential provision. Real consequences were intended. If the threatened "tough action" was to follow, the firms were entitled to be clear as to the legal basis upon which that would happen.

117. Common failing 15 was related to example 12(C). It required oral disclosure of a non pro rata refund term. Firms commonly failed to disclose in good time and in a clear, fair and not misleading manner that the termination of the policy would not lead to a rebate of premium, proportionate to duration of cover. Whether that was a significant and unusual limitation was an issue between the FSA and BBA. The FSA had asked firms in the past to consider whether this sort of term was such a limitation but now said that firms ought to conclude that disclosure was necessary whenever it was likely to be relevant to a customer, eg if there was a prospect of early repayment of the loan. So the content of what had to be disclosed was greater than hitherto.

118. Mr Flint submitted that this sort of approach imposed in reality a general obligation on firms to draw attention orally to that type of term since there would always be a prospect of early repayment or refinancing of the loan or cancellation of a single premium policy. If such a term were a significant and unusual limitation, it should be included in the Policy Summary, but now attention had to be drawn to the point orally. This was an important illustration of the wider point about the way in which

the Principles and the common failings were to be used, since it applied to a very common form of single premium PPI policy and to a common source of complaints about them. This mattered because sales training, procedures and proof of correct use of the procedures are adapted to the rules promulgated by the FSA.

119. The vice in common failing 15, and in the way in which the FSA proposed to use it, was that it positively added to the specific requirements in ICOB chapter 5, creating obligations in every case to draw a customer's attention to or explain orally refund terms, and give the consumer time to read them. The requirements of chapter 5 were only that the refund terms were in the policy summary and there had to be an oral signpost, so this was not just an augmentation of but an inconsistency with the listed requirements. There could be cases in which a failure to explain how refund terms worked would fall foul of ICOB 2.2.3R, or of some other rule or of Principle 1 but that was no basis for adding such a wide requirement by the means of common failing guidance. It would not be sufficient compliance with common failing 15 just to hand out a leaflet on request.

120. More generally, Mr Flint contended that the FSA's commentary on common failing 15 in relation to face to face and telephone sales went beyond ICOB 5.3.1R. It reads:

> "The Principles require firms to pay due regard to a customer's information needs and communicate information to the customer in all situations in a way that is clear, fair and not misleading. In sales primarily conducted orally, it was not enough just to provide important information in writing. So, we have found it to be a failing where there was not a fair presentation of the information during the sales discussion, by, for example:
>
> - giving an oral explanation; or
>
> - specifically drawing the customer's attention to the information on a computer screen or in a document and giving the customer time to read and consider it.
>
> In addition, the requirement to pay due regard to a customer's information needs and communicate information in a clear, fair and not misleading way required the firm to provide balanced information when making reference to a policy's main characteristics (whether orally or in writing). So, we have found it to be a failing if, where the firm described the benefits of the policy orally, it did not also provide an adequate description of the corresponding limitations and exclusions in a way that was clear, fair and not misleading, for example orally. Further, ICOBS requires that, if a firm provides information orally during a sales dialogue with a customer on a main characteristic of a policy, it must do so for all the policy's main characteristics."

121. The difference is that ICOB 5.3.1R requires that in an oral sale, there must be a Policy Summary, and the customer must be told that it is important to read it, whereas the Open Letter Standard went beyond that and, contended Mr Flint, required an oral explanation of the policy or drawing attention to the main points on a computer screen.

122. In the Policy Statement 10/12, the FSA responded to the industry criticism that there had not always been an obligation to draw specific attention to price or refund terms in every sale, by saying that it had always been of the expressed view that firms' obligations toward their customers extended beyond those set out in specific ICOB or ICOBS rules. In dealing with customers, firms had also to comply with obligations set out elsewhere, for example, in the Principles and the general law.

> "In particular, Principle 7 requires firms to pay due regard to the information needs of their clients and communicate information to them in a way that is clear, fair and not misleading. In sales primarily conducted orally, it is not enough just to provide important information in writing. There should be a fair presentation of the information to the customer during the sales discussion, by, for example, giving an oral explanation, or specifically drawing the customer's attention to the information on a computer screen or in a document and giving the customer time to read and consider it."

123. The Policy Statement gave another example of the role of the Principles in response to the BBA's point that there never had been a rule which required the difference in the terms of the underlying loan and policy terms to be disclosed, or the consequences of this mismatch, which could arise where the lender was also the insurer under the policy. If the consumer was only to be protected for part of the duration of the loan, that should be made clear to him so that he could make an informed choice. This was required under Principles 6 and 7 for advised and 9 for non-advised sales. This exemplified what the BBA submitted was the FSA's legally erroneous approach.

124. The FOS had adopted a similar line to the FSA and submitted Mr Flint, was guilty of the same legal error. Its Online Resource set out Principle 7, and continued:

> "In considering complaints, the ombudsman will assess the information provided – and the context in which it was provided. If the sale was made primarily by phone or at a meeting, and evidence suggests failures in the oral disclosure of information by a firm, we are unlikely to consider that subsequent written information automatically corrects previous shortcomings".

125. This, he said, ignored the specific rules and assumed a duty of oral disclosure which could only derive from the Principles in conflict with the specific rules.

126. The Resource listed what it called "information issues" likely to require careful consideration which included the impact of early termination of a single premium policy. The approach of the FOS was this:

> "We need to consider the overall impression left by the disclosures made by the firm. Does this represent a fair and balanced summary of the policy – noting not just its benefits but also its limitations and exclusions? Or is the impression given by the firm one that understates or ignores the limitations of the policy?"

127. Mr Flint pointed out that this was a very general approach to an issue covered by specific rules, which had been the subject of detailed consultation and represented the regulator's judgement as to what was required. The error of law was that the question for the FOS was whether the firms complied with the requirements of ICOB 5.3 in respect of the provision of information; the FOS was instead asking in a general way whether the customer was in a position to make an informed choice.

128. Mr Flint took me to three decisions of the FOS to illustrate the effect which he said the Online Resource approach was having on Ombudsman decisions on complaints about disclosure, but with the approach starting in about 2007. These show what appear to be policy summaries which complied with specific rules in ICOB in respect of disclosure; at least the decisions did not go against the firms on the basis of such a breach. One case went further and the summary did refer to the non-pro rata return of premium on early termination, in compliance with an agreement reached between the industry and the FSA in 2006 that the effect of non-pro rata return of premium would be illustrated in the policy summary. Yet, in each case, the Ombudsman found against the firm on the basis of a breach of the general Principles requiring sufficient clear, fair and not misleading information to be provided so that an informed choice could be made. The FOS was now upholding a high percentage of the complaints made to it, of which complaints about single premium policies and the return of premium were a large part. The precise figures were debateable.

129. This was contrasted directly with a decision of the FOS in 2006 in which it had rejected a complaint where the Adjudicator held that the established view of the FOS was that in loan protection policies the firm was entitled to provide for non-proportional rebates, if it was reasonable for the policy holder to be aware of that. In that case the agreement had stated that that would be the case, as did the policy summary. No requirement was imposed for any greater disclosure or oral explanation by reference to Principles.

The FSA's submissions

130. Mr Brindle contended that the position of the BBA was not that the Principles had no application to PPI sales at all. The BBA argument had to be that the specific rules excluded the operation of the Principles in relation to certain factual situations. This, he submitted, was close to the FSA position, albeit expressed as the obverse, which was that there were certain factual situations in the course of PPI sales where the rules did not cover the point, regulatory gaps, and so recourse could be had to the Principles. It was not the FSA's case that it would seek to enforce the Principles where to do so would conflict with specific rules passed on the same subject. Its difficulty arose with what the BBA meant by its argument that the Principles could not be used to augment the specific provisions of the rules, short of a conflict with them. This was to the FSA the opening up of the regulatory gap which lay at the heart of its concerns about the BBA arguments.

131. The FSA was also concerned that these regulatory gaps would increase if Principles were excluded from any role on the basis that specific rules had been created to cover some aspects of the sales process. This would mean that specific rules would be required to govern every aspect of a sale, when not every method, least of all one devised with the avoidance of the rule in mind, could be anticipated and provided for.

132. Mr Brindle relied on the decision of the Divisional Court in *Re a Solicitor and the Solicitors Act 1974*, 21 February 2000. This was an appeal against the findings of a Solicitors Disciplinary Tribunal that a solicitor had been guilty of two specific failings in not dealing speedily with taxation and correspondence, and a third allegation that those failings meant that he was also guilty of "conduct unbecoming a solicitor". It was argued on his behalf that in the absence of specific rules requiring a solicitor to deal with those matters speedily, he could not be found guilty of the third charge of unbecoming conduct. The three judge Court rejected that as entirely misconceived. Coleman J said:

> "The purpose of Professional Conduct Rules, (which operate in relation to solicitors as with the Professional Conduct Rules operating in relation to most other professional bodies) is to identify in particular those areas of conduct in respect of which there should be specific prohibitions or requirements because they are likely to represent the most prevalent situations and the most prevalent conduct then in the profession. The fact that such a particular area of conduct is specifically dealt with does not mean that all other conduct is permissible or within the standards of the profession. It is thus ordinarily open to professional disciplinary tribunals to apply sanctions for professional misconduct generally, regardless of whether it is conduct singled out for mention in the rules. Were it otherwise, professional people might be permitted to conduct themselves in plainly deplorable ways without any disciplinary control."

133. Lord Pannick pointed out that that case did not deal with conflict between specific and general rules or the augmenting of a specific rule by a general rule; rather the issue arose because of the absence of a specific rule in the first place.

134. Mr Brindle submitted that the inclusion of the limiting requirement in the ICOB 2.2.3(1)R restatement of Principle 7, that a breach of the specific rules only arose if reasonable steps were not taken, reflected a judgment by the FSA that if the rule were to be actionable, as the restatement of it would be, there should be such a requirement. The role of the Principle was not exhausted by the restatement but it was of no great consequence if it were, since it reflected what PRIN 1.1.7G said about the application of the Principles: that it would be for the FSA to prove fault on the part of the firm before finding that an unrestated Principle had been breached; see paragraph 29 above.

