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Juggling Conflicting Demands: The Case of the UK Financial Ombudsman Service FREE

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Abstract

This article builds upon current scholarship regarding regulatory enforcement to analyze and theorize the little-researched context of public bodies' handling of consumer complaints against firms. The analysis is based on a case study of the Financial Ombudsman Service (FOS), which is a British public agency that handles consumer complaints regarding the retail selling of financial products. The study documents and seeks to explain the FOS' and firms' interaction and their choices between cooperative and adversarial strategies. It finds that the FOS' interaction with firms oscillated between cooperative informal conciliation and adversarial standardized determination of complaints. Firms resisted informal conciliation of complaints when concerned that their agreement to redress an individual complainant might be interpreted by the regulator (the Financial Services Authority), or the media, as entailing compensation awards to a large number of other customers in similar circumstances. Equally, the ombudsman was inclined toward an adversarial, precedent-bound approach to complaints when facing external risks to its autonomy and reputation. These findings form the basis for the formulation of hypotheses regarding the strategic interaction of other third-party complaint handling schemes with both private and public service providers. Furthermore, the findings stress the importance of analyzing regulatory encounters as multiactor games in which firms and regulators interact amid conflicting demands and uncertainties posed by other actors and institutions in their environment.

INTRODUCTION

of the British and Irish Ombudsman Association include 10 organizations that handle consumer complaints against private firms alongside 10 ombudsman schemes that scrutinize public sector bodies. However, empirical studies of these institutions and their interactions with firms are scarce (notable exceptions include Nader 1980; Steele 1974). In contrast, numerous studies have explored regulators' and firms' strategic interaction in the context of legal enforcement. This article builds upon the latter scholarship to analyze and theorize the little-researched context of third-party complaint handlers' interactions with firms.

The article is based on a case study of the Financial Ombudsman Service (FOS), which is a British public agency that handles consumer complaints regarding the retail selling of financial products. It documents and seeks to explain the FOS and firms' interaction and their choices of cooperative versus adversarial strategies. It finds that the FOS' interaction with firms oscillated between cooperative informal conciliation and adversarial standardized determination of complaints. Firms resisted informal conciliation of complaints when concerned that their agreement to redress an individual complainant might be interpreted by the regulator (the Financial Services Authority [FSA]), or the media, as entailing compensation awards to a large number of other customers in similar circumstances. Equally, the ombudsman was inclined to adopt a formal standardized approach to complaints when facing multiple risks to its autonomy and reputation. These findings form the basis for the formulation of hypotheses regarding the strategic interaction of other third-party complaint handling schemes with both private and public service providers. Furthermore, the findings stress the importance of analyzing regulatory encounters as multiactor games in which firms and regulators interact amid conflicting demands and uncertainties posed by other actors and institutions in their environment.

In what follows, the theoretical section builds upon studies of regulatory enforcement to derive initial directions to the analysis of firms and third-party complaint handlers' choices of cooperative versus adversarial strategies. Thereafter, the research methodology and case study are presented. Next, the reader is provided with thick description of two case studies of the FOS' interaction with firms, which depict the key patterns that are later analyzed. The article builds upon the two case studies and additional data to explain the FOS' strategies and firms' responses to them. Finally, the discussion and conclusion summarize the empirical findings and discuss their implications for the study of third-party complaint handling

Rational choice analyses of enforcement may be crudely divided into those that treat such interactions as two-actor games (between regulators and firms) and those that highlight the multiactor nature of regulatory domains. The former type of analyses put their emphasis upon regulators' aims to achieve regulatory objectives at minimum costs and firms' interests in minimizing regulatory burden. In what has become a standard postulation, these studies suggest that regulators are able to achieve their goals by adopting a responsive regulatory approach. That is, shying away from sanctions in cases of technical breach of rules and supporting firms' efforts to comply while punishing firms for violations that engender substantive risks (Ayres and Braithwaite 1992, chap. 2; May and Wood 2003; Scholz 1984). This scholarship further predicts that, in response to such responsive regulatory strategy, most firms will reciprocate by engaging in compliance with the objectives of regulation even beyond formal legal requirements. It therefore expects firms and regulators' iterated interactions to yield a benign equilibrium involving responsive regulation and voluntary compliance.

Extension of the above analysis to the context of third-party complaint handling suggests that in the same manner that regulators seek to secure firms' compliance, third-party complaint handlers presumably aim to process cases and redress what they assess as worthy complaints. They further aim to reduce the time and resources involved in the handling of complaints so as to mitigate their workloads and case backlogs. The scholarship regarding public ombudsmen suggests that complaint handlers might attain these aims by winning service providers' consent to remedy complainants' grievances on the basis of informal conciliation of complaints in lieu of time-consuming investigations and formal decisions (Jamieson 1999; Seneviratne 2002, 223–5). Rational firms would presumably cooperate with informal conciliation insofar as it minimizes their overall compensation payouts and mitigates risks to their reputation. I suggest that complaint handlers might encourage firms' consent to informal conciliation of complaints by adhering to two strategies. The first regards complaint handlers' resolution of complaints on a case-by-case basis so as to achieve equity in individual disputes (hereafter, “individual-dispute resolution”) rather than formulation of general standards (or precedents) and their uniform application across categories of cases. Adherence to individual-dispute resolution might encourage firms' amenability to conciliation if they are assured that their agreement to redress in one case would not automatically entail compensation to other clients in similar circumstances. In this way, individual-dispute resolution lowers firms' stakes in settling

The second strategy that cooperation-seeking complaint handlers might employ involves their adherence to confidential resolution of complaints rather than giving publicity to their decisions and sharing information gathered from complaints with other institutions and the media (e.g., Jacoby 1999a). Complaint handlers' management of complaints provides them with access to abundant information regarding firms' failures to satisfy their customers. Some complaints may expose firms' breaches of regulations and/or systemic problems in their internal compliance systems. Such information is of interest to both regulators and the media. To encourage firms' cooperation with informal conciliation, complaint handlers might prefer confidential resolution of disputes and avoid sharing information from complaints with third parties. Under these conditions, complaint handlers' power to selectively pass information to the regulator with regard to obstructive firms, or to name and shame such firms in the public domain, turns into a powerful disciplinary tool given the value that most firms attach to their corporate reputation (Gunningham, Thornton, and Kagan 2005; Parker 2002). In sum, it is proposed that in the same way that responsive regulation encourages firms' voluntary compliance, complaint handlers' *selective* adherence to individual- and confidential-dispute resolution might encourage firms' consent to informal conciliation.

