HAUSFELD

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Dear Dentons

Review of John Swift QC and the Financial Conduct Authority's Response

1. We note your instruction by the Financial Conduct Authority ("**FCA**") in the above matter and refer to your letter dated 22 February 2022 (the "**FCA's Response**") which responds to our client's pre-action protocol letter dated 8 February 2022 (the "**Letter of Claim**"). Defined terms in this letter take the meaning given to them in the Letter of Claim, unless otherwise stated.

2. Our client is disappointed by the FCA's Response and will now prepare its claim for issuance. However, some of the points raised in the FCA's Response fall to be addressed immediately by our client, in particular in relation to:

   a. the FCA's position and the reasons it has given for making the Decision;
   b. our client's request for further information and documentation, having regard to the FCA's duty of candour;
   c. interested parties; and
   d. costs.

3. These are set out below. For the avoidance of doubt, any issues, points, or matters in issue as a result of the FCA's Response, which are not addressed below, are not admitted by our client.

<u>The FCA's Position and Its Reasons for the Decision</u>

4. At paragraphs 2.5, 6.1, and 7.3 of the FCA's Response, it is alleged that our client is in substance seeking to challenge the decisions and actions of the FSA between 2012 and 2013. That allegation is rejected. The Decision is the subject of our client's challenge, and our client has been informed that it was made in September 2021, and it was made public on 14 December 2021.

5. Our client does allege that the decisions of the FSA in 2012 and 2013 were unlawful, but accepts that, on the basis of information presently known, such decisions are not capable of challenge by

way of judicial review. However, as described in the Letter of Claim, the regulatory landscape, insofar as relevant to the issues in dispute in this matter, is materially the same now as it was in 2012 and 2013. As such, when making the Decision, the FCA was subject to the same regulatory duties and obligations. The FCA appears to be aware of this, since the FCA's Response states that it gave consideration to whether it should seek to procure redress for the Excluded Customers when making the Decision, presumably in view of its current regulatory obligations. Further and crucially, our client and the public were only made aware of the vast body of evidence considered by the Review, much of which is centrally relevant to the challenge of the Decision and, ultimately, the matters that will fall to be determined in this dispute, upon the publication of the Decision.

6. Whilst there is inherent overlap between the events of 2012/2013 and the Decision, that does not obviate the fact that the FCA has made a new decision, subject to conventional legal principles. That the FCA has erred in law when making the Decision to the same extent the FSA did when establishing the Scheme does not erode the unlawfulness of the Decision and does not prevent the Decision from being challenged now. Indeed, it is clear from the terms of the FCA's Response itself (for example, paragraph 6.1) that the Decision was a fresh one, and therefore capable of review.

7. Further, at paragraph 6.11, the FCA alleges that the Letter of Claim seeks to use what the FCA characterises as a disagreement between the Review and the FCA as to the lawfulness of the scope of the Scheme, as a basis for our client's challenge. That allegation is not accepted. Our client's challenge is founded upon the FCA erring in law as to the basis upon which the scope of the Scheme was restricted. That is not a matter of a disagreement or difference of opinion; rather it is a matter of the correct interpretation of the relevant law and the connected discharging of the FCA's obligations in accordance with it. Neither the FCA, nor Mr Swift QC, nor our client is the ultimate arbiter in this respect. However, from everything we have observed in respect of the FCA's actions and decision-making in September 2021, December 2021 and the *inter partes* correspondence of 2022, the FCA has simply failed to engage with majority of the substance of Mr Swift QC's analysis.

8. As to paragraph 6.14 and the summary of reasons as to the alleged reasonableness and correctness of the scope of the Scheme (and thus the Decision):

    a. The pressure on the FSA in 2012/2013 to act did not provide it then – and does not provide the FCA now – with a basis to act unlawfully. By the Pilot Review the FSA had evidence to substantiate the sheer volume of mis-selling, including to Excluded Customers, and as referred to at paragraph 49 of the Letter of Claim, the FCA itself recognised the dangers of acting in haste.