135. Mr Brindle submitted that the examples relied on by Mr Flint and drawn from ICOB 3, 4 and 5 had not used a "restatement" of Principles unlike ICOB 2, but had used the language of "amplify" and "reinforce" to describe the role of specific rules in relation to the Principles. That language showed particularly that the specific rules could not be interpreted as exhausting the role of the Principles.

136. Mr Brindle pointed out that it was not the BBA case that the Policy Statement had requested something to be added to the policy summary which the specific ICOB rule on the content of a policy summary did not require, still less that it required the addition of something that the rule required it to omit or the omission of something it should contain. He accepted that any use of the Principles to require a topic to be added to the summary could well be to use the Principles to create conflict, which was not the purpose of their use by the FSA. The BBA complaint was about the use of the Principles to require a greater degree of oral communication about certain aspects which might be ignored in an oral presentation. That was an amplification of the specific rules, so that any oral presentation was fair. And no firm could have thought that it was entitled to make an unfair oral presentation. The Policy Statement and common failing 15 in the Open Letter were drawing attention firmly to that point. There was nothing new in this approach to the use of the Principles. One of the difficulties in the way of the BBA argument on the illegitimate role of the Principles was that the specific rules had to be read together. ICOB 2.2.3R was a restatement of Principle 7, save for the words "reasonable steps", and what a firm had to do or not do under, say, ICOB 5.5.3R would be governed by ICOB 2.2.3R, even if the Principles had no further role.

137. The FSA agreed that it did not in fact see the rules and guidance as exhausting the implications of the Principles, and that it thought that the Principles should be used even where there were specific rules, as it had made clear in its consultation response, CP 10/6. This was in large part because it said that it had made clear the role of the Principles in the Handbook itself. There was nothing in either ICOB or ICOBS which stated that they were exhaustive of the Principles and constituted the entire and complete statement of all the obligations of firms in relation to insurance policies which fell within its scope.

138. Nor had the FSA ever suggested that that was how the specific rules were to be seen. It had always said the contrary. The FSA had for many years made its position clear on the role of the Principles, and had not adopted a new position on that with the

Policy Statement. It had emphasised them as "independent and inexhaustible", to use the phrase of Ms Sinclair, Head of Department of the Conduct Risk Division of the FSA. She gave the example in 2004 of the FSA document addressed to the senior management of regulated firms and entitled "Treating customers fairly – progress and next steps". The high level principles were key to the operation of an efficient retail market for financial services; the principle of fair treatment for consumers had to be embedded in the operations and culture of firms. Firms were told themselves to supplement the detailed rules by a thoughtful implementation of the high level requirements of fairness; the FSA did not want to press on with ever more detailed and intrusive regulation. It was the detailed rules which supported the high-level rules. This was again made clear during the consultation in 2007 on the amendments to ICOB, which became ICOBS.

139. Mr Brindle rejected the BBA argument that if the FSA were right, there would be no need for detailed rules at all. It would have been unwise for a regulator to rely simply on high level Principles alone, and in any event the specific rules enabled a consumer to bring an action based on them which he could not do on the Principles alone. Specific rules on PPI sales were retained or added where necessary to deal with well-demonstrated failures, and to bring about change to the behaviour of firms.

140. Ms Sinclair gave illustrations in her Witness Statement of the regulatory gap which the BBA's contention would open up. There is no specific ICOB rule which prohibits the selling of a PPI policy to someone who can never claim under it, even where the seller knows that to be the case. Such conduct would be covered by Principles 1, 3 and 6, but not if the BBA argument were correct since there were specific rules governing the sale of PPI policies. There is no specific ICOB rule which prevents the non-advised sale of a PPI policy where the cost of the premium plus interest payable, when added to the loan, exceeds any amount which could ever be paid out under the policy. Yet that would engage Principles 1 and 6. There is no ICOB rule which prohibits, on a non-advised sale, the sale of a single premium PPI policy with a refund provision which is not proportionate to the duration of the policy where the seller knows that it is likely that the loan to which the policy was related would be refinanced shortly after the policy was taken out. This would be a breach of the Principles as explained in common failing 15. She accepted that all such conduct might, on particular facts, involve breaches of specific rules in ICOB. The first example was used by Mr Brindle to test the true position of the BBA: was it saying that this could be dealt with by the application of the Principles, or that the application of the Principles had been exhausted by the specific ICOB rules? If the former, then the application of the Principles was accepted by the BBA and its point was limited to a debate, which it was agreed was not fruitfully for resolution by this court, as to which factual situations gave rise in practice to the application of conflicting or exhaustive specific provisions.

141. Mr Flint denied that these examples showed that there was any regulatory gap: Principle 1 was not inconsistent with ICOB, and was always available to protect the customer from the salesman who sold a policy from which he knew the customer could not take any benefit. Principles 6 and 7 could not however be used to add to the content of the ICOB rules on substantive information requirements, since that would

be inconsistent with the specific rules. Nor should an extreme example be used as a basis for asserting a general duty to give advice. The second example would apply rules on advised sales commission disclosure to non-advised sales as well.

142. In any event, submitted Mr Flint, this concern about a regulatory gap was misplaced: the FSA could take enforcement action if the acts breached the Principles construed conformably with the rules. But it was necessarily assumed by the FSA that the Principles could be breached even if the specific rules were complied with, so the Principles were being wrongly used to create a conflict with the rules. The last example given above illustrated the point since there were provisions about disclosure in the policy summary, and so there was no reason why compliance with those rules should still leave a firm liable for breach of the Principles. It would be open to the FSA to make specific rules if it thought that necessary.

The FOS submissions

143. Mr Malek for the FOS contended that it had not had a case in which the Ombudsman had concluded that a firm had indeed complied with the specific rules in ICOB, but had upheld a complaint on the basis of the Principles, beyond those restated in ICOB. The FOS had delivered tens of thousands of PPI sales-related decisions over the last two years, and no firm had ever raised such an issue, nor had a firm sought to challenge a finding on that basis. This could well be because under ICOB and ICOBS, the incorporated but restated Principle 7 and the effectively incorporated Principle 9 meant that such an argument would not arise. Mr Malek instanced a policy summary which complied with ICOB 5.5.5R, but which failed ICOB 2.2.3R since an important point was hidden away amidst a great deal of other information, or provided in very small print.

144. The decisions which I was shown however did not enable me to come to so confident a conclusion. They were characterised by general references to the Online Resource material and conclusions as to whether material was clear, fair and not misleading. They did not contain any clear analysis of whether there had been compliance with a specific rule or not, or whether the finding, which from its terms could have been based on a Principle, was in fact based on one notwithstanding compliance with the specific rules. In other words, the FSA contention that it would not rely on the Principles to create conflict was not an approach which could necessarily be discerned from the Ombudsman's decisions which I saw; and I believe I saw a selection of typical decisions.

145. However, as Mr Malek's analysis of them did show, the heart of the decisions did reflect requirements of rules other than Principles, and it would be wrong to analyse them without recognising the importance to them of ICOB 2.2.3R, the restatement of Principle 7.

146. There had been no challenge to an FOS decision on the basis that the FOS was simply treating all types of sale, advised and non-advised, distance or face to face, in the

same way notwithstanding the obvious differences between them. Nor had there been a challenge to the way in which the FOS used the Online Resource over the years of its existence until September 2010.

147. The increase in the percentage of complaints upheld on PPI sales was not caused by a change in approach by the FOS in reliance on the Online Resource or Principles - it denied any such change; it was caused by a change in the nature of the complaints from rejected claims to sales procedures. The Online Resource reflected what by November 2008 was already the FOS practice and contained no new advice to the public as to how complaints would be handled.

148. Mr Malek supported the FSA approach to the need for high-level overarching Principles since there could develop otherwise what he called a "tick box" mentality among sales staff, when the variety of personal and sales circumstances and sale techniques would mean that the overriding duties to treat customers fairly would be by-passed.

149. The FOS had long regarded it as important that oral presentations should be fair, with drawbacks and limitations pointed out, if advantages were being explained as well. Mr Malek doubted that the BBA were really saying otherwise. The BBA had misunderstood the significance of the discussion of the Principles in the Online Resource in this respect. It did not require the oral disclosure of all the information which had to be in writing; it was concerned that any oral presentation should be balanced. An unbalanced oral presentation would probably not be cured by a balanced written document which the customer took away with him. It would be wrong to treat the only question for the FOS as being whether the firm complied with a specific ICOB rule on the presentation of written information regardless of what the salesman said of the advantages and disadvantages, even if nothing that he said was of itself actually wrong.

150. He instanced a policy knowingly sold to someone whose age meant he would never be eligible for its benefits, even where sufficient information had been given to enable an informed choice. This would involve a breach of Principle 1, integrity, as well as being a breach of the duty of utmost good faith on both parties to an insurance contract under the general law. It would also involve a breach of Principle 7.

151. Mr Malek did not rule out that the Ombudsman would uphold a complaint where the specific rules had been complied with but a Principle had still been breached, as Lord Pannick accepted could be lawful but only exceptionally. Quite apart from circumstances which did not really illustrate that point since compliance with a detailed rule in ICOB would not necessarily mean that the restated Principle 7 in ICOB 2.2.3R had been complied with, neither this restatement nor the effective incorporation of Principle 9 into ICOBS could mean that the FOS should then ignore the Principles. Once the Principles were relevant, the weight which should be attached to them in any particular case was for the Ombudsman.

152. So there was a difference between how the FOS saw its role in relation to Principles and how the FSA saw them; the FOS did not accept that its statutory duties would prevent it upholding a complaint on the basis that that was fair and reasonable, even where there was a conflict between specific rule and Principle, although it did not believe that such a situation had arisen.

153. Besides, submitted Mr Malek, the Ombudsman's duties under s228, to decide complaints on the basis of what was fair and reasonable could not lead to him being circumscribed by what did and did not augment the rules or add further obligations. The width of this duty and the material relevant to his decisions, including the general law, to a large extent mirrored in the Principles, and codes of industry practice, showed that whatever constraints the FSA might be under in relation to the Principles, those constraints would have no practical effect on the way in which the FOS was duty bound to carry out its functions.