Few regulatory studies further analyze the conditions under which interactions between rational regulators and firms fail to yield cooperative equilibriums, suggesting that adversarial, rules-based interactions may result due to both regulators' and firms' aims to maximize credit and avoid blame in multiactor environments. Most notably, Bardach and Kagan's (2002) study of environmental regulation suggests that consumer groups' monitoring of the regulatory process may induce regulators to adopt rules-based uncooperative forms of regulation. The micromechanism leading to rigid, rules-based regulation, as suggested by Bardach and Kagan, involves a combination of consumer groups' control over regulatory agencies via the political arena and agencies' defensive responsiveness to foreseeable criticism. Strict adherence to rules protects regulators against accusations of leniency from proregulation advocates and against firms' allegations of unpredictable, inconsistent, and unfair regulation. Olson (1995, 1996) following Noll's (1985) "external-signals" framework suggests that regulators' choices of enforcement strategies are shaped by their motivation to maximize positive feedback and minimize negative feedback from multiple external audiences of which firms are only one, albeit important, group. This scholarship implies that regulators might engage in adversarial, rule-bound enforcement strategies, despite their inefficiencies, to protect

Kagan, and Thornton 2004; Gunningham, Thornton, and Kagan 2005; Koski and May 2006; May 2004; Parker 2002). Although this literature has emphasized that firms' reputation sensitivity leads them to overcomply with regulation, the findings of this article suggest that it may further give rise to their conflict with regulators.

Likewise, firms and third-party complaint handlers may choose to forgo the cost-effectiveness of informal conciliation due to their aims to maximize credit and avoid blame in their interactions with a variety of stakeholders. Complaint handlers might opt to conduct thorough investigations and adopt precedent-based decision making so as to preempt challenges of their judgments and criticisms of their inconsistency. They may be disposed to share information from complaints with other institutions, such as regulators, in order to secure these bodies' support and cooperation. Finally, they may proactively seek media coverage of their decisions on behalf of complainants so as to enhance their public image. Similarly, firms might object to informal conciliation if they believe that their agreement to redress in one instance might open them to criticisms of inconsistent, unfair, and even unlawful treatment of other customers.

METHODOLOGY

Research Design

The data upon which the article is grounded were gathered during nonparticipant observation research at the FOS, conducted between November 2003 and December 2004, including (a) random sample of complaint files, drawn from all cases handled by 12 FOS adjudicators, from two adjudication teams, over a period of over 3 years. This offered rare insight into complaint handlers' microinteraction with firms, (b) interviews with 34 FOS officials, 4 FSA officials, 1 Treasury official, 1 representative of the Association of British Insurers, and a number of former financial ombudsmen,[1] (c) FOS internal correspondence and guidance, and (d) observations at the FOS' offices, including internal talks and training sessions.

Case Study Background

The FOS was created by statute in 2000 merging seven previously separate

complainant, who was dissatisfied with the firm's decision, could request its review by the FOS. Between 1999 and 2004, the yearly number of complaints reaching the FOS escalated from 25,000 to 100,000. These complaints, which filtered through to the FOS, comprised around 0.2% of retail financial sales and 2%–10% of the complaints to firms.[2] Thus, although numerous, the volume of complaints to the FOS was small when compared with firms' financial sales and their internal handling of customers' complaints. The increase in the number of finance-related complaints, in general and to the FOS in particular, may be attributed to two factors. One was consumers' loss on investments as a result of financial markets' collapse following the September 11, 2001, attacks and their decline throughout 2002 and 2003 in response to the burst of the "dot-com bubble." The other was vigorous media coverage of retail finance "mis-selling"[3] scandals and of the FOS' decisions. Financial firms, the industry regulator the FSA, and the FOS were all exposed to close media scrutiny regarding their responsibility for consumer loss and its management.

As elaborated below, the FOS' institutional structure—its operational autonomy from the FSA and its decentralized decision making—privileged and facilitated informal conciliation rather than formal determination of complaints. This structure borrowed from, and partly differed, from the traditional Scandinavian ombudsman archetype and from the British Parliamentary Commissioner for Administration (hereafter, the British parliamentary ombudsman) that was modeled on the Scandinavian example.

The FOS' duties of accountability partly differed from those of traditional ombudsman schemes. A classic ombudsman is an independent body which directly reports to parliament. The FOS in contrast was accountable for its financial expenditure to the FSA, which nominated the FOS Board members. Yet, the FSA (and the FOS Board) had no authority to intervene in the ombudsman's exercise of its professional judgment, and it generally steered clear of such interference. Although the FOS was expected to take account of FSA's regulations, its mandate empowered it to make judgments on complaints "by reference to what is, *in the opinion of the Ombudsman*, fair and reasonable in all the circumstances of the case" (The Financial Services and Markets Act 2000, sec. 228). Moreover, the FSA and the FOS both held that in judging what is "fair and reasonable," the FOS was not bound by FSA's regulations and that its decisions in favor of complainants did not necessarily imply that firms were in breach of regulations. The FOS' operational autonomy from the FSA and its broad mandate enhanced the ombudsman and firms' flexibility to settle complaints according to their

decisions and the FSA's regulations were guided by a joint set of broad principles, which reflected established notions in the retail investment professional community. These outlined what amounted to "suitable" investment advice and required firms to match investment products to customers' "attitude to risk," needs, and financial capability.[4] However, these principles were themselves rather ambiguous, and the FSA was reluctant to lay down detailed prescription regarding their implementation (FSA 2003).