    b. Further, as the Letter of Claim records in reference to the Review: (i) the FSA had no intention of denying Excluded Customers access to the Scheme. The initial intention of sub-dividing the Private Customers/Retail Clients had been to offer so-called Unsophisticated Customers automatic redress in respect of the most complex products, without factual enquiry. However, the Banks seized upon that proposal and sought to use that sub-division as a means to exclude so-called Sophisticated Customers entirely, with apparently no resistance or even discussion from or with the FSA; and (ii) the £10 million notional swap limit criterion of the sophistication test was introduced by HM Treasury, not

the FCA. The FCA's Response does not engage with these points, and they do not sit well with the FCA's current attempts (in particular in justification of the Decision) to characterise the restrictions on the scope of the Scheme as a positive and reasonable exercise of discretion in accordance with its obligations.

c. It is not accepted that the Scheme would not have been agreed if the FSA had insisted on the inclusion of all Private Customers/Retail Clients, nor that this would justify the exclusion of the Excluded Customers in any event. The FCA regulates the banks and it had and still has: (i) a firm evidential and legal basis upon which to procure agreement by virtue of the other regulatory powers available to it, both then and now; and (ii) an obligation to protect the Private Customers/Retail Clients cohort of consumers who were and are pre-defined, by pre-existing statute and regulation, as requiring the relevant protection.

d. It is a hollow argument to say that Excluded Customers were in no worse position than if the FCA had not acted at all. The same could be said of so-called Unsophisticated Customers if they had been excluded. The FCA recognised that it had an obligation to procure redress – that obligation extended to all Private Customers/Retail Clients, and the FCA therefore failed to discharge its obligation.

9. As to paragraphs 6.18 and 6.19, the FCA betrays a concerning deference to the Banks that it regulates, by suggesting that it is a material consideration that the Banks might not cooperate in the future if the FCA were to seek to properly and lawfully discharge its regulatory obligations now. That is no basis upon which to justify an unlawful decision and to repeat a prior error of law. Such an argument is contrary to the FCA's own concerns regarding abidance with the rule of law and consistency of regulation – it is not good regulation to be consistently incorrect.

10. Further, the suggestion at paragraph 6.20 that the FCA would be required to take new steps to establish that the banks had mis-sold the relevant products and that loss had been caused, is rejected. The FCA has the entirety of the evidence of the Scheme, and the evidence compiled by the Review, already available to it (in addition to other evidence that it will have gained on this issue since 2012). At paragraph 6.21 the FCA's Response refers to an "*assumption*" being made as to sales to Excluded Customers but provides no detail as to what the assumption was, and what it was based on. In fact, in the Pilot Review which included the Excluded Customers, over 95% were deemed to be non-compliant sales, and in the Scheme across thousands of transactions, it was over 90% of sales. The FCA has provided no evidence – i.e. it has put no cards face up on the table – to explain why it assumes that such a mis-selling rate did not occur in respect of sales to Excluded Customers (and we note that even on the FCA's assumption the FCA recognises that "*sizeable aggregate loss could have been experienced across some sophisticated customers*"). Our client would say that all of the evidence points to similar rates of mis-selling to those encountered in the Scheme, which provides a significant and compelling reason for redress to be provided now.

11. Moreover, our client understands that there is not a single case of an IRHP being sold to Private Customers/Retail Clients prior to 2009, in which the requirements of what is now COBS 14.3.2R(2)(d)[1] were complied with, because no IRHP mis-selling victim was ever told about the

[1] https://www.handbook.fca.org.uk/handbook/COBS/14/3.html, which was omitted from paragraph 67(e) of the Review

line of credit taken by their bank in respect of the contingent liability of the relevant product. It follows, if that understanding is correct, that all sales to Excluded Customers were non-compliant.

12. As to the remainder of the position and reasons set out in the FCA's Response, we refer to the Letter of Claim for our client's position.