Conclusions on the second main issue

154. I start with a few preliminary observations. There was a considerable dispute on paper between the FSA and BBA about the extent to which the common failings could truly be said to illustrate breaches of existing specific rules. The FSA said that "pretty well" they all could; the BBA gave numerous examples of where it said they could not. These were all part of the argument that the Open Letter was using the Principles to create conflict with the specific rules or illegitimately to augment them. Neither side wished me to resolve all those precise issues of interpretation and application seriatim, for which I am grateful. It was agreed to be sensible for me to deal with the examples put forward by Mr Flint and Mr Brindle. The form of any relief would then depend on the views I expressed in this judgment. This however has not made it straightforward to focus on a precise or concrete error of law.

155. It was not said that any existing rules are unlawful, or that the amended DISP provisions of the Handbook are unlawful in the sense of being ultra vires. It was not said either that any powers had been abused. The Principles have co-existed for years alongside specific ICOB rules, without giving rise to any identified problems of interpretation or application either by the FSA or by the FOS.

156. The issue about how the general Principles and specific rules inter-relate arises now because the package of measures in the Policy Statement includes amendments to the DISP section of the FSA Handbook, and the Open Letter common failings. Firms now have to have regard to the substantial flaws and common failings in deciding what acts or omissions constitute a breach of an obligation leading to redress. The general Principles underlie the determination of what these flaws and failings are, and the provision of redress for them. The FSA is explicitly interpreting and applying the Principles and common failings as well as the specific rules. The FOS is doing likewise.

157. I am far from clear that this is a change of approach at all on either of their parts. Indeed it appears to me very likely that this represents no change at all on the part of the FOS, even though the particular identification and role of the common failings is new. However, what the Policy Statement has made explicit and emphasised, if it were not clear already at least in relation to the Principles, is that the FSA and FOS do not interpret or apply the specific rules as if they were an exhaustive statement of the firms' obligations in the areas to which the specific rules operate, and even compliance with them may not prevent an obligation being breached. The change to my mind is one of emphasis in the expression of what has always been the FSA and FOS approach. No recent FOS decision was pointed to as clearly embodying the asserted error.

158. The nature of the argument that the general Principles cannot be used to "contradict or augment" the specific rules where they are the embodiment of the Principles to the extent the FSA thought appropriate, or where the specific rules "occupy the field" to the exclusion of the general, requires examination in principle and in practice. Mr Brindle accepted that the Principles could not be used to contradict the specific rules, although there is obvious scope for debate about what adds to and what actually contradicts a specific rule. He also appeared to accept that there might be circumstances in which the true construction of the rules meant that they had in fact covered every aspect of the Principles. But no examples were put before me which he agreed amounted to a contradiction of a specific rule by a Principle or to a Principle being applied where the specific rules had exhausted all scope for its application.

159. It was common ground that not all the Principles were affected by the BBA argument, notably but not exclusively Principle 1. It seems to me also that whatever the true scope in practice of the argument that the Principles could not be used to "contradict or augment" the specific rules, the argument at best only applied where the specific rules were or purported to be the full implementation of the Principles to the extent that the FSA had thought appropriate. Where those rules were not and did not purport to be the complete expression of the Principles so far as desired by the FSA, the use of a Principle to add to the specific provisions of rules, was lawful even on the BBA argument.

160. There was a certain amount of shadow-boxing, or coyness, in the submissions of the three parties to the argument. I was not clear that the parties were in reality all that far apart in what they thought were legitimate outcomes from their arguments. Mr Brindle challenged the BBA to say whether it would accept various situations in which the FSA contended that the BBA argument would lead to a regulatory gap which no sensible person would accept. The BBA answer was to deny that its submission would create such a gap, or that it could be filled by specific rules if necessary. It may be rare, even unheard of, as Mr Malek suggested, for the situation to arise where a firm has been required to pay compensation for breach of a Principle where it has complied, for example, with the obligations to take reasonable steps, and the Principle is interpreted as requiring it to do more. The FSA and FOS arguments were notable for the denials that the Policy Statement would have the effect asserted by the BBA. Mr Brindle placed considerable emphasis on the effect of ICOB 2.2.3R as showing that common failing 15 went no further than what the ICOB rules already

required. The BBA's arguments conversely were notable for denials that they would create the regulatory gaps and problems asserted by the FSA and FOS.

161. I turn to the substance, dealing first with the general approach. In my judgment, and fundamentally, the BBA analysis rather puts the issue the wrong way round when it contends that the Principles cannot be used to contradict or augment the specific rules. The relationship between them has to be determined by understanding the true role of the Principles. The Principles are the overarching framework for regulation, for good reason. The FSA has clearly not promulgated, and has chosen not to promulgate, a detailed all-embracing comprehensive code of regulations to be interpreted as covering all possible circumstances. The industry had not wanted such a code either. Such a code could be circumvented unfairly, or contain provisions which were not apt for the many and varied sales circumstances which could arise. The overarching framework would always be in place to be the fundamental provision which would always govern the actions of firms, as well as to cover all those circumstances not provided for or adequately provided for by specific rules.

162. The Principles are best understood as the ever present substrata to which the specific rules are added. The Principles always have to be complied with. The specific rules do not supplant them and cannot be used to contradict them. They are but specific applications of them to the particular requirements they cover. The general notion that the specific rules can exhaust the application of the Principles is inappropriate. It cannot be an error of law for the Principles to augment specific rules.

163. That role for the Principles has been clear from the language describing their role in the Handbook; see PRIN 1.1.7G to 1.1.9G, and paragraphs 29-31 above. That was also clear from what the FSA said in the 1998 Consultation Paper and the Supplementary Memorandum on which Lord Pannick relied in submission on the first ground.

164. If the question, as posed by Lord Pannick's submission, makes the intent of the FSA in promulgating the rules relevant to the question of their construction in this respect, it is plain that no such exhaustion of the Principles was intended in the making of specific rules. The FSA was very clear before and in the Policy Statement about that: the Principles remain the overarching source of obligations.

165. It was not suggested that the relationship intended by the FSA between Principles and specific rules was ultra vires the Act, or an abuse of power. It is perfectly possible for specific and general rules to have the relationship for which it contends. The relationship for which it contends is explained in the Handbook. I find it very difficult to see what error of law there can be in a rule-making regulator explaining that intention and giving effect to it, unless the language it has used precludes it.

166. It follows that there is no reason in principle why the specific obligations in the rules should not be subject to the wider role of the Principles. The specific obligations are not to be seen as exhausting the requirement to comply with high level Principles.

The unhelpful concept of the specific rules "occupying the field" is inapt to express the true position. The Principles "occupy the field"; they stand over the specific rules. It is the general performing its role as the overarching requirement which cannot be displaced by compliance with specific rules if the overarching requirement is breached. Since the correct starting point is that the Principles govern the sales activities of the firms at all times, the real question is whether there is any reason to interpret a specific rule as excluding the general so that a breach of the Principles goes unredressed, even though a specific rule has been complied with.

167. I turn now to the specific examples given by the parties. The BBA's first example related to ICOB 2.2.1G which describes ICOB 2.2.3R as restating in an amended form that part of Principle 7 which relates to the "communication" of information, rather than what information has to be communicated. It does so by stating a requirement that reasonable steps be taken to communicate in a clear, fair and not misleading way, where Principle 7, unrestated, would have left the obligation unqualified. The FSA's chosen language of "restatement" is an indication that it removed the broad effect of Principle 7 where the "restatement" applies.

168. To a lesser extent the same point can be made in relation to ICOB Chapters 3 and 4 for example where in 3.5.2G(2) and 4.1.6G(1) specific rules are described as "amplifying", and in ICOB 5.1.9G as "reinforcing" e.g Principles 6 and 7. There are specific rules which require only reasonable steps to be taken in relation to the fairness of the content of what is communicated rather than its manner, where Principle 7 "unamplified" or "unreinforced" would have left it unquantified.

169. I conclude that it would be wrong to construe either set of provisions as exhausting the role of Principle 7 or as meaning that any wider application of Principle 7 necessarily contradicted a specific rule. First, given what I accept is the explicitly overarching role of the Principles, I would expect the clearest possible language in ICOB to show that Principle 7 had been rewritten so that its reach in relation to communication requirements had been so radically altered throughout this area. Second, I accept Mr Brindle's explanation that this qualification was introduced because the rules containing them were to be actionable whereas the Principles were not. This is borne out by ICOBS 4.2, and by ICOB 2.2.1G. The Principle was restated for the purpose of making it actionable, not to limit its overall regulatory scope. Principle 7, unrestated, is as applicable in non-actionable regulations as is Principle 1, the continuing applicability for which was not at issue. The language of the restatement does not say that "only" or "no more than" reasonable steps are to be taken. There is no express limit on the language of Principle 7 for all regulatory or redress purposes.

170. It would be too sophisticated or muddling an approach to distinguish significantly in effect between "restatement" and "amplification" or "reinforcement". It is only the word "restatement" which gives real room for the BBA argument, for which an answer is readily available. "Reinforce" is an odd word to use for the introduction of the qualification. But "reinforce" and "amplify" are clearly used to mean that the generality is being given particularised expression rather than diminished scope.

171. Accordingly I do not regard a requirement to take reasonable steps in relation to the "communication" limb of Principle 7 as precluding reliance by the FSA or FOS, on Principle 7 unqualified, as a matter of the construction of the rules taken as a whole. This would also apply to any other specific requirement to take reasonable steps where a Principle was more widely expressed.

172. In the end, for the reasons given by Mr Brindle, this example of differences in approach may not amount to much of a difference in practice. The effect on the FOS would be to a degree different anyway, as I shall come to. But I regard it as unsatisfactory, in what is anyway something of an unsatisfactory form of argument but seeking to give what useful decision I can, to resolve issues as to the significance of the deliberate listing of substantial flaws and common failings, which at least in part draw on the Principles and are not confined to specific rules, on the basis that it may be difficult to see in practice where they go beyond ICOB 2.2.3.R. Indeed, ICOB 2.2.3R can itself give rise to a scaled down version of the BBA's argument in relation to the specific rules in ICOB: are its general terms excluded where more detailed rules exist? So I am concerned to decide the principles of how these various rules inter-relate.