Unlike classic ombudsmen who are restricted to making recommendations only to service providers, the FOS had formal authority to require firms to redress complainants. However, the FOS' informal structure rendered this formal authority less significant. The FOS operated a de facto two-tier complaint handling process. All complaints were initially handled by low-level complaint handlers ("adjudicators") who had no formal legal authority. During the research period, the FOS employed over 400 adjudicators. When adjudicators found a complaint to be prima facie valid, they issued an initial assessment and recommendation to the firm to offer compensation to the complainant without further formal decision. Firms (and complainants) were entitled to challenge adjudicators' assessments by requesting a formal review by an "ombudsman," of which there were 19 at the time of this research. Requests for an ombudsman's review increased the FOS' case backlogs due to the relatively small number of ombudsmen and the carrying out of further and more thorough investigations. Consequently, despite the FOS' formal power to authoritatively determine complaints, the organization's internal two-tier structure rendered its complaint handlers reliant upon firms and complainants' consent to informal conciliation.[5] This was especially the case given the FOS' rapidly increasing caseload during the research period.

Both adjudicators and individual ombudsmen enjoyed a considerable degree of individual discretion in handling complaints. Casework managers' supervision tended to focus more upon the swiftness of case handling and the quality of adjudicators' interpersonal interactions with complainants and less upon the content of adjudicators' professional judgments (Gilad 2006, 2008). Ombudsmen, at the time of the research, were not formally supervised, and although they held regular meetings to discuss complex cases and general policy matters, they enjoyed substantial individual discretion in reviewing adjudicators' informal decisions. This decentralized structure, which bestowed substantial discretion upon adjudicators and ombudsmen, created an apt environment for the FOS' case-by-case,

its role to individual-dispute resolution rather than formulation of general precedents to guide the FOS and firms' handling of other complaints and transactions.

The above suggests that the FOS' operational autonomy from the FSA, its two-tier structure, its decentralized decision-making structure, and the organization's ethos privileged complaint handlers' adherence to informal individual-dispute resolution. The above theoretical discussion would suggest that complaint handlers' preference for individual-dispute resolution was likely to encourage firms' cooperation with informal conciliation. On the whole, over 90% of complaints were informally settled by adjudicators without recourse for ombudsmen's formal decisions. However, the ratio of firms' appeals for an ombudsman's review varied substantially between adjudication teams and areas of work. In the two researched teams, firms' inclination to request an ombudsman's review was higher than the organizational average, and this was especially the case in one of these teams. High ratios of firms' appeals for an ombudsman's review were typically associated with the FOS' handling of new influxes of complaints of a systemic nature. This emerged as a salient issue in interviews and case file data regarding the two researched teams, as well as in interviews with participants outside these two teams. The analysis below focuses upon, and seeks to explain, instances in which the FOS and a number of large retail investment firms experienced such antagonistic interactions.

TWO ILLUSTRATIVE CASE STUDIES

Below are two case studies of the ombudsman's handling of what were then new types of complaints of a systemic nature. The first case study is based on analysis of sampled complaint files regarding two teams and interviews. The second case study is based on public FOS press releases and newsletters, media analysis (LexisNexis), the Chief Ombudsman's address to the Building Societies Association annual conference and interviews. The aim of these illustrations was to depict key tendencies in the FOS and firms' interactions in instances of tension. Later in the article, I build upon the two case studies, and additional data, to further explain these tendencies and their root in the uncertainty and demands that complaint handlers and firms faced from other actors and institutions in their environment.

Risk Rating of Firms' Products

with a corresponding high-risk profile. A few ombudsmen analyzed the products' investment structure and guided adjudicators as to what they perceived to be the correct risk ratings. The result was that adjudicators consistently upheld the complaints on the grounds that firms incorrectly evaluated the risk of the investments, which they marketed to their clients. This closely coordinated decision-making differed from the FOS' usual adherence to decentralized individual-dispute resolution. Firms persistently requested ombudsmen's review of adjudicators' informal assessments and protested to FOS senior executives. Interviewees explained that firms were disinclined to accept informal conciliation because they were concerned that, in the event of an FSA inspection, their agreement, in an individual case, that their risk rating was flawed might result in the FSA requiring them to apply the decision to a larger set of analogous complaints and past sales. An ombudsman put it like this:

> If we say [to the firm that the risk of] this fund is not this risk [as claimed by the firm], then they [the firm] come across a problem that we're saying that to them, issuing hundreds of decisions to them, and the FSA [might] walk in the next day and say, "So, is this fund not this risk?" And then they've got a hundred thousand other cases, which they might have to proactively review, which costs them a fantastic amount of money (interviewee O2).

The same point was made by another ombudsman in an internal talk to complaint handlers:

> Most firms accept our [risk] rating scale. But...some...do not...They have sold thousands of products to low-risk consumers. If they agree with us, the FSA may come round and say, "You agreed with the Ombudsman on this case, so why don't you compensate all those who bought it." And they'll say "Right" and go bust (field notes, July 2004).

