

A SUPPLEMENT TO ADAM SAMUEL'S CONSUMER FINANCIAL SERVICES COMPLAINTS AND COMPENSATION, SECOND EDITION - FOR MIFID II CASES

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1. Introduction

1.1 As the second edition of Consumer Financial Services Complaints and Compensation was being printed, the FCA produced its final rules for handling complaints relating to the Markets in Financial Instruments Directive II (MiFID II), due to enter into force on 3 January 2018. Annex L to PS 17/14 introduces a new DISP 1.1A which as DiSP 1.1.3R(2) explains, will apply to the MiFID complaints of a MiFID investment firm. The same applies to the MiFID complaints of a third country investment firm received from retail or elective professional clients.

2. MiFID II itself

2.1 The Directive says very little about complaints. Article 75 requires states to ensure the setting up of complaints and redress procedures for the out-of-court settlement of consumer disputes concerning the provision of investment and ancillary services provided by investment firms. Recital (151) requires that bodies exist to settle disputes out of court and Article 75(1) insists that states ensure that all firms adhere to one or more such bodies implementing such complaint and redress procedures. Article 75 and Recital (151) make pious comments about cross-border co-operation. Finally Article 75(3) insists that national regulators tell ESMA of the complaint and redress procedures.

3. The MiFID Org Regulation

3.1 The "Delegated Regulation supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive" is called by the FCA the "MiFID Org Regulation".

3.1 Much of the Regulation is not exactly rocket science. Recital (29) insists on investment firms having rigorous procedures for complaints handling. Recital (38) is a bit more advanced. It insists that actual or potential clients should be able to express their dissatisfaction with investment services provided by investment firms. Their complaints should be handled effectively in an independent manner by a complaints management function which could be carried out by the compliance function. Recital (41) insists that people involved in complaint-handling should be included in remuneration rules to ensure that client's interests are not "impaired".

3.2 Article 22(2) requires investment firms to establish and maintain a permanent compliance function operating independently with responsibilities to report to the management body at least annually on complaints-handling reporting and remedies undertaken to or to be provided. It must also monitor the complaints process' operations and consider complaints as a source of relevant information for its general monitoring responsibilities. Finally, under Article 26(7), the compliance function must assess and as a result create a risk-based monitoring programme taking into consideration information gathered "in relation to the monitoring of complaints handling".

¹ An earlier version of this appeared on Compliance Resource Network in July 2017.

3.3 As part of the requirement in Article 16(2) of MiFID II for investment firms to have policies and procedures sufficient to ensure compliance of the firm, Article 26 of the MiFID Org Regulation contains its own rules on complaints.

3.4 Article 26(1) insists on investment firms having, implementing and maintaining “effective and transparent complaints management policies and procedures for the prompt handling of clients’ or potential clients’ complaints.” Firms have to keep records of complaints and the measures taken to resolve them.

3.4.1 The policy has to “provide clear, accurate and up-to-date information about the complaints-handling process” and be “endorsed by the firm’s management body”.² Firms have to publish the details of the process to be followed which have to include “information about the complaints management policy and the contact details of the complaints management function”.³ As with the current DISP 1.2.1R, the information must be provided to clients or potential clients, on request, or when acknowledging a complaint.⁴ Investment firms have to enable clients and potential clients to submit complaints free of charge.⁵ This has long been a requirement in practice, currently in DISP 1.3.1AR.

3.5 Article 26(3) requires investment firm to create a “complaints management function responsible for the investigation of complaints” which can but does not have to be located in the compliance function. Article 26(4) repeats a combination of DISP 1.4.1R and Principle 7 by insisting that firms when handling complaints, communicate with complainants clearly, in plain language that is easy to understand and respond to complaints without “undue delay”.

3.6 Article 26(5) requires respondents to “communicate the firm’s position on the complaint” to complainants and tell them of their “options”. These include any alternative dispute resolution entity, in the UK, the Financial Ombudsman Service “or that the client may be able to take civil action”.