173. Mr Flint submitted that common failing 15, supported by example 12 in new DISP Appendix 3.6.2E, went further than the specific rules in ICOB 5.3.1.R and 5.5.5R, which require a written policy summary and require it to include significant and unusual exclusions and limitations, in that it required firms to regard as a "significant and unusual" limitation the fact that early termination of the policy would not lead to a return of premium proportionate to the duration of cover whenever that was likely to be relevant to the customer. This would have to be disclosed orally since it was a common failing not to disclose that. This submitted Mr Flint was likely to be all single premium cases, and I accept he is likely to be right as to how it will be seen.

174. I accept that this goes further than the specific rules do; it does not contradict them; but it augments them, to use the language of the BBA submissions. That is lawful in my judgment. It exemplifies the FSA's view that the Principles may require this oral disclosure, depending on the circumstances, even though the specific rules do not. This is not an illustration of the Principles or DISP amendments contradicting specific rules: it requires nothing to be done that specific rules forbid, or omitted which they require. It does not require it to be treated as a significant and unusual limitation and put in the policy summary. It may require oral disclosure in an oral sale. The FSA is entitled to draw on its experience and that of the FOS in handling complaints to conclude that a non pro rata return of single premium is a term which may require oral disclosure in what may well be the generality of cases. In my judgment, the DISP amendments and the Open Letter common failings are being used to bring out what the Principles, read with specific rules, require in particular instances. By specific rules, I do not mean ICOB 2.2.3R. I have already dealt with its effect, as a restated Principle. Principle 7, unqualified, and common failing 15 may or may not add significantly to the effect of ICOB 2.2.3R. But if they do, that effect, lawful in my view, is not excluded by the existence or terms of the specific rules.

175. Mr Flint contended that examples 4 and 12 or common failing 15 also required more than ICOB 5.3.1R in another way. ICOB 5.3.1R required, in an oral sale, that the relevant information be in the Policy Summary which the customer should be told it was important to read. Examples 4 and 12, and common failing 15, additionally required that any oral presentation be balanced. It should deal with limitations as well as advantages, describing the whole policy in balanced and fair terms. This was seen as a contradiction of the specific rules by Mr Flint, and if not, it was an augmentation of them where they had exhaustively provided for what information had to be conveyed on an oral sale.

176. I disagree that it is a contradiction. The Handbook amendments and Open Letter do not require something to be omitted or done which the rules require or forbid. The specific rules are silent on the topic of how oral presentations should be conducted. There can be no contradiction of the specific rules unless they are construed as the exhaustive expression of all obligations. There is no justification for such a construction in the absence of clear wording giving effect to a clear purpose or intention of such an outcome. The overarching or underlying Principles are simply being applied where the rules do not cover the point.

177. The nature of an oral presentation or sales pitch is not covered by the specific rules. ICOB 5.3.1R only requires the attention of the customer to be drawn orally to the importance of reading the policy summary. I do not see any contradiction at all between that ICOB rule and the common failing standard which deals with the problem, left unattended by the specific rules, of how far a salesman can go in explaining the advantages and value of the policy without explaining the drawbacks. Of course, it adds to the rules in the sense used by BBA. But this could not possibly be seen as an area of selling in which the rules had made specific provision for oral sales, intending to exhaust the scope of Principles 6, 7 or 9, leaving the whole regulation of what might be said to the operation of Principle 1. It is actually a very good example of why the FSA approach to the role of Principles is correct, and illustrates the need for an overarching framework from which the specific rules are drawn without exhausting the ability of the Principles to cover gaps in the regulatory framework to deal with new techniques, unforeseen circumstances, sales methods otherwise unregulated and changes to sales methods in response to specific rules. I repeat the point I made at the end of paragraph 174, for the avoidance of doubt

178. To my mind, the three examples given by Ms Sinclair further show that the FSA approach is right; in so far as the Principles add to the specific rules so as to deal with those situations, it shows that they should do so. They do not contradict rules, but add to them to cover areas which are not covered specifically. I found Mr Flint's answers unpersuasive. If Principle 1 would cover the sale of a policy where the customer could never claim under it to the knowledge of the seller, along with the general law, as he contended, I see no substance in the point that Principles 3, 6 and 7 should not also apply to it. If only Principle 1 applied, there is an obvious gap in the general regulation unless Principle 1 is pressed into service to cover the territory of other Principles.

179. To my mind there is an obvious regulatory gap if everything depends on the scope of Principle 1, but if it has the width which Mr Flint seemed to feel bound to give it, there is little substantive effect in his point that other Principles, including Principle 7 as restated cannot perform the same necessary task. But if he is wrong about the scope of Principle 1, he leaves a large gap. I do not think that the style of regulation should be required to become one of detailed regulation of every point simply because on what may be an ad hoc basis, certain aspects are subject to detailed provision.

180. I regard his point that to require disclosure of the fact that the cost of the policy exceeded any recoverable benefit would turn a non-advised sale into an advised sale, and would now require commission disclosure that was only required by the rules on an advised sale, as something of an over-statement of the effect of the changes. Indeed, these answers helped persuade me of the justification of the FSA's concern about the width and number of regulatory gaps, which the BBA arguments would create.

181. I do not accept the BBA approach which is that if specific rules are made for a type of sale but omit certain aspects of it, those aspects become matters for the choice of firms and are unregulated save by those Principles which have not been expressly referred to in the rule.

182. I did not find authority of great assistance here. *Re a Solicitor* is distinguishable, but does offer some assistance in how one should approach the relationship of the particular to the general in the regulatory sphere. I do not agree with HHJ Waksman in *Harrison v Black Horse Ltd* that ICOB should be seen as detailed code which is necessarily co-terminous with and thus fully expressive of any duty of care, if the first part of the judgment I have cited means that. He defines the duty of care as co-terminous before concluding that it cannot be wider. His decision is however obviously right for the reasons which he then gives as the "fundamental point".

183. However, the position of the FOS is to a degree different, as Lord Pannick accepted. The *Heather Moor & Edgcomb* decision is of value to the FOS. Lord Pannick accepted it showed that, exceptionally, the FOS could hold that a firm should pay compensation for breach of the Principles even though it had complied with the specific rules, and even where the two were in conflict. Mr Malek was keen to show that that had not occurred, although as Mr Flint pointed out, that was not at all clear from the way in which the determinations were structured.

184. The width of the Ombudsman's duty to decide what is fair and reasonable, and the width of the materials he is entitled to call to mind for that purpose, prevents any argument being applied to him that he cannot decide to award compensation where there has been no breach of a specific rule, and the Principles are all that is relied on. Even if I were to accept the BBA argument that the FSA could not use the Principles to contradict or augment the specific provision where they were exhaustive of the application of the Principles, that would not prevent the FOS deciding that it was fair and reasonable to treat the firm as having breached an exhausted or contradicting

Principle, and require the payment of compensation. If for example there were limitations on the FSA created by the restatement of Principle 7 in ICOB 2.2.3R and 3.2.1G, or amplifications, they would not inevitably constrain how the FOS must decide complaints. That would involve no necessary error of interpretation by the FOS. That would simply be the consequence of a decision as to what was fair and reasonable. It would involve the FOS deciding that one of the conflicting provisions was the dominant provision, or that there were aspects of the Principles which were not adequately or fully represented in the specific rules. But I see no reason why he should not so decide, or why that should involve misinterpreting the provisions. It involves giving them meaning and weight according to his special function.

185. I do not accept that this is something which is lawful if it is only done exceptionally. That can only be an expectation that the circumstances which warrant it will be very infrequent, which is what I too would expect. But if it is lawful, as Lord Pannick accepted, it can be done whenever and how often circumstances warrant it.

186. I would also accept that if the FOS is to find against a firm, which has complied with the relevant specific rules, on the basis of a breach of the Principles or common failings, the Ombudsman must explain that that is so, and give adequate reasons for his decision. If Mr Flint is right that the decisions he showed me involved adverse findings against firms which had complied with the relevant specific rules, and I commented on this above in paragraph 145, then the degree of reasoning appears legally inadequate, at least on my provisional view. What is a theoretically lawful decision as a matter of construction of the rules, may be neither fair nor reasonable on their properly reasoned application to particular facts.

187. I would not have refused relief on the grounds of delay if I had concluded that the FOS was applying and continuing to apply a legally erroneous construction of the rules since that ongoing error would have needed correction for the future as Mr Malek accepted. I would not have granted any relief which affected its past decisions, requiring it to carry out a review of past findings.

188. Accordingly, I reject the BBA's second ground.

Ground 3: the s404 scheme

189. Mr Fordham developed these submissions for Nemo, the Interested Party, which Lord Pannick for the BBA adopted. His essential submission was that s404 "occupied the field", to use the language in which this and part of the second main submission was couched, so that if the FSA perceived a problem which fell within the scope of s404, and thus for which s404 provided the remedy with safeguards for those affected, it could only deal with that problem by proceeding under s404, and not by any other method. On the facts here, the problem which s404 was designed to address had arisen in the eyes of the FSA, and its decision to proceed other than under s404, using instead the Policy Statement and the Open Letter Standards was unlawful. The

general powers of the FSA were not to be used to avoid the restrictions and requirements of s404.

The statutory provisions

190. Until 11 October 2010, s404, headed "Schemes for reviewing past business", provided for a scheme to be made if the Treasury authorised the FSA to establish and operate one. It could only authorise that if it were satisfied of certain matters, and there were procedural requirements to be followed. The scheme involved consideration as Mr Fordham put it, of failure, liability and compensation. This sort of provision was first introduced in the FSMA. The question of what arrangements were appropriate would be informed by the statement of functions in s2, and by the considerations relevant to the exercise of those broad functions, including proportion between burdens imposed for benefits gained. The scheme then took effect, in relation to its consequences for firms, as if it constituted rules by which firms were bound. There was no provision enabling the procedures to be short-circuited in the event of some urgency.