The FOS' threat that it will report the resistant firms to the FSA did not result in their cooperation. Moreover, when the FOS reported a few of the resisting firms to the FSA, seeking its assistance, the regulator was disinclined to intervene. Following further negotiations between firms and the FOS, it was agreed that in future, complaint handlers would restrict themselves to judging whether the products were suitable to the needs of individual complainants. Adjudicators were guided to focus their analysis upon firms' assessment of the complainants' individual risk profiles and financial needs

cooperation with consensual resolution of those complaints that reached the FOS. Analysis of complaint files shows how, following the above compromise, one firm adopted a strategy according to which it rejected complaints that reached it but voluntarily offered compensation to those complainants who referred their case to the FOS. Another firm still tended to request ombudsmen's reviews in these cases.

Dual Variable Rate Mortgages

In mid-2001, the FOS received some 600 complaints alleging unfair and unequal treatment by five financial firms, which offered low mortgage rates to new customers while tying some of their existing clients to higher rates. At the relevant time, the selling of mortgages was not regulated by the FSA.

As the FOS was in the process of assessing the relevant cases, the complaints were already widely covered by the popular press. In September 2001, the FOS made an initial decision in favor of the complainants in two cases. It then announced that it would handle subsequent complaints by employing Lead Cases with regard to each firm, operating as de facto precedents, while allowing firms and individual complainants to argue that their case differed from the Lead Case. This approach was considered within the FOS as innovative and breaking away from the organization's customary adherence to decentralized, individual-dispute resolution. The media closely covered both the FOS' decisions and firms' "compliance" with them. Consequently, the number of similar complaints to the FOS rapidly escalated (from 570 in 2001 to 6,500 in 2002).

One of the five firms made a first move to restore its reputation and announced its intention to voluntarily extrapolate the FOS' decision to all its customers who were in a similar position, resulting in some 90 million pounds of compensation. The media then put pressure on its competitors to follow, which they did reluctantly in varying speeds and degrees. Another firm, for whom the financial implication of applying the FOS' ruling across the board was especially high, was particularly reluctant to apply the decision to other complaints and transactions. It therefore attracted considerable adverse media coverage.

The FOS' decisions were rewarded with strong consumer and media support, as well as endorsement from backbench MPs. The FOS' measurement of complainants' satisfaction with its services during this period peaked as a result of the organization's popular image in the press. Yet, the financial

members to the Treasury to limit the FOS' powers by introducing judicial appeal over its decisions and for the FSA to take over the future handling of complaints of a systemic nature. In response, the Treasury initiated a review to assess the need for change in the regulatory framework. This was followed by deliberations with firms and a public consultation issued by the FOS and the FSA. The consultation resulted in a compromise that required relatively minor changes to the FOS' processes.

Overall, the above case studies indicate the following tendencies in the FOS' conflict with financial firms when handling new complaints of a systemic nature. First, the case studies manifest complaint handlers' inclination to standardize their handling of new influxes of widespread complaints rather than resolving complaints on a case-by-case basis. Second, they suggest a variation in firms' willingness to engage in informal conciliation in light of their sensitivity to the risk of future regulatory intervention and/or adverse media publicity that might entail application of the ombudsman's decisions as precedents to other similar complaints and transactions. Third, the case studies depict the FOS' inclination to "discipline" firms' uncooperative behavior by reporting systemic problems to the FSA but not to the media. Fourth, they suggest that firms were not necessarily responsive to FOS' threats that they will be reported to the FSA and that the FOS' reporting of firms did not always result in regulatory intervention. Moreover, the case studies reveal firms' ability to retaliate and endanger the FOS' operational autonomy by calling for political intervention. These tendencies are further analyzed below in light of the initial theoretical discussion.

FOS' AND FIRMS' STRATEGIES IN A MULTIACTOR GAME

The theoretical section proposed that complaint handlers might encourage firms' consent to informal conciliation by adherence to individual- and confidential-dispute resolution and induce the future cooperation of resistant firms by passing information from complaints to third parties, such as regulators, or by naming and shaming them in the public domain. It was further suggested that complaint handlers and firms' gains and constraints in multiactor games might lead them to forgo such selective, cooperation-seeking strategies. The following analysis relies upon the above two case studies and additional data to analyze the FOS and firms' strategies. The analysis commences with depiction of the micromechanisms that drove

name and shame firms in the public domain and why despite this approach, it sometimes failed to win firms' cooperation.

Alternating Individual-Dispute Resolution and Standardization

The FOS' dominant complaint handling strategy privileged individual-, ad hoc, dispute resolution. As mentioned, this strategy was reflected in the ombudsman's organizational ethos and embodied in its decision-making structure, which granted adjudicators and ombudsmen broad individual discretion when handling what were perceived as "one-off" complaints. Although many of these one-off complaints were part of widespread systemic incidences (e.g., endowment mortgage complaints, which constituted more than half of the FOS caseload[7]), they were nonetheless perceived by both firms and the FOS as presenting infinite variance. In contrast, when handling new influxes of complaints of a systemic nature, such as the above illustrative case studies and other similar cases, adjudicators' decisions were governed by their standardized application of centrally elaborated guidance by the ombudsmen.

Standardization of complaint handlers' decision making was associated with the FOS' conflict with firms. As illustrated in the above case studies and elaborated upon in the next sections, when faced with standardized decisions, firms were under increased pressure, due to their concerns with future regulatory intervention or media scrutiny, to apply the ombudsman's decisions to similar complaints and transactions beyond those that reached the FOS. In response, the FOS faced industry allegations that it was pursuing a regulatory role, setting and implementing principled decisions with wide implications. For example, a senior executive's internal e-mail to all employees asserted:

> [The FOS] has been subjected to unprecedented scrutiny ... by industry bodies concerned about a drift away from individual dispute resolution to decisions of principle with potentially wide-ranging application (FOS, unpublished internal communication, November 2003).