Documents

13. We note that the FCA recognises its duty of candour, which requires the FCA to make full and frank disclosure and conduct judicial review proceedings with "*all their cards face up on the table*", where "*the vast majority of the cards will start in the [FCA's] hands*".[2]

14. With this in mind, we have trouble understanding why the FCA has not provided (at a minimum):

    a. a copy of the Board Paper, referred to throughout the FCA's Response. This has been described in detail and appears to be centrally relevant to the Decision, but the FCA has simply described this "*card*", rather than putting it "*face up on the table*". That is unsatisfactory, and the suggestion at paragraph 7.2 that the FCA has "*consistently explained the reasons for the Decision which are further elaborated upon at paragraphs 6.11 to 6.27 above [i.e. in substantial reference to the Board Paper]*" sits uncomfortably with the fact that our client and the public have never seen the Board Paper, the FCA has not provided a copy, and only by the FCA's Response has its existence become known to our client;

    b. minutes of the FCA Board meeting of July 2021, and what is referred to as a "*draft response*", both referred to at paragraph 6.2, and apparently of central relevance to the Decision; and

    c. any documents which explain and record the basis of the assumption referred to at paragraph 10 above and paragraph 6.21 of the FCA's Response (the "**Assumption Documents**").

15. We therefore request copies of (i) the Board Paper; (ii) the minutes of the Board meeting of July 2021 and any document relating to that meeting equivalent to the Board Paper; (iii) the "draft response"; and (iv) the Assumption Documents. If these documents will not be provided, please provide detailed reasons why, in reference to the FCA's compliance with its duty or candour.

16. With regards to the requests for information and documents in the Letter of Claim, the FCA's Response quotes (at paragraph 10.1) the pre-action protocol which states that each request that satisfies proportionality should be met: *"The defendant should comply with any request which meets these requirements unless there is good reason for it not to do so"*. However, the FCA's Response then suggests (at paragraph 10.3) that the volume of requests made is such that the FCA will not respond to any: "*In respect of the other documents requested, our client considers that the breadth of documents being sought is not proportionate and falls short of the guidance in the Pre-Action Protocol*."

[2] *R v Lancashire County Council, ex p Huddleston* [1986] 2 All ER 941 at page 945

17. We note that the FCA has not responded to paragraph 108 of the Letter of Claim at all. We request that the FCA now provides a response. If its answer to any of 108(a), (b), and/or (c) is to the effect that no such consultations took place, please confirm that is the case expressly.

18. As to the requests for documents at paragraph 109 (b), the FCA's Reponses appear to imply that the FCA has no documents that fall into this category that are relevant to the Decision. We request that it confirms that this is the case.

19. In respect of all other document requests that have been made, our client's position is reserved.

Interested Parties

20. As to paragraph 8.1, our client has given consideration as to whether any group or groups representing Excluded Customers ought to be interested parties. We do not consider that such groups should properly be included as interested parties because only the FCA will be bound by any decision of the court. Any effect on wider groups and the Excluded Customers will be indirect and as a consequence of what the FCA may or may not be required to do upon the court's direction. In any event, our client is in contact with several such groups, all of whom support the course being adopted by our client.

21. The same applies as regards the Banks. These proceedings relate to the FCA and the lawfulness of its actions. The Banks will not be bound by any decision of the court and any effect will therefore be indirect.

Costs

22. We refer to paragraphs 3.2 and 12.1 of the FCA's Response, in which you (i) seek clarity as to how our client is funding these proceedings; and (ii) state that the FCA will likely seek security for costs.

23. The APPG is not a legal person, but it is supported by a corporate secretariat, the Athena Foundation Limited (company number 09944760). We are instructed by the members of the APPG, each of whom is acting in their capacity as either elected members of the House of Commons or members of the House of Lords. None of the members has an economic interest in the claim and it is being pursued by them on the basis that it is in the public interest.

24. The APPG has very limited means, which are raised entirely through donations, is funding its own legal costs for the judicial review via donations (with the legal teams working at very substantially reduced, and loss making, rates), and would not able to meet the costs of the FCA in the event that it does not succeed in its claim. The APPG will therefore be applying for a Judicial Review Costs Capping Order at upon issuance of the claim. The APPG will be unable to proceed with the claim if such an order is not granted.

25. We consider it likely that such an order will be granted given the wide public importance of this case, the thousands of people who were affected by IRHP mis-selling, and, importantly, the profound importance to society as a whole of a financial regulator that functions properly, lawfully and is fit for purpose. We invite you to confirm whether or not your client will resist the making of such an order.

Conclusion

26. We request that you provide the documents and information requested at paragraphs 15, 17, and 18 above by no later than 4 March 2022.

27. As with previous correspondence, this letter will be placed in the public domain.

Yours faithfully

Hausfeld & Co LLP

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