191. Thus s404 provides:

> "(1) Subsection (2) applies if the Treasury are satisfied that there is evidence suggesting-
>
> (a) that there has been a widespread or regular failure on the part of authorised persons to comply with rules relating to a particular kind of activity; and
>
> (b) that, as a result, private persons have suffered (or will suffer) loss in respect of which authorised persons are (or will be) liable to make payments ("compensation payments").
>
> (2) The Treasury may by order ("a scheme order") authorise the Authority to establish and operate a scheme for-
>
> (a) determining the nature and extent of the failure;
>
> (b) establishing the liability of authorised persons to make compensation payments; and
>
> (c) determining the amounts payable by way of compensation payments.

> (3) An authorised scheme must be made so as to comply with specified requirements.
>
> (4) A scheme order may be made only if-
>
> (a) the Authority has given the Treasury a report about the alleged failure and asked them to make a scheme order;
>
> (b) the report contains details of the scheme which the Authority propose to make; and
>
> (c) the Treasury are satisfied that the proposed scheme is an appropriate way of dealing with the failure.
>
> (6) For the purposes of this Act, failure on the part of an authorised person to comply with any provision of an authorised scheme is to be treated (subject to any provisions made by the scheme order concerned) as a failure on his part to comply with rules."

192. By s429(1) an order authorising the establishment of a scheme had to be placed before Parliament for approval by resolution of each House.

193. S415A, from April 2010, read: "Any power which the Authority has under any provision of this Act is not limited in any way by any other power which it has under any other provision of this Act."

194. The new s404, in force from 11 October 2010, provides for "consumer redress schemes" in essentially similar circumstances and with essentially the same aims. The procedures are different in that the Treasury and Parliament are no longer involved in the formal procedures; it is the FSA which makes the scheme, but by s404D, the rules of the scheme can be challenged before the Tribunal. Just as s404(1)(b) only applied where the loss suffered is actionable loss, so too does the new provision. Consumer redress schemes cannot therefore be used, as the FSA agreed, for breaches of Principles. Guidance issued by the FSA in July 2010, in connection with the coming into operation of that new provision, envisaged a number of options as to how a consumer redress scheme might be operated. These included requiring firms to undertake a pro-active review of all cases falling within the period covered by the scheme (to which Mr Fordham attached some weight), and an opt-in provision for customers whom the firm had been required to contact.

195. The DISP rules in the FSA Handbook contained provisions dealing with what it called "root cause analysis". In respect of the sort of complaints which underlie this case, DISP 1.3.3R, from 2007, provides that a firm:

> "must put in place appropriate management controls and take reasonable steps to ensure that in handling *complaints* it identifies and remedies any recurring or systemic problems, for example, by:
>
> (1) analysing the causes of individual *complaints* so as to identify root causes common to types of *complaint;*
>
> (2) considering whether such root causes may also affect other processes or products, including those not directly complained of; and
>
> (3) correcting, where reasonable to do so, such root causes."

196. Guidance in DISP 1.3.5G, from November 2007, says that a firm should have regard to Principle 6, concerning fair treatment for customers when it identifies such problems, and consider of its own initiative whether it should provide redress to those who had not complained. So DISP 1.3.3.R was taken by this Guidance beyond the use of complaints by firms as a tool for discovering, analysing and addressing deep-seated problems.

197. Mr Fordham contended that the historical context for s404 was relevant to its construction. In order to show what range of schemes were within s404, how broad was its scope, and the extent therefore of the field for which it made what he contended was exclusive provision, I was shown what had happened on industry-wide reviews of past business relating to pensions products before the FSMA 2000. These were said to be relevant because, by the Financial Services and Markets Act 2000 (Transitional Provisions) (Reviews of Pensions Business) Order 2001 No 2512, made under the FSMA, reviews of past business in relation to pensions and free-standing additional voluntary contribution schemes were continued as if they were schemes under s404. The *"pension review provision"*, which by Article 2(3) *"has effect…as if it were a provision of an authorised scheme within the meaning of s404…subject to any modifications later made in accordance with article 6…"* meant any legislation and any other provision including written guidance providing for a review, or relating to its conduct, or taking other steps with respect to selling pensions. Mr Fordham emphasised "the taking of other steps" with respect to pension and FSAVC schemes. So the general powers which had been exercised before 2000, were now subsumed within s404, and not some other general rule-making power. These reviews were not all mandatory, were quite flexible in approach, contained filter mechanisms, their conduct was dominated by guidance; and their aim was to achieve appropriate redress for customers, where there was a problem widespread in the industry, through a review by the firms of their past business. But since they all were now deemed to fall within s404, the scope of s404 had to be broad enough to encompass them. Its scope was not limited to compulsory reviews initiated by the FSA and Treasury through the procedures laid down in the section.

198. Although the provisions, which governed the reviews begun before s404 came into force, were dominated by guidance, one pre-2000 Act regulator, the PIA, did make a rule enabling it to require the review of past business in broad and general terms. Mr Fordham contended that, after the enactment of s404, it would have been inconceivable that the FSA should possess similarly broad rule-making powers under Part 10 of the FSMA, given the purpose of s404.

199. Mr Brindle denied any value in the previous review provisions since they were only deemed to be schemes, and failures to comply with the provisions were to be treated as failures to comply with rules. Guidance became rules. When the 2000 Act came into being, the reviews then underway had to be given a firm statutory base. So although the former schemes were guidance based and not compulsory, they were given a rough and ready berth under s404. He contended that the phasing of the former pension reviews did not fit readily with the way in which a true s404 scheme would work, which would require universal coverage of the firms engaged in the "particular kind of activity", although as the scheme worked through to liability under s404(2)(b), there might be some who would drop out.

200. In 2003, in the course of a Note produced by the FSA for public consumption on what did or did not constitute misselling, the FSA dealt with concerns about retrospective redefinition of regulatory requirements in the context of reviews of past business. The Note contrasted the past Pension Review with a more targeted firm by firm review of past sales, and continued:

> "Since 2001, section 404 of FSMA has reserved to the Treasury the ability to authorise the FSA to establish any industry-wide review of past business. The Act provides that HM Treasury would need to be satisfied that there had been widespread or regular failure and that private persons have suffered (or will suffer) loss. This takes the burden of proof way beyond incidental shortcomings within particular firms. Moreover, the Act requires the Treasury to proceed by way of specific Order, which must be approved by both Houses of Parliament. The FSA is therefore not able, as previous regulators were, to order industry-wide reviews of past business on its own account."

The factual background

201. I have already set out the important FOS letter to the FSA of 1 July 2008; paragraph 41. The Executive Summary of the Policy Statement 10/12 said that the package of measures stemmed from the FSA's serious concerns about "*widespread weaknesses in previous PPI selling practices and the detriment such selling was likely to have caused to a significant number of consumers; and the industry's poor handling of the increasing volume of PPI complaints, and its neglect of root cause analysis and fairness obligations toward non-complainants.*" It emphasised that the package should be seen in the context of the FSA's wider strategy and work concerning weaknesses in past PPI selling practices. This included enforcement action in 24 cases

leading to fines totalling £12.6m and past business reviews, and other past business reviews agreed with several major firms.

202. The consultation process led the FSA to the following conclusions:

> - "we have made a reasonable analysis of the benefits, and a reasonable estimate of the ranges of costs and of the wider impact, that may arise from our final measures;
>
> - the rationale for our final measures is sound, their scope appropriate, and their likely impact fair and proportionate, despite the large cost implications for industry;
>
> - the overall PPI strategy, of which our final measures form a key part, remains appropriate and necessary to address significant consumer detriment;
>
> - We should stand by and retain the open letter [with amendments]
>
> - Evidential Provisions (rather than Guidance) concerning the determination and, where appropriate, redress of a sales failing (as a type of rule, these are more likely to change firms' behaviour in the way we consider necessary) "

203. This, submitted, Mr Fordham, was very much the territory occupied by s404.

204. The Policy Statement contained the views of the FSA towards root cause obligations. It had expected and reminded firms, under Principle 6, to consider the position of non-complainants who might have suffered from deficiencies which a firm identified in dealing with complaints, and to take steps of its own initiative which might lead to redress. The use by firms of root cause analysis was an important part of the FSA's strategy for dealing with consumer-led complaints about mis-selling of PPI. It saw this as a proper use of Principle 6, fair treatment, adding on s404:

> "this is very different from a s404 review since a firm will only have to act towards non-complainants if it finds recurring shortcomings in its own sales in the course of its own root cause analysis (which must be diligent and robust) of such sales (and complaints about them), whereas in a s404 review it would have to act towards non-complainants because it was included in the scope of the s404 review established in response to a widespread or regular failure by firms."

205. Firms should use the DISP section of the Handbook on complaints-handling when reviewing PPI sales. The Statement also preferred the use of the complaints-led

package of measures over a s404 scheme, the use of which it had considered, because it regarded the complaints-led approach as *"an effective and appropriate approach that is swifter and more proportionate than a s404 review of sales.*" The scale and extent of detriment was not such as now to make a s404 scheme more proportionate. Mr Fordham submitted that, to the FSA, it was only swifter because the safeguards were omitted, and only more proportionate because redress extended beyond redress for breaches which were actionable, but to which a s404 scheme would be limited.

206. The FSA emphasised the importance of firms being individually responsible for delivering *"fair outcomes"* and treating customers fairly. The primary responsibility for undertaking root cause analysis lay with each firm. They should be under no illusion about the importance placed by the FSA on their obligations in that respect. Firms would be monitored, inadequate measures should be changed, particular attention would be paid to complaints about single premium policies on unsecured loans because of their volume, and if any firm could not demonstrate that it was "*delivering fair outcomes, it can expect tough action from us*", including referral for investigation and enforcement, and a requirement to revisit what it had failed to do adequately. The Policy Statement recognised that what might be proportionate for one firm to do would not necessarily be the same for all; each had to take fair and reasonable decisions about that. It was likely to be fair and proportionate for firms to contact the generality of relevant customers.

207. The rationale for the new measures was that the FSA had gathered since 2005 *"wide and deep evidence of weaknesses in PPI sales practices across the market.*" This had led to the growing number of complaints about PPI sales, which supported its view about these weaknesses, as had concerns voiced by other bodies. The FOS decisions on complaints were *"generally compatible with the approach we have consulted on and finalised here*".