A senior member of the FOS' Board of Directors similarly commented on the industry's criticism that in its handling of complaints of a systemic nature, the ombudsman exceeded its legitimate role:

Yet, as further explicated in the next sections, the FOS was not necessarily able to win firms' cooperation by adhering to individual-dispute resolution in these cases. Some firms were concerned with any ombudsman decision that could potentially be interpreted by other actors—the FSA or the media—as applicable to other cases. As demonstrated below, these firms tactically tracked inconsistency in the ombudsman's handling of similar complaints in order to challenge what they perceived as decisions with potentially wide implications.

The dynamics that led complaint handlers to standardize their approach to new complaints of a systemic nature is illustrated below through microanalysis of one complaint. In this instance, an adjudicator was allocated a complaint while the FOS was in the course of a fierce dispute with another firm with regard to the risk rating of its investment products. The adjudicator was inclined to endorse the complaint. However, before doing so, he requested advice from an ombudsman, writing "I am mindful of the situation with [another firm's] fund and so would like to be sure of my ground before writing to the firm." The ombudsman replied that he believed that this firm adequately risk-rated its product. Yet, acknowledging the danger in inconsistent decisions concerning the two firms, the ombudsman suggested that the adjudicator gathers additional information from the firm (to ascertain the differences or similarities of the two firms' cases) and thereafter seeks further advice from two additional veteran ombudsmen. In reply to the adjudicator's request for further information, the firm's complaints administrator pointed out that in the past, the FOS decided five similar cases in its favor. Yet, the two ombudsmen, from whom the adjudicator was guided to seek further advice, recommended that the firm's risk rating of the product was incorrect and that the complaint should be upheld. The adjudicator therefore issued a decision in favor of the complainant and sent out an e-mail notification to all his team members to ensure future consistency. The FOS issued four additional similar adjudications to the firm. The firm appealed for an ombudsman's review in all five cases. In its application for ombudsman's reviews, the firm once again contended that in the past, the FOS adjudicated similar cases in its favor, including one decision by an ombudsman. Prior to the ombudsman's review of the pending cases, a meeting was held between the ombudsman, the firm's chief compliance officer, and the fund manager. Following this meeting, a compromise was reached between the FOS and the firm regarding the future handling of similar cases. This entailed particularization of the FOS' adjudication of future complaints, that is, focusing upon complainants' individual circumstances, rather than the firm's risk rating of its products.

firms' inclination to track inconsistency across time in the FOS' decisions and to use it as a defense against adverse decisions. Foreseeing such criticism, and until the point of compromise with the firm, complaint handlers secured a high degree of centralization and coordination of their individual decisions.

Similarly, during the research period, the FOS coordinated its internal approach to the handling of Precipice Bonds[8] complaints, which attracted intensive press coverage. To maximize internal consistency, the handling of Precipice Bonds complaints was allocated to a small number of specialized teams of adjudicators, who closely coordinated their approach. Adjudicators were provided with product-specific training and guidance from the ombudsmen. Additionally, following requests from the FSA, there was also close cooperation and exchange of information between the two agencies. Interviewees explained that Precipice Bonds required a standardized approach because of the intense media coverage that was associated with them. For example, a senior FOS official explained that in response to media coverage around Precipice Bonds, the FOS both internally homogenized its approach and closely coordinated with the FSA.

> We [the FOS and the FSA] have got a coordinated approach to all the Precipice Bonds stuff ... In fact we [the FOS] are aiming to deal with them on a very coordinated approach, such that if we find issues with a certain firm ... we would actually then batch all those cases and deal with them on a very quick follow through ... it's probably politics as much as anything ... it was very high profile. FSA were always in the press about "Are you looking to make sure that people are OK with Precipice Bonds?" "What were you doing about it in terms of regulation?" ... it certainly became the case that very quickly the FSA and the FOS ... needed to have ... some kind of coordination about it. And indeed we have our own [internal] coordinated approach to dealing with Precipice Bonds as well (interviewee S3).

The above data suggest that standardization was induced by complaint handlers' expectation of firms' resistance to their pro-consumer decisions, as well as in response to media coverage of the FOS' decisions. Under these conditions, individual adjudicators anticipated firms' appeal for an ombudsman's review if the complaint was upheld and they wanted to commit the ombudsmen to their position in advance. Similarly, ombudsmen operated under the assumption that firms might apply for judicial review in

explain the logic of the organization's decision making. In short, standardization was shaped by the concurring motivations of complaint handlers on different levels of the organization to avoid blame in their interaction with other actors and institutions. Although standardization intensified the FOS' conflict with firms, it was a rational strategy given the risks for blame that the organization and individuals within it were facing.

Regulatory Involvement

The FOS was usually reluctant to share with the FSA firm-specific information, such as the ratio of cases, which it decided in favor of complainants out of a firm's overall complaints. Interviewees explained that passing this type of information to the FSA would discourage firms' cooperation with informal conciliation, because a firm's agreement to settle a large number of similar complaints would have resulted in an abnormal upholding rate, which could have raised questions from FSA supervisors. A senior FOS executive explained,

> If we just passed unqualified data to [the FSA], supervisors ... might suddenly jump on ... and say "oh goodness you seem to uphold a lot more complaints against this [firm]" and ... rush off to the firm saying "oh, you've been behaving badly here" (interviewee E6).

However, encouraging firms' cooperation with informal conciliation of those complaints that reached the FOS was not the ombudsman's sole concern. Interviewees suggested that they would threaten a firm that it will be reported to the FSA if its customers' complaints indicated a clear breach of regulations regardless of the firm's amenability to redress the minority of complainants who pursued their case all the way to the FOS. That is, unless, in response to such threat, the firm would agree to redress future complaints by its customers irrespective of whether or not the complainants appealed to the FOS. The above senior executive explained this policy, noting that passing information to the FSA in these circumstances was perceived as an exception to the ombudsman's general preference for individual- and confidential-dispute resolution:

> We see ourselves as an organization that is involved in private dispute resolution ... We are not in the business of naming and shaming firms, we are not in the business of shopping them to the regulator for minor things ... our business is dispute resolution. If we can resolve disputes that's fine ... Unless there is something of a

> evidence, but sometimes we think it's necessary to tell them (interviewee E6).