3.7 Firms have to supply information on complaints and their handling to the relevant regulators and “where applicable under national law, to an alternative dispute resolution (ADR) entity.” The meaning of this quotation is less than clear, particularly as the nature of the information is not specified.⁶

4. To what does DISP 1.1A apply? *Insert into Consumer Financial Services Complaints and Compensation after 1.3*

4.1 A MiFID complaint must be about the provision of investment services by an investment firm (including a third country one) or CRD credit institution.⁷ Complaints about ancillary services delivered by an investment firm are also included.⁸ So are cases about the sales of structured deposits to clients or advice to clients on them delivered by either investment firms or CRD credit institutions.⁹ Collective portfolio management investment firms remain subject to MiFID for activities allowed by articles 6(3) of the UCITS Directive and 6(4) of the Alternative Investment Fund

² Art. 26(1), para. 2

³ Art. 26(2)

⁴ Art. 26(2)

⁵ Art. 26(2)

⁶ Art. 26(6)

⁷ DISP 1.1A.3G(1-2)

⁸ DISP 1.1A.3G(1)

⁹ DISP 1.1A.3G(3)

Management Directive.¹⁰ MiFID complaints are also about the equivalent business of third country investment firms.¹¹

4.2 Probably unnecessarily, DISP 2.3.1AR has been added to make it clear that all these types of complaints are within the compulsory jurisdiction's subject-matter. A new DISP 2.3.1BG makes it clear that FOS can deal with a complaint about an act of a MiFID investment firm preparatory to the provision of the investment or ancillary service so long as it is an integral part of the service. This includes generic advice to a customer before or during the provision of investment advice or service or an ancillary service.¹²

4.3 Firms that do not hold client money or assets can claim exemption from MiFID under Article 3(1)(a-c) but of course cannot then use passporting rights. So, small IFAs, without clients that they advise when they are abroad, fall outside MiFID.

4.4 DISP 1.1A.5G applies DISP 1.1A to complaints made by clients to MiFID investment firms as defined in MiFID which include professional and for such business eligible counterparties. For third country investment firms, DISP 1.1A only applies to complaints from retail and elective professional clients.¹³ However, only rules marked EU and DISP 1.1A.39R apply to ineligible complainants within these categories.¹⁴ These rules only apply to complaints from ineligible MiFID complainants of third country investment firms if the complainants are retail or elective professional clients.¹⁵

4.5 The "EU" rules cover consumer awareness,¹⁶ the requirement to have an effective complaints management policies and procedures¹⁷ endorsed by the board,¹⁸ access to the complaints process free of charge,¹⁹ the creation of a complaint management function,²⁰ root cause analysis²¹ and the need to respond to complaints in plain language and without undue delay,²² keep records²³ and provide information to regulators.²⁴ DISP 1.1A.39R applies the reporting rules except that the parts of the report which firms have to provide to the FCA must include material about complaints received from all three types of complainants, rather than just eligible complainants to which the current rules limit the reports.

4.6 Different firms and different rules

4.6.1 A formidably complex table in DISP 1.1A.7R set outs which parts of the new rules will apply to complaints from eligible complainants about activities carried on from

- an establishment in the UK by
 - MiFID investment firms; or

¹⁰ DISP 1.1A.3G(4-5)

¹¹ DISP 1.1A.4G & arts 39 & 41 of MiFID 2

¹² DISP 2.3.1BG

¹³ DISP 1.1A.5G(2)

¹⁴ DISP 1.1A.6R(1)

¹⁵ DISP 1.1A.5G(2)

¹⁶ DISP 1.1A.10EU

¹⁷ DISP 1.1A.12EU

¹⁸ DISP 1.1A.13EU

¹⁹ DISP 1.1A.16EU

²⁰ DISP 1.1A.17EU

²¹ DISP 1.1A.18EU

²² DISP 1.1A.24EU & 29EU

²³ DISP 1.1A.37EU

²⁴ DISP 1.1A.38EU

- third party investment firms (retail and elective professional clients only),
- a UK firm's branch elsewhere in the EEA and
- an EEA firm's branch in the UK.

4.6.2 DISP 1.1.A.42R only applies to a UK firm's branch elsewhere in the EEA. All other types of firms are exempt from that. This is unsurprising because the rule requires a branch of a UK MiFID investment firm abroad but in the EEA to "adhere" to a "relevant" ADR entity in the relevant EEA state as regards consumer disputes about investment and ancillary services. Otherwise, all of DISP 1.1A applies to UK establishments.