> "We have not seen any convincing evidence to support the industry claim that the FOS significantly changed its approach after that published policy of November 2008. And in any case, we had evidence of, and were concerned about, the high rate of overturns firms were already experiencing at the FOS at end 2007 and through 2008, so it is clear the FOS's approach at that time was already identifying a high incidence of poor complaint handling and of consumer detriment from PPI sales."

208. The new Guidance in the DISP amendments to the Handbook, which the Policy Statement introduced, repeated in 3.4.1G the outline of DISP1.3.3R but set out more elaborate requirements for the firm to consider. These included the concerns raised by complainants at the time of sale and subsequently, the reasons for rejected claims and complaints, the stated sales practice at the time, evidence about those practices, regulatory findings, and relevant decisions by the FOS. If systemic problems were thought to exist, they should be taken into account as possible causes of failings when dealing with complaints even if the complainants had not raised the issue themselves. So, submitted Mr Fordham, the individual firms were required to examine past sales to see if there was a recurring or systemic problem, and if so, they then had to put in

place various measures to ensure what the FSA thought was appropriate redress, and failing which they would expect to face "tough" investigatory or enforcement action. This was a structure not unlike that of the informal pre-2000 Act reviews, now deemed to be s404 reviews.

209. The new DISP Appendix 3.4.3G continued:

> "Where a *firm* identifies (from its *complaints* or otherwise) recurring or systemic problems in its sales practices for a particular type of *payment protection contract*, either for its sales in general or for those from a particular location or sales channel, it should (in accordance with *Principle 6* (Customers' interest) and to the extent that it applies), consider whether it ought to act with regard to the position of *customers* who may have suffered detriment from, or been potentially disadvantaged by such problems but who have not complained and, if so, take appropriate and proportionate measures to ensure that those *customers* are given appropriate redress or a proper opportunity to obtain it. In particular, the *firm* should:
>
> (1) ascertain the scope and severity of the consumer detriment that might have arisen; and
>
> (2) consider whether it is fair and reasonable for the *firm* to undertake proactively a redress or remediation exercise, which may include contacting *customers* who have not complained. "

The submissions

210. Mr Fordham submitted that the problems to which the new DISP provisions were addressed were the problems which the Policy Statement and the Open Letter Standards were addressing, with the Principles given the role in them of which complaint was made. All of this new guidance was intended to apply to firms across the board a uniform approach to achieve what the FSA thought would be appropriate redress, for widespread misselling of PPI. Thus it all fell within the field occupied exclusively by s404.

211. Mr Fordham accepted that, in principle, it would be lawful for the FSA to tell an individual firm that it had to conduct a root cause analysis. But there came a point, on his case, that it could not tell a large number of firms to carry out root cause analysis where there was widespread misselling in the eyes of the FSA. Once the problem

reached the scale which fell within s404, the FSA could only proceed by s404 and not by telling firms to carry out root cause analysis. He supported that by pointing out that the FSA had considered and decided against a rule requiring a review of rejected complaints; it had done so because of the then expected changes to s404. The implication was that s404 in its new form could usefully be invoked to deal with that problem and, if so, s404 in its old form was also available to deal with the problem here, and is the power which the FSA knew it should be using.

212. Mr Fordham cited *R v Liverpool City Council ex parte Baby Products Association* 2000 LGR 171, Lord Bingham of Cornhill CJ sitting as a single judge in the Queen's Bench Division, in support of his submissions as to the way in which a specific power to deal with a particular problem would supplant the general powers which a public body might otherwise rely on. The Consumer Protection Act 1987, with Regulations, enabled a local authority, which had reasonable grounds for suspecting that any safety provision had been contravened in relation to goods, to issue a "suspension notice" prohibiting a person on whom it was served from supplying those goods. It would be a criminal offence to breach that prohibition. The City Council became concerned about the safety of certain models of baby walker. These concerns were strongly opposed by the suppliers. The Council decided to issue a press release to warn the public and to cause the recall of the product. The Council relied upon the general ancillary power in s111 and the general power to publish information relating to its functions in s142 of the Local Government Act 1972. That decision was quashed.

213. Lord Bingham accepted the thrust of Mr Fordham's submission that:

> "What, however, was impermissible was to make a public announcement having an intention and effect which could only be achieved by implementation of clear and particular procedures prescribed in an Act of Parliament when the effect of the announcement was to deny the companies the rights and protections which Parliament had enacted they should enjoy. So to act was to circumvent the provisions of the legislation and to act unlawfully."

214. It did not matter that the procedures under the 1987 Act were cumbersome and not useful for an emergency; the solution to that was amendment not circumvention.

215. That principle was not at issue. Mr Brindle submitted that it was a clear and obvious case, but wholly distinguishable on its facts from the present: the local authority had sought to achieve the same end result as that which the statue provided for, but by an informal route. But that is simply wrong; the actions of the authority did not include making supply a criminal offence, which is what the statutory scheme would have achieved. I confess to finding the application of the principle surprising, at least without very specific discussion of the differences between the effect of the scheme and the effect of the informal approach in that respect, and the reason for the procedural safeguards. A public announcement of a request that supplies of the products be suspended which had no enforceable legal consequences was held to be

beyond the power of a public body because of the existence of a procedure whereby a suspension notice could be issued breach of which had criminal consequences. The procedure actually adopted afforded no specific procedural protection to the suppliers, but breach of it also had no criminal consequences for them.

216. Mr Fordham referred me to two other authorities to illustrate the principle he relied on. *Credit Suisse v Waltham Forest London Borough Council* [1997] QB 362 also concerned the scope of s111 of the Local Government Act 1972. Parliament had made detailed provision in a number of Acts for the discharge of the housing duties on local authorities. These detailed provisions did not contain a power to give a guarantee in connection with a bank loan to a company which the local authority had formed to assist in the acquisition and development of housing for its statutory housing functions. Neill LJ said at p374C that, although the purpose behind what the Council did was laudable:

> "where Parliament has made detailed provisions as to how certain statutory functions are to be carried out there is no scope for implying the existence of additional powers which lie wholly outside the statutory code. Section 111(3) makes it clear that the power to enter into financial obligations is subject to any statutory controls which may be imposed"

Peter Gibson LJ added:

> "I agree with Neill L.J. that, having regard to the detailed statutory scheme governing the housing functions of a local authority and in particular the express provisions relating to raising money to provide housing and to giving financial assistance to others to acquire housing, there is no scope for treating section 111 as authorising a local authority to give a guarantee and indemnity such as were given in the present case. It is simply inconsistent with the statutory scheme that a local authority should have the power to set up a company and give a guarantee of the company's liabilities and an indemnity."

217. *R v J* [2004] UKHL 42 [2005] 1 AC 562 held that it was an abuse of process to prosecute unlawful sexual intercourse with a girl aged between 13 and 15 as a charge of indecent assault so as to circumvent the 1 year time limit which by statute applied to the former but not to the latter offence. The Act might be anachronistic but to allow the conduct said to constitute the offence to be charged in that way would be to deprive the statutory limit of any meaningful effect. Lord Clyde and Lord Roger also dealt with the issue as one of statutory construction or application. The intention of Parliament was that prosecution for unlawful sexual intercourse with a girl aged between 13 and 15 should be begun within one year of the intercourse. Lord Clyde said that "at the heart of the matter is the proper understanding of the relationship between the two statutory provisions". Lord Roger regarded the issue of statutory construction as critical. "Section 14 must be construed and applied in a way that respects and does not defeat that intention. This is enjoined by more than one

principle of statutory construction." "It would be wrong to construe section 14 in such a (literal) way as to permit the prosecutor, however well-intentioned, to use it to evade the time bar applying to [such prosecutions]." The Crown had "cut across" Parliament's intention.

218. Mr Fordham contended that s404 exclusively occupied the field, in what I found an increasingly unhelpful way of describing the issue. He recognised that the next and important question, if analysing the issue in that language, was to define the field which s404 exclusively occupied. He contended that it was not simply the imposition on firms of a compulsory pro-active review of past business. The field could not be defined simply by the statutory pre-conditions and limits to its operation; otherwise, the intended operation of the section could be evaded by the device of avoiding the safeguards. He meant by the field, steps intended to achieve a review of past business with a view to customer redress in the light of perceived widespread defaults by firms.

219. The old s404 provision was rather less flexible than the new. But as Mr Fordham suggested, that could mean that the field occupied by the new s404 was broader than that occupied by the former one with which I am primarily concerned. In any event, Mr Fordham suggested that the scope of the Treasury's powers in s404(2) and (4) were such that it could design schemes which were as flexible as the former pensions reviews had been, and could provide for coverage for all but with those required to take particular measures being targeted based on thresholds for complaints upheld, publicity and opt-ins, or by mode of sale or type of customer. So the field was a large one.

220. If the intended purpose and consequence of the steps taken by the FSA "cut across" the field occupied by s404, they would be unlawful. The Act, on its true construction did not permit an alternative formal set of rules to be used nor did it permit a less formal procedure by way of guidance. The principle for which he contended applied, as the *Liverpool* case illustrated, to formal and informal alternative methods of achieving the aim provided for specifically by statute.

221. It would be unlawful to use the provisions addressing "root cause analysis" to avoid the obligations in a s404 scheme, nor could the FSA lawfully encourage the widespread use of "root cause analysis" obligations to deal with what s404 dealt with. The FSA could not lawfully avoid the safeguards by saying that it was not making universal provision for a particular kind of activity, as envisaged by s404, but was targeting only the majority of firms affected. It could not be thought that the new arrangements which the FSA was introducing and which were challenged in this case added nothing, in view of the cost benefit analysis it undertook, and the huge costs which they would impose on the industry. These were assessed by the FSA at between £0.8bn and £1.3bn over five years in relation to complaints handling, with the wider costs of the package ranging between £1.1bn and £3.2bn. There were between 3.8m and 11.3m non-complainant customers who might be contacted, and 15m who might be assessed for initial mailing by the firms. 35 intermediaries might fail at a cost to the compensation scheme of about £35m.