Similarly, an FSA official, who had regular interactions with the FOS, suggested that the FOS would report a systemic problem when it perceived a firm's behavior to be "egregious" irrespective of the firm's amenability to informal conciliation:

> I think they [the FOS] ... have a general public interest concern, as well [as an interest in resolving those complaints that reach the FOS], that if there are lots of people who are bothering to go to the Financial Ombudsman Service, who are being treated inappropriately [by firms], then there's probably a ... much bigger group of complainants who have not challenged what the firm has said but have also been treated inappropriately and unfairly ... and is something that they [the FOS] feel is appropriate for them to report. But that has to be fairly egregious behavior (interviewee T4).

Yet, other interviewees explained that although in principle the FOS would report a clear breach of regulation by a firm that systematically rejected its customers' complaints while offering redress to those complainants who appealed to the FOS, it did not proactively compile information to expose such conduct. In practice, adjudicators were unlikely to probe behind the reasons for firms' voluntary offer to redress complainants, because it was in their interest for complaints to be informally conciliated as swiftly as possible. Interviewees could not recall a case in which an "amenable" firm was reported to the FSA other than with regard to endowment mortgage complaints. In the latter case, it was the sheer volume of complaints that strained the FOS' resources, creating a special incentive for complaint handlers to monitor and report systemic failures in firms' internal management of complaints.[9] In other cases, a firm's mismanagement of complaints or a systemic failure in its selling practices was likely to go undetected if it was inclined to offer redress once complaints reached the FOS, because there was no pressing incentive for adjudicators and their team managers to raise it with ombudsmen or executives as a problem.

In contrast to the FOS' general caution regarding sharing firm-specific information with the FSA, it was inclined to invoke the threat of passing information to the FSA when uncooperative firms persistently challenged adjudicators' decisions by appealing for ombudsmen's reviews with regard

refer cases up the ladder for consideration by their line managers, ombudsmen, and executives, and the latter were therefore more likely to conclude that the complaints indicated a systemic failure that entailed reporting to the FSA. Interviewees asserted that in response to the threat of being reported to the FSA, a lot of firms not only were cooperative with handling their cases at the FOS but also further ensured that similar complaints did not reach the ombudsman in future. That is, in fear of being reported to the FSA, these firms were inclined to offer redress to all their customers who filed a similar complaint with the firm or at least to do so inasmuch as complainants showed determination to appeal to the FOS.[10] Yet, as illustrated in one of the above case studies, not all firms were responsive to the FOS' threats.

When firms did not respond to the threat of being reported to the FSA, and after first exhausting all means of amicable communication, the FOS sometimes reported recalcitrant firms to the FSA in order to attain the latter's assistance. Such threats presumably put firms in danger of FSA enforcement, as well the risk that the FSA will require them to apply the ombudsman's decision not only to all similar complaints but also to all their past sales of the relevant product. However, as illustrated in one of the above case studies, reporting firms to the FSA was not always effective in mobilizing FSA enforcement and large-scale redress. Complaint handlers were therefore uncertain about the conditions under which provision of information to the FSA would instigate a vigorous regulatory response. Consequently, they were relatively slow to act upon their threats and report firms to the FSA. For instance, a team manager contended,

> I could think of one firm that was pushing everything to a final decision [by an ombudsman] and we issued a bundle of decisions in one go, with a covering letter from the ombudsman saying, "Right, now, if you don't start falling into line, we'll tell the FSA you're not being fair to your customers." So, we do use it sometimes as a threat … that we will … say to the FSA, "There's a problem here and they're [the firm] not being fair to their customers, it's causing us a problem, something needs to be done here." I'm not sure there's a great faith, always [at the FOS], that the FSA is that interested or willing to sort some of the problems out … So … you don't know if it's worthwhile [to report firms] (interviewee M1).

Complaint handlers suggested that firms were equally uncertain whether a report by the FOS will put them at risk for FSA enforcement or large-scale

> For firms, it was always a gamble ... There was always the hope [on the firm's side] that ... maybe the FSA wouldn't think it was as serious as we did, or maybe that wasn't number one on the FSA's priorities that year ... So, maybe, when it came to the crunch of having to deal with the FSA about it, they could get their lawyers involved ... they might be able to find a way through it .... Just because we reported it ... didn't necessarily mean that something absolutely terrible was going to happen (interviewee E1).

The FOS and firms' uncertainty regarding the FSA's likely response was at least partly related to the above-mentioned ambiguity surrounding the notions of advice suitability and "investment mis-selling."[11] Moreover, as mentioned earlier, the FSA and the FOS maintained that the ombudsman's mandate of fair and reasonable provides consumers with protection, which may exceed firms' duties according to the FSA's regulatory requirements. Under these conditions, firms had to make a judgment as to whether an ombudsman's decision in favor of a complainant is likely to be interpreted by the FSA, ex post, as indicative of their breach of regulation.

Further data are needed in order to fully account for the variance in firms' responses to the FOS' decisions and threats in light of their uncertainty regarding the FSA's likely response. I tentatively suggest that this variance was shaped by a combination of firms' relative tolerance to the risk of regulatory enforcement and the costs of applying the ombudsman's decision across the board, given the number of similar complaints and the average redress per complaint. An official of the Association of British Insurers, the main industry trade body, succinctly explained,

> [Firms are] not obliged [to apply an ombudsman's decisions to other complaints]. They will need to take a commercial decision ... What's the cost of upholding these cases [and paying redress] versus what's the risk of not doing it? And, for better or worse, they will make a decision which is based on where they are most comfortable to sit as an organization (interviewee T7).