4.6.3 For UK firms in other EEA states, disclosure of FOS to which it would not be subject on the website and general conditions does not apply. Nor do the rules in DISP 1.1A.20-21 about investigating and assessing complaints which are in almost identical terms to DISP 1.4. DISP 1.1A.22-23 are also excluded. They deal with the obligation to co-operate with FOS and the provisions on complaints resolved within the next three business days following receipt. DISP 1.1A.26-27 and 31-33 which lay down requirements for final response letters that look very like DISP 1.6.2R and guidance on disclosing the material about FOS also do not apply. The same concerns DISP 1.7 on complaint forwarding, the time-bar provisions in DISP 2.8.1R, the reporting rules and data publication requirements.

4.6.4 EEA firm branches in the UK do not need to have a complaints management policy, handle complaints effectively in an independent way and publish complaints data.

5. Initial disclosure – DISP 1.1A.10-11 – replicating DISP 1.2.1R – and applying Article 26(2) of the MiFID Org Regulation - Consumer Financial Services Complaints and Compensation at 2.4

5.1 DISP 1.1A.10EU and 11R repeat DISP 1.2 by requiring firms to publish details of their complaint handling processes.²⁵ This material has to provide information on the complaints management policy and contact details of the complaint management function.²⁶ Information must be supplied about the FOS including its website address have to be supplied on the firm's website and general conditions of contracts entered into with eligible complaints.²⁷ This may require slightly more detail than the current rules, notably about the policy, but not much. In practice, the complaints management policy will be that the firm gratefully accepts complaints as an opportunity to review and correct problems that have arisen and seeks to reach fair and reasonable results on them in a prompt efficient manner. Beyond that, there is nothing meaningful that one can say.

6. Complaints management policy and procedures – different from procedures required by DISP 1.3.1R? – DISP 1.1A.12-16 - Consumer Financial Services Complaints and Compensation at 2.2

6.1 The complaints management policy and procedures is required by DISP 1.1A.12EU and 13EU in the same way that firms have to have and implement procedures under the current 1.3.1R. The marginal difference is that the Board has to endorse the policy and that document has to be set out separately. As with the current procedures, the policy has to be in writing and made available to all relevant staff through "appropriate internal channels".²⁸ Senior management is responsible for implementing and monitoring compliance with the policy under 1.1.15G. In practice, the same people cannot monitor compliance with something for which they are responsible. The right to make

²⁵ DISP 1.2.1R(1)

²⁶ DISP 1.1A.10EU which goes further here than DISP 1.2.1R(1) and 1.2.3G(1) although it reflects best practice already.

²⁷ DISP 1.1A.11R & 1.2.1R(4)

²⁸ DISP 1.1A.14G (this is current best practice) although it is not in the rulebook.

complaints free of charge, currently in DISP 1.3.1A is reproduced in 1.1A.16EU. The effect of the rules on super-equivalence, is to disapply the provisions in DISP 1.3.1AA-AD on various charging telephone lines. However, the FCA is likely to interpret 1.1A.16 as requiring compliance with those provisions.

7. The complaint management function - *Consumer Financial Services Complaints and Compensation at 4.2*

7.1 DISP 1.1A.17EU insists on the formal creation of a complaints management function to investigate cases. This can be the compliance department although it does not have to be. How that team can exercise its second line supervision functions in relation to complaint handling while handling the cases themselves has not been revealed.

8. The investigation - *Consumer Financial Services Complaints and Compensation at 4.2*

8.1 For ordinary cases (those not resolved within the next three business days), 1.1A.28R covers acknowledgement and keeping the complainant informed in the same way as DISP 1.6.1R. See *Consumer Financial Services Complaints and Compensation at 3.3 & 4.5.1*.

8.2 DISP 1.1A.19G insists on effective complaint handling “in an independent manner”. This is the same as “competently, diligently and impartially” in DISP 1.5. R(1). Behaving in an “Independent manner” is a better description of what is required since anyone investigating a complaint against their employer is not impartial. Unfortunately, the FCA has then reproduced DISP 1.4.1R in 1.1A.20R for no reason. See *Consumer Financial Services Complaints and Compensation at 4.2*.