222. Mr Brindle forcefully submitted that it was improbable that Parliament had intended that the only regulatory response which the FSA could adopt to deal with widespread concerns, which it thought would satisfy the Treasury that the conditions in s404(1) were met, was to provide a report to the Treasury under s404 (4)(a). The contentions of the NEMO left unclear what powers the FSA would have if the Treasury were not satisfied of the conditions, or refused to make a scheme order or if Parliament did not approve it: did all its other powers revive or had it lost them for good in relation to that widespread misselling? It would be odd indeed if Parliament reduced the FSA's regulatory options, the deeper and wider its concerns about misselling. It would be quite wrong, and had not really been the basis of NEMO's argument, to treat the mere existence of the circumstances which triggered the availability of the powers in s404 as sufficient to bring into play the principle for which NEMO contended in reliance on the *Liverpool City Council* case. It was necessary also to examine the purpose and effect of the powers deployed to see if they fell foul of the principle. S415A, a replacement for an earlier provision, gave further support to his contentions about the role of s404.

223. There had been no challenge to the root cause provisions which preceded the amendments. Root cause analysis required firms to consider whether they ought to act on their own initiative with regard to customers who had not complained. Mr Brindle submitted that all that the new guidance in the DISP amendments provided was a logical extension of the root cause provision, and was still a complaints driven process. The changes to root cause analysis in the DISP section of the Handbook added no new obligations. DISP Appendix 3.4.2G was tied into the existing root cause obligation. This existing obligation required firms, as part of their complaints handling, to consider whether there were recurring or systemic problems. This required them to consider whether there were other products which might also be affected which had not been complained about and which required redress. This was no more than a useful extension of existing provisions on root cause analysis.

224. He next submitted that what the FSA had sought to and had achieved by the Handbook amendments on root cause analysis was very different from the outcome of a s404 scheme. The relevant field which was the exclusive preserve of s404 was compulsory, pro-active, industry or sector wide past business review and redress, based on widespread concerns about misselling. That was not what the package of measures or this component was dealing with. S404 depended on there being a failure to comply with rules relating to what he said would be an activity described at a general level, s404(1). It had to be necessary to establish the nature and extent of that failure, to establish liability to make compensation payments and to determine the amounts payable as compensation, limited to what was actionable.

225. By contrast, the FSA said it had used guidance and not compulsion. There was no punishment for not complying with guidance, whatever the FSA might then seek to do about non-compliance. The FSA Enforcement guide explained how guidance was enforced. Guidance would help firms decide what action they should take, illustrate what would be compliance with the rules, did not set a minimum standard of conduct nor would a departure necessarily indicate a breach of a rule. But guidance might be relevant to an enforcement decision, for example, in helping to assess whether it could

reasonably have been understood that the conduct in question fell below the standards required by the Principles, and what the gravity of the conduct was.

226. The package of measures as a whole went beyond a pro-active review. It did not apply across a whole or significant sector of the industry, but was dependent on the position of particular firms. And it was all complaint led, although it involved the use of root cause analysis. Part of the reason for the package of measures, and the main reason for this component of it, was that the industry had neglected its obligations in relation to root cause analysis, and had failed to deliver fair outcomes to those to whom these policies had been missold, including non-complainants.

227. The fact that a s404 scheme could not deal with breaches of the non-actionable Principles was a factor in the decision not to report to the Treasury with a view to a s404 scheme, but not the main one, according to the evidence of Ms Sinclair. In reality, on Mr Brindle's submissions and the evidence, the failure of the industry to apply the Principles as the overarching framework within which the more specific rules operated was important to the thinking behind the measures in the Policy Statement.

Conclusions on the s404 ground

228. The issue to be resolved is one of statutory construction: to what extent or in what circumstances does the existence of the powers in s404 constrain the use of other powers?

229. I accept, and it was not really disputed by Mr Brindle, that factual circumstances had arisen in 2010 in which the FSA could have reported to the Treasury about the widespread misselling of PPI and asked for a scheme order, with reasonable prospects of it proceeding successfully through the whole statutory process. There was evidence of widespread misselling and that private persons had suffered and would suffer loss in respect of which firms were liable to make compensation payments, for breaches of actionable rules. This evidence was the basis for the FOS letter of 1 July 2008 and FSA's actions. He did not dispute that the aim of the FSA's DISP amendments was to bring about appropriate redress for those who were non-complainants suffering from systemic failings, by applying the same standards as were laid down for complainants.

230. Although it is a necessary condition for the making of a scheme that the Treasury be satisfied of widespread misselling and loss by private persons upon a report to it by the FSA, the existence of circumstances which would warrant a report by the FSA and the Treasury being satisfied of those two requirements, is not by itself sufficient to deprive the FSA of all power to act in any other way to deal with misselling of PPI. It would be absurd if the regulatory powers diminished in range and scope the more serious the circumstances in which they were needed. Neither the language of s404 itself nor its role as part of the overall regulatory framework could warrant the implication in it of a restriction on all other powers merely because those

circumstances were satisfied. I agree with Mr Brindle on that point; it was not really an issue either in the way Mr Fordham developed his submissions.

231. Mr Brindle is right, and again it was not at issue, that it was necessary to go further and examine the purpose, nature and effect of a scheme in order to see whether the FSA is seeking by other methods to achieve that for which s404, on its proper construction, was intended to be the exclusive remedial vehicle.

232. The purpose of the statutory scheme is to provide a remedy for widespread misselling which has caused loss, that is in the circumstances required by s404(1). That remedy is provided by the combination of a review of past business and the payment of compensation. The statutory nature of a scheme is contained in s404(2). It has to determine the nature and extent of the widespread failure to comply with rules; then it establishes the liability of individual firms and finally it determines how much the individual firms must pay to each of its affected customers. As Mr Fordham put it: failure, liability and compensation. The statutory effect, by s404(5), is achieved by enabling breaches of scheme provisions to be treated as breaches of rules, leading to enforcement and compensatory measures.

233. I accept Mr Brindle's description of it as a compulsory, pro-active industry or sector wide vehicle for a review of past breaches of rules and the provision of redress for actionable complaints, in circumstances where there was widespread concern about misselling and where private persons had suffered or would suffer loss. I would only qualify "pro-active" by adding that this activity is regulator driven and controlled. The flexibility asserted by Mr Fordham, if correct, does not alter the accuracy of that description.

234. The purpose and effect of a s404 scheme can usefully be contrasted first with the provisions in the DISP section of the Handbook, before amendment, to which no legal challenge has been raised. The rule, DISP 1.3.3.R, required a firm to react to what it learned through its handling of complaints about recurring or systemic problems whether in that area of its activities or in other areas as well. To do this, it had to analyse complaints and see if they had a root cause. Complaints were therefore not to be treated as discrete individual events. It was only the guidance in 1.3.5G, which said that under Principle 6 a firm should consider of its own initiative providing redress to those who had not complained. Guidance could be relevant to enforcement decisions but could not directly lead to a remedy.

235. So those provisions applied at all times to all firms; DISP 1.3.3.R was compulsory. It required firms to be pro-active in putting in place procedures enabling the root causes of complaints to be analysed for what they might tell of recurring or systemic problems. This could and often would entail a review of past business. Those problems were then to be remedied by changes to the way the firm conducted its business. The focus of 1.3.3.R is remedying a firm's deficiencies, not redress for customers. Compensation for non-complainants was not compulsory, nor enforceable.

236. This all differed from a s404 scheme in a number of respects. DISP 1.3.3.R does not require widespread concerns across a sector of business; rather it looks to the depth and then range of the problems within a particular firm. The obligation is to put in place management controls and to take reasonable steps to ensure that handling complaints on an individual basis also enables wider problems to be discerned.

237. It is not explicit that a review of all past business is required, although that is one obvious way in which the root cause of systemic problems will be investigated and put right. But its purpose was not the provision of redress. The payment of compensation to non-complainants is not compulsory, but merely guidance, which can only be enforced indirectly.

238. The degree of regulatory oversight is considerably less, since the particular management controls and reasonable steps required to ensure that systemic problems are identified are for the firm to judge, although the underlying obligation is an enforceable rule. Nor was the process of review, analysis and remedy subject to the degree of regulatory control which a scheme could entail.

239. None of this was said to involve any conflict with s404 powers. The effect of the changes made in 2010 is therefore crucial to the arguments. Mr Brindle contends that they are a logical extension of the existing provisions, albeit expected to be very widespread in effect and acknowledged to be expensive for firms. Mr Fordham says that, if not a s404 scheme in all but name and shorn of statutory safeguards, nonetheless it does all of significance that such a scheme would do.

240. The changes proceed in two stages. First, there are the changes to complaints handling, which are in substance changes to the basis upon which decisions on complaints should be made, by reference to the new evidential rules in DISP and the common failings. These draw upon the overarching effect of all the Principles, in relation to which I have rejected the challenges in grounds 1 and 2. There is no doubt however that those changes are intended to achieve a significant alteration in the way firms deal with complaints. It would not achieve a significant alteration in the way the FSA and FOS dealt with complaints, at least as the FSA and FOS had perceived their position. Nor is it intended to be a significant alteration in the way the FSA thinks firms ought to be handling complaints. It is to achieve what the FSA considers firms should have been doing all along if they had properly applied the rules including the Principles.

241. The second part of the changes is where the relationship to s404 comes in, in the relationship between review of past business and compensation. The Policy Statement reminded all firms of the obligations which they were already under in DISP 1.3.3.R to undertake root cause analysis. It then emphasised the role of Principle 6 as the source of the obligation to pay compensation to non-complainants, if root cause analysis brought non-complainants to light fair treatment of whom required redress. Principle 6 was already identified as the source of that obligation in the 1.3.3.G in the unamended DISP.

242. However the new guidance is distinctly more elaborate in detailing what steps a firm is to take in root cause analysis; the basis upon which it assesses its failings is related to the way the FSA said the Principles and common failings should be used, and the basis upon which redress is required is similarly altered. The tone of the guidance, and the tone of the Policy Statement is distinctly harsher and more threatening if firms do not follow the guidance. But it remains guidance.