In line with the insight of the above interviewee, it seems that highly risk-averse firms were inclined to systematically apply the ombudsman's decisions to all similar complaints that reached them (in addition to those that were filed with the FOS) in order to avoid the threat of being reported to the FSA. If the issue was to come up in a future FSA supervision, these firms could show that once an ombudsman decision alerted them that their

the FOS. Under these conditions, the FOS was likely to eventually report them to the FSA. Disputing the ombudsman's decisions and resisting informal conciliation put these firms in a position to further argue their case with the FSA. Given the relative ambiguity of the FSA's rules and the potential divergence of interpretations, discussions with the regulator could well have resulted in no further action. Finally, risk-tolerant firms were inclined to offer redress to the small minority of complainants who appealed for an FOS review while rejecting similar complaints of those who did not. As explained above, although in principle the FOS was inclined to report such firms if it perceived the complaints as indicative of a clear regulatory breach, in practice it was unlikely to do so. However, these firms faced the risk that they would be in a vulnerable position if their inconsistent behavior emerged in future FSA supervision. An FSA supervisor explained why the latter, third strategy, exposed firms to greater risk in comparison with the second:

> If I was a firm, I would be reluctant to accept that [an ombudsman's decision] would automatically apply to all my outstanding complaints [at the FOS], because I know that the FSA would think, "Ah, there's a systemic issue at this firm," and then I would come under even more regulatory scrutiny ... as a supervisor, you would ... think, "OK, now this firm, there's an admission of guilt, they've accepted that in a number of cases, well, we've got a systemic issue at the firm." ... I would say ... [as a firm] I'm incentivized ... to fight each case. There's little to gain from early acceptance (interviewee T1).

Media Involvement

The FOS was sensitive to firms' reputation concerns. Although it regularly published summaries of a selection of its decisions, these were anonymous and did not expose firms' corporate identity. The FOS further rejected demands from consumer groups to publish general comparative information regarding the volume of complaints and its upholding rate in relation to individual firms. More generally, the FOS was cautious against being perceived by the industry as making use of the media to encourage the already rapidly growing numbers of consumer complaints. An FOS executive explained that, as long as firms were small enough and therefore less likely to attract media's and consumer groups' proactive monitoring, the FOS was likely to enlist their cooperation to informal conciliation by adhering to confidential-dispute resolution:

> precedent for themselves [be]cause no-one will know about it. The whole environment is one of confidentiality, which we believe is the best environment to resolve complaints. It is a little bit like any forum of dispute resolution—it's always better behind closed doors (interviewee E2).

The FOS could have presumably threatened resistant firms, inasmuch as their cases displayed poor selling practices or mismanagement of complaints, that they would be named and shamed in the public domain. Given financial firms' particular sensitivity to adverse publicity, naming and shaming would have been a greater menace than reporting them to the FSA. Yet, the FOS was disinclined to employ naming and shaming as a means for inducing firms' cooperation. A possible explanation might be that naming and shaming firms could have damaged the ombudsman's rapport with the industry as a whole due to the likely adverse impact of such action upon the industry's already fragile public image. As demonstrated, the Treasury's review of the FOS' powers was prompted by industry's collective action following media coverage of the FOS' decisions regarding dual variable rate mortgages. Thus, damaging the industry's reputation put the ombudsman's powers and autonomy at risk.

Moreover, publicizing firms' mishandling of complaints or poor sales practices could have strained the FOS' relationship with the FSA, since it implicitly involved a public allegation of regulatory failure. Consequently, an executive explained that although the FOS could have employed naming and shaming in order to induce firms' cooperation, it perceived such strategy as too costly:

> We haven't [named and shamed firms] in the past and there are very strong reasons why we haven't ... it's something that we will do only after such consideration, because we do feel that there are so many negatives, that for us it's almost like a nuclear option ... we could [do it], but we would really have to be driven to it (interviewee E2).

The above analysis explicates the FOS' unconditional preference for confidentiality. Yet, financial firms nonetheless perceived the ombudsman's decisions as a threat to their public image. Although the FOS did not name and shame firms, it had no control over complainants' ability to independently draw media's or consumer groups' attention to favorable decisions on their behalf. Moreover, journalists often got involved with

earlier. Consequently, despite the FOS' reluctance to name and shame, firms were exposed to the risk that its decisions would be picked up by the media and result in damage to both their reputation and pressure that they offer similar compensation to all their relevant customers. Such media coverage probably put further pressure on the FSA, as a regulator, to account for its actions and omissions. Consequently, the FOS' strategic adherence to confidential-dispute resolution was not always sufficient for building a cooperative rapport with the industry and the FSA.

DISCUSSION AND CONCLUSION

The theoretical introduction to this article proposed that in order to process complaints and rectify consumer grievances at minimum costs for themselves, complaint handlers might seek firms' cooperation with informal conciliation. Building on regulatory enforcement literature, it was suggested that complaint handlers might encourage firms' cooperation with informal conciliation by selective adherence to individual and confidential resolution of complaints. It was further suggested that complaint handlers' and firms' additional goals to maximize support and minimize blame vis-à-vis other stakeholders and institutional overseers might lead them to adopt adversarial strategies. In light of these theoretical directions, the discussion below summarizes and seeks to explain FOS strategies and firms' responses to them. The implications of the findings for other third-party complaint handling institutions and for regulation more generally are further discussed.