9. Assessment - *Consumer Financial Services Complaints and Compensation at cap. 5*

9.1 Equally, to no obvious advantage, the FCA has tacked on the current DISP 1.4.1R(2) and (5) on the assessment of complaints in DISP 1.1.A.20R-21G and the obvious requirements to cooperate with FOS and comply with any FOS award or settlement made by it rather than the firm (DISP 1.4.4R).

10. Complaints resolved by the end of the next three business days - *Consumer Financial Services Complaints and Compensation at 3.2.8*

10.1 In a conscious echo of DISP 1.5, firms are invited to apply 1.1A.24-27 instead of 28-34 to cases resolved by close of business on the third business day following the day on which it is received. 1.1A.24EU requires communication in plain language and prompt replies. 1.1A.25 requires firms to tell complainants about the firms’ position on the complaint including any dispute resolution options, in practice FOS. 1.1A.26R and 27G echoes the summary resolution communication requirement of 1.5.4R.

11. Drafting final responses - *Consumer Financial Services Complaints and Compensation at cap. 6 & 8.5.3*

11.1 After that, DISP 1.1A.29-33 just reproduces DISP 1.4 and 1.6.2R on the requirements for final responses. One possible difference is that, under DISP, 1.1A.30EU respondents only “have to communicate the firm’s position on the complaint” which is much more sensible than the requirement in 1.6.2R(1) that one has to state whether the complaint is upheld or rejected. By contrast, there is an obscure indication in DISP 1.1A.30EU that the final response must inform the complainant about their options including the fact that the client may be able to take civil action. It is unclear whether the firm has to refer to this option which should be pretty obvious. In any event,

nothing here prevents a firm from pointing out that since FOS is free, a refusal to use it may be mentioned to the judge in support of an application for costs.

DISP 1.1A.36R basically repeats DISP 1.8's offer to firms to reject time-barred complaints without handling the merits while explaining why the case is time-barred. This should not be used unless the case on the merits is weak or difficult to investigate.

12. Rag-bag information - *Consumer Financial Services Complaints and Compensation at 3.2.3 & 8.1*

The increasingly discredited and unused 1.7 on forwarding is applied to MiFID cases by 1.1.35R. DISP 1.1A.34G then unnecessarily refers readers to the requirements of DISP 2.8 about going to FOS, namely that eight weeks must have passed before a reference will be accepted by the Ombudsman if no final response or summary resolution communication has been issued.

13. Root cause analysis (DISP 1.1A.18EU)- *Consumer Financial Services Complaints and Compensation at 7.5*

The compliance function has to analyse complaints and data to identify and address risks or issues under DISP 1.1A.18EU. This is currently picked up in rather more detail for non-MiFID cases by DISP 1.3.3R. The current and annoying DISP 1.3.4G on root cause analysis in MiFID cases unsurprisingly disappears as a result. Firms are, nevertheless, recommended to continue applying DISP 1.3.3R in its entirety to root cause analysis regardless of whether a case is governed by MiFID, since the processes laid down will represent compliance with 1.1A.18. Experience suggests that compliance may not be the right department to do root cause analysis since it may be tempted to ignore any procedural failures for which it is responsible unless a different team was in place at the time.

Recording (DISP 1.1A.37EU), reporting (1.1A.38EU-39R) and data publication (1.1A.40R-41G) - *Consumer Financial Services Complaints and Compensation at 3.2.9, 7.3& 7.4*

Recording and reporting requirements remain as for non-MiFID cases except that, for MiFID complaints, under 1.1A.39R reports must cover whether complainants were retail or professional clients or eligible counterparties. The complaints data summary must include relevant material about any MiFID complaints.

Final thoughts

As one can see, nothing much will be changing in the complaint handling world in January. The Board will have to approve the complaints policy and someone will have to work out the difference between complaints procedures and policies. Final responses will not have to state that a complaint has been upheld which is a relief for investment firms when dealing with complainants who never wanted to complain in the first place. On the surface, MiFID firms will be saved from having to read some of the more long-winded parts of DISP but will be most unwise to do so. The FCA will always regard the rules that it devised as evidence of best practice. There will be a marginal tweak to the reports required. Above all else, though, the dreadful layout of DISP has just been made worse. None of this helps compliance with the rulebook, let alone good customer relations.