243. I accept largely Mr Brindle's submission about the nature and legal effect of these changes. Although I would not accept that they are of no great significance, in view of the aim of the FSA and the undeniably high costs, they are a logical extension to the existing DISP provisions, or a more emphatic, impatient, and specific use of them. They are not in law significantly different from the existing unchallenged provisions in DISP. First, I have accepted the lawfulness of the way in which the FSA seeks to use the Principles both as a source of compensation and as a source of obligation not so much augmenting specific rules, as the ever-present substrate to the overlay of specific rules. Whether or not that is a change in emphasis or approach by the FSA towards firms' obligations, firms carrying out root cause analysis under DISP 1.3.3.R would now be required to apply that approach, and under 1.3.5.G would have to consider compensation to non-complainants in respect of those failings.

244. Second, the change, by way of guidance, to the specificity with which root cause analysis is carried out may more resemble what may be found in a s404 scheme and what might have been found in pre 2000 Act reviews, but I cannot see that as a change of such legal significance that it shifts the new measures into a field in which the proper construction of s404 gives it exclusive operation.

245. The third area of change concerns not the basis upon which compensation is addressed but the language of the new guidance. It still follows however the conceptual framework of DISP 1.3.3.R and 1.3.5G. A systemic or recurrent fault has to be identified by the individual firm, albeit upon the supposedly new basis. It has to consider whether Principle 6 requires redress for non-complainants. If so, it has to consider what are appropriate measures, which means that depending on the scope and severity of consumer detriment it has to consider a pro-active exercise, including notification of non-complainants. All of that could be comprehended within the operation of the earlier guidance.

246. Finally, the tone of the guidance and Policy Statement is more emphatic and is intended to produce results that the present guidance has not produced. But it remains guidance.

247. I do not see those changes, separately or in combination, as going far beyond that which NEMO has accepted as undeniably lawful. The supposed change in the basis upon which failures are assessed and the actual change to the behaviour of firms which it is intended to effect, is no doubt a component of the additional costs. But that has nothing to do with whether this is a s404 scheme in disguise or function. The obligation to undertake root cause analysis is already embodied in an actionable rule

of universal application. But it is only those firms which themselves identify systemic or recurrent problems which are advised to take further steps. Guidance as to how to undertake such an analysis is not a compulsory scheme. The compensation provision is essentially an elaboration of what could have been spelled out from DISP 1.3.5.G.

248. I do not think that it is useful to ask and answer the question of what field is occupied by s404, and then ask whether the changes in the Policy Statement occupy it. That rather distracts from and misstates the issue of statutory construction. The question is whether or not the provision for a scheme in s404 carries with it the necessary implication that what the FSA has set out in the Policy Statement is excluded from the FSA's powers as regulator.

249. It is certainly not excluded by any express words. A specific provision is capable of carrying an implied exclusion of other general or other specific powers, but I do not consider that s404 implicitly excludes what the FSA has done, even though it would have been possible for a scheme to have been set up to achieve much or rather more of the same end, and part of the reason why it was not was the cumbersome nature of the remedy, and the fact that it would not apply to breaches of the Principles.

250. First, in construing a regulatory provision in an Act, it would require clear indications in the language that the greater the problem, the more Parliament intended to restrict the flexibility of the way in which the regulator deal with it. Far more likely is that Parliament would have added to the regulator's armoury. There is no such indication here at all. S415A is a modest indication to the contrary.

251. Second, there is no doubt that the DISP rule on root cause analysis is a lawful rule of universal application, enforceable and actionable. And that guidance that the discovery of systemic problems should lead to compensation for non-complainants is likewise lawful. So there is already in existence a lawful mechanism which can achieve firm by firm all or much of what a scheme would achieve in relation to that firm. The structure of the Act does not suggest exclusivity for s404 in relation to review of past business and redress for non-complainants. That was not suggested, since it was not suggested that the use of root cause analysis to proved redress for non-complainants through guidance was unlawful.

252. Third, if it is lawful for the FSA to point out to an individual firm that it should be looking to a root cause analysis, I find it absurd that the FSA should be disabled from that when it wishes to point out to a large number of firms in a sector that that is exactly what they ought to be doing. If a statute is to have the effect, on its true construction, of making a single lawful act unlawful if done one hundred times, I would expect that to be very clear. This is not a situation in which the number of acts changes their nature. But it differs markedly from a scheme which would oblige all firms in the sector actually to undertake a review as opposed to considering whether they should.

253. Fourth, since root cause analysis and a scheme have much in common in terms of review and redress, one would not expect to see a very large distinction in nature, purpose or outcome for individual firms; if s404 excludes other remedies, one would expect the exclusion to be narrow rather than broad. I have already said that the existence of circumstances in which a scheme could successfully be promoted is not of itself a basis for the exclusion of other remedies.

254. Fifth, I see differences in the compulsion applied to every firm in the sector of the scheme to undertake the analysis. The s404 scheme would apply to them all, making them all carry out some form of analysis, and it might or might not have a size or value of business threshold below which the scheme did not apply to certain firms. There might or might not be a filtering out at a second stage. The regulatory oversight would be significant. Failure would lead to enforcement measures directly for failure to comply with the scheme provisions, compensation and actionable redress for breaches of the scheme rules as well as for the failure to comply with the underlying rules. Root cause analysis however already applies where there is already evidence of systemic failure. The techniques of review of past business are still guidance, as is the provision of compensation. Whatever s404 excludes, it is not that remedy in my view.

255. Sixth, Mr Fordham made a number of points which suggest that the measures in the Policy Statement on root cause analysis were in reality an evasion of s404. S404 is to be construed so as not to permit the evasions of its ambit by the simple adoption of features to which s404 does not apply. As a statement of principle, I accept it.

256. Mr Fordham put considerable weight on what he described as the protections for the industry in the need for the Treasury to make the scheme on certain bases, and for Parliament to approve it. I am not sure that those procedures are only protections for firms as opposed to means of oversight of the FSA. Be that as it may, there were different protections in the new section but the important point was that there were protections which showed that measures should not be devised to achieve the same result as a scheme would achieve, unless formulated and processed as a statutory scheme. The FSA did not want to follow the scheme route in part because of what it saw as the cumbersome procedures. Those cumbersome procedures were what Mr Fordham regarded as procedural protections.

257. The cumbersome nature of a s404 scheme under the former provisions is not a reason, in my view, why the FSA could ignore it and choose a route which was excluded on the true construction of s404. But that does not make it any the less a proper reason for choosing an alternative remedy if it is lawfully available. Its cumbersome nature does not help ascertain its exclusive effect; it is no more than an invalid reason for evading its exclusive effect, whatever that is. The further the FSA is from a s404 scheme, bearing in mind that the lawful use of root cause analysis is bound to bear some similarities in nature, purpose and effect, the more difficult it is to say that the measures are excluded on that basis by the provisions of s404. I do not see that the nature of the measures in the Policy Statement, costly though they will be, and destructive of a number of businesses, can be seen as evading procedural protections which firms were intended by Parliament to enjoy.

258. Looking at them overall, the new Handbook provisions do not have the universal compulsion, regardless of the degree of individual failure by the firm, nor the regulatory oversight and effect by enforceable rules which a s404 scheme would have. So although there are similarities in scope, and aim, I do not regard these measures taken as a whole as a device or evasion of the protective requirements of s404, and thus forbidden by it. The protective measures are related to the widespread compulsion which firms face at least in the first place, regardless of their own contribution to the concerns and measures which they may have taken. The measures are also related to the enforcement of scheme provisions as rules with all which that may entail in terms of disciplinary and other risks. Where, as with the measures in the Policy Statement, that is not the position, the argument that the safeguards have been evaded is readily answered by the fact that the consequences to which they apply do not arise either.

259. There are undoubtedly parallels with the facts of the Liverpool *City Council* case, fewer with *Credit Suisse*, and fewer still with *R v J.* Each of those cases, reflects common principles but their application is dependant on the facts of each case. While I admit that I find the application of the principle in *Liverpool City Council* surprising given that the protections are clearly related to the consequences of a scheme, I have to decide this case on the facts of it and not by reference to the degree of parallel with that case. There are also three important differences. The regulatory framework permits rules to provide for root cause analysis, in addition to s404. This of itself brings in similarities with s404 quite lawfully; and that rule with guidance is what is being deployed here. S404 and root cause analysis are all specific remedial parts of the same regulatory framework. Neither is a general but ancillary power akin to s111 of the Local Government Act 1972. Second, there is a real difference between the s404 and the Policy Statement measures in both enforcement and in effect on those who have not caused concern. Third, the problem in the *Liverpool City Council* case for the manufacturers was that the press notice damaged their sales and reputation, without the means to disprove the concerns, and protection against that effect. Here, there is no requirement to stop selling PPI; there is no reputational damage to all sellers; it is only those whose sales show systemic problems on their own analysis who have to take remedial steps.

260. Parliament has excluded breaches of the Principles of themselves from the scope of a scheme, and part of the FSA's reasoning in deciding not to initiate a scheme was that it would not cover such breaches, which it regarded as important to its regulatory approach to this problem. But although a set of rules which covered widespread failures to comply with Principles and created a "scheme" in all but the procedures which a true s404 scheme would have to go through, might very well be a device unlawfully to evade an implied restriction, that is not the position here.

261. The widespread failures include breaches of Principles but are not limited to the Principles. More importantly, and for the reasons which I have set out, the Policy Statement measures attacked in this ground have to be looked at as a whole and do not amount to a scheme impermissibly targeting Principles, and evading safeguards.

262. Seventh, I was not persuaded by Mr Fordham's submissions on the construction of s404 by reference to the past reviews which were deemed to be s404 schemes. There were sound reasons for providing for those past reviews to be continued within the new statutory framework without more ado. "Deeming" them to be s404 schemes enabled them to be regulated as if they were such schemes without involving a judgment that they would have been capable of being such schemes if started after the 2000 Act came into force. In the end however, although accepting Mr Brindle's submissions on this point, the argument did not advance the real issue.

263. Accordingly, I reject this third ground of challenge.

Overall conclusions

264. I grant permission to argue all three grounds, but dismiss them.