As explicated above, to enlist firms' cooperation with informal conciliation, the FOS generally adhered to individual and confidential resolution of complaints. Complaint handlers were inclined to adopt this approach even when handling recurring widespread complaints. This strategy was ingrained in the FOS' organizational ethos and in its organizational structure, which granted broad discretion to individual adjudicators. It further resulted in the ombudsman's disinclination to unreservedly pass firm-specific information from complaints to the FSA or to publicize information from complaints, which could have exposed firms to the risk of regulatory enforcement and/or harmed their reputation. In addition, to induce the cooperation of resistant firms, the ombudsman selectively invoked its ability to report to the FSA's information from complaints regarding these firms' mishandling of complaints or poor selling practices. It should be emphasized that complaint handlers by no means suggested to

conciliating those complaints that reached the ombudsman, their initial mismanagement of complaints and/or apparent systemic failures in their sales practices were much less likely to be escalated within the FOS as problems that entail consideration of referral to the FSA. Likewise, firms (and complainants) were generally amenable to adjudicators' informal conciliation, and over 90% of the FOS' caseload was processed without recourse to formal decisions. Thus, the predominant equilibrium of the FOS' interaction with firms involved cooperative informal conciliation of complaints on the basis of individual- and confidential-dispute resolution.

However, complaint handlers' strategies cannot be understood without appreciation of their concerns and uncertainty regarding the expectations and likely actions of multiple external audiences, which resulted both in their adoption of adversarial strategies and in their leniency toward uncooperative firms. Thus, on the one hand, when handling new influxes of complaints of a systemic nature, complaint handlers were inclined to centralize and standardize their approach. Although such standardization intensified the FOS' conflicts with firms, it safeguarded it against allegations of bias and unpredictability in the event of judicial review or proactive monitoring by the media and consumer groups. It further protected individual complaint handlers by allowing them to justify their decisions by reference to a general organizational approach. On the other hand, due to their uncertainty regarding the FSA's likely response, complaint handlers were slow to act upon their threats to report uncooperative firms to the regulator. Moreover, the FOS was reluctant to name and shame uncooperative firms in the public domain. Complaint handlers perceived the impact of naming and shaming upon individual firms' cooperation with informal conciliation as inconsequential in comparison to the possible damage to the FOS. Exposing systemic failure in firms' management of complaints or sales practices impacted upon the public image of the financial industry as a whole, as well as upon the reputation of the FSA as its regulator. Consequently, if the FOS were to name and shame individual firms, it would have put itself at the risk of galvanizing collective industry action as well as damaging its relationship with the FSA.

Likewise, firms' concerns that their agreement to redress in one case might open them to criticism resulted both in their overcompliance as well as in adversarial reactions to FOS' decisions regarding new types of recurring complaints. Due to uncertainty regarding the FSA's expectations, and/or likely media exposure, the FOS could not provide firms with assurance that its decisions would have no implications for other complaints and

decisions to all similar complaints. Firms' uncertainty regarding the FSA's expectations and likely actions was rooted, at least in part, in the relative ambiguity of the FSA's regulations with regard to advice suitability and the implications of the ombudsman's decisions in particular. This uncertainty put the onus on firms to judge whether a decision by the FOS was likely to be interpreted by the FSA as indicative of a regulatory breach or simply as unfair in the specific circumstances of the case.

Thus, the above suggests that the FOS and firms alternated their strategies, oscillating between cooperative and adversarial equilibriums. When handling both one-off and familiar recurrent complaints regarding which the FSA's position was relatively clear and where media exposure was less probable, both firms and the FOS opted for cooperative individual and confidential informal conciliation. In contrast, with regard to new influxes of complaints, about which the FSA's position was still unclear and media coverage was intense, the FOS opted for precedent-based decision making, and firms were less inclined to accept informal conciliation. In such cases, the FOS was unable to assure firms that the scope of its decisions will be limited to the individual complaints due to its inability to control the interpretation and usage of its decisions by the FSA or the media. Risk-averse firms were consequently in a position where they had to choose between applying the ombudsman's decisions to all similar complaints and fighting each and every individual case. Thus, FOS' and firms' strategies were shaped in response to the external threats and demands associated with the handling of different types of complaints rather than in response to one another's strategies.

What general hypotheses might be drawn from the above analysis to the study of other third-party complaint handling schemes and to regulation more broadly? It is probable that in common with the FOS, other third-party complaint handling schemes aim to minimize the time and costs of caseload processing. Consequently, it is expected that they similarly engage in individual- and confidential-dispute resolution in pursuit of service providers' consent to low-cost informal conciliation. Moreover, insofar as complaint handlers and service providers in other domains face risks of external scrutiny, it is hypothesized that their strategies will similarly oscillate between cooperative informal conciliation and adversarial, formal, and standardized complaint handling.

More generally, this article contributes to a relatively small number of studies, which stress the importance of analyzing regulators' interactions

regulators' choices between cooperative and adversarial strategies are likely to alternate in response to the perceived opportunities for credit and blame that are involved in specific tasks and events. Thus, the same regulator and firm might choose cooperation in one instance and conflict in another not as a result of one another's strategies in a previous game but as a consequence of the perceived variance in the external circumstances surrounding their individual encounters. The analysis further suggests that the multiactor nature of regulatory games might lead regulators and firms to both over- and undercooperate with one another. On the one hand, to protect their reputation vis-à-vis the media and consumer groups, regulators may choose adversarial enforcement strategies toward cooperative firms, and firms may choose to overcooperate with vindictive regulators. On the other hand, regulators may choose leniency toward uncooperative firms due to their concerns that forceful enforcement may result in intervention by firms' political allies or in conflict with other institutional overseers. Similarly, firms might choose adversarial strategies toward cooperative regulators due to their uncertainty about the expectations and actions of other institutional overseers. Finally, the article shows that more attention should be devoted to the impact of regulators' and firms' uncertainty about the law itself in shaping their inclination to both over- and undercooperate with one another.

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1 In order to ensure anonymity, the dates and places of interviews are not disclosed since this information could render the identity of interviewees apparent to their colleagues at the FOS. Interviewees are represