Arguing until Blue(fin) in the face

23 October 2014

Court tells FOS that insureds under a D&O policy are not consumers

The Financial Ombudsman Service has suffered a major defeat in the Administrative Court which will come as a relief to D&O insurers and brokers.

D&O insurance is regarded in the market as a commercial and not a retail line of business. However, a decision by FOS that a director claiming in a personal capacity as an insured under a D&O policy was a consumer and therefore was an "eligible complainant" threatened to open the entire market to FOS jurisdiction.

Those new to the issues raised by *R (on the application of Bluefin Insurance Services Ltd) v Financial Ombudsman Service Limited*[1] should read my colleague Robbie Constance's blog[2]. In brief, the former director of a company faced claims by an investor for allegedly dishonest misrepresentations and for breaches of personal covenants at the time of the company's fund-raising. The former director, Mr Lochner, claimed that he notified his brokers of the claim and that they had failed to notify the company's D&O insurers who thereafter rejected the claim. Mr Lochner subsequently complained to FOS about the alleged failure to pass on his notification.

In his keenly anticipated judgment, published on Monday, Wilkie J held that (i) whether or not FOS has jurisdiction to consider a complaint is a matter of "precedent fact", an objective issue that can be considered by the courts and (ii) a director claiming under a D&O policy for indemnity for personal liabilities arising out of his/her activities as a director is not a consumer for the purposes of the DISP rules.

Preliminary issue: can the courts determine whether or not a complainant is a consumer as a matter of "precedent fact"?

The key preliminary issue was whether a complainant's eligibility under the DISP rules was a matter for the Court or for FOS to determine. The Claimants argued that the court should determine the jurisdictional issue as a "precedent fact" to FOS using its discretion on the merits. FOS contended that eligibility was a question for it, alone, to determine and that the Court could

Any comments or queries

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1. [2014] EWHC 3413 (Admin).
2. "FOS in the D&Ock", Robbie Constance, 2 July 2014, accessible on RPC's Financial Services Blog: www.rpc.co.uk/financial-services-blog.

intervene only if FOS's determination was *Wednesbury* unreasonable or based on a misdirection (a much higher threshold for intervention).

FOS emphasised section 225(1) FSMA which states that Part XVI FSMA on the Ombudsman Scheme "provides for a scheme under which certain disputes may be resolved quickly and with minimum formality by an independent person." FOS argued that to make eligibility a matter of "precedent fact" determinable by a court would frustrate the purpose of the scheme because of the risk that this gateway issue would be litigated by firms before allowing complaints to proceed to adjudication.

FOS also argued that the Administrative Court's decision in *R (on the application of Bankole) v Financial Ombudsman Service Limited*[3] applied to the scope of the FOS's discretion to determine jurisdiction. In *Bankole* the Court held that whether or not a complaint had been referred to the FOS within the time limits specified in DISP 2.8 was a matter within the FOS's discretion and not for the Court to determine.

Wilkie J disagreed. He saw the question of eligibility as an objective "hard-edged fact" which could be determined as a "precedent fact" by the courts without interfering with FOS's discretion. In the event that he was wrong on this point, he also considered whether FOS's decision involved a misdirection in law challengeable by way of judicial review.

First alleged misdirection of law: the point of time by reference to which the assessment of eligibility was to be made

It was common ground that the assessment of eligibility must be undertaken when the complaint is made. However, the Claimant submitted that this assessment could be based on the complainant's status at a previous time. It argued that the relevant time was when the transactions creating the relationship out of which the complaint arose, either the date of entry into the D&O policy or the date of the act or omission which was the subject of the complaint.

FOS disagreed and submitted that the complainant must fall within the definition of eligibility at the time the complaint is brought; a view with which Wilkie J concurred.

Second alleged misdirection of law: did FOS incorrectly conclude that the director was "a consumer"?

Despite agreeing with FOS on the first alleged misdirection of law, Wilkie J held that Mr Lochner was not a consumer at the time he complained to FOS.

FOS had decided that Mr Lochner, no longer a director of the company and facing personal claims against him, was acting in his personal capacity, outside of his trade, business or profession. In court, FOS argued that, as he was no longer a director, his position was no different to that of his spouse who was also covered under the policy and who, it was commonly agreed, could have been an eligible complainant. FOS also argued that the D&O policy was analogous to a Permanent Health Insurance policy and again there was no dispute that a beneficiary under such a policy could be an eligible complainant. FOS held that this conclusion was open to it on the facts and that it could not be described as irrational.

However, Wilkie J was not persuaded by these submissions. Wilkie J held that Mr Lochner, in complaining to FOS, was seeking a determination and an award for compensation for damage arising out of the claim made against him by the investors

3. [2012] EWHC 3555 (Admin).

in his former company. The claim against Mr Lochner was in respect of his alleged wrongful acts when acting as a director of the company and those acts were in the course of his trade, business or profession. The D&O policy benefitted him as an insured person only in respect of his liability to third parties (the investors) by virtue of his acting in the capacity of director, official or employee of the company and, therefore, in the course of his trade, business or profession. Not only, therefore, as a matter of "precedent fact" was Mr Lochner not a consumer but also there was no proper basis on which FOS could have concluded that his purposes were outside his trade, business or profession and FOS had misdirected itself in law.

Finally, Wilkie J opined that a group protection policy was entirely different to a D&O policy because it provided protection in respect of the private interests of the members and a complaint would be for a purpose outside the beneficiary's trade, business or profession. Nor did the fact that Mr Lochner's spouse might be able to complain assist.

Conclusion

Wilkie J held that the claim for judicial review had succeeded and he granted an order quashing the FOS's decision to entertain the complaint made by Mr Lochner.

Will FOS seek permission to appeal?

It will be interesting for FOS-watchers to see whether FOS seeks permission to appeal. The FOS's next steps may reveal how it perceives its role – either as an alternative venue for disputes independent of the courts and the regulators or as an integral part of the wider UK legal system – and whether it is happy to share the definition of its role and jurisdiction with the courts.

It may be that FOS simply wanted to seek certainty on the correct interpretation of the DISP rules and now that the Administrative Court has established the limits of its jurisdiction it will take steps internally to change the way it approaches complaints. Alternatively the curtailment of the FOS's discretion implied by Wilkie J's decision may prove unacceptable and it may try to continue the fight.

Although there is no inherent conflict between the judgment in *Bluefin* and *Bankole*, the FOS is likely to desire clarity from an appellate court as to which approach is right. Given the arguments raised by FOS and the scope for satellite litigation from firms keen to restrain the FOS's jurisdictional creep it is possible that this matter will go to appeal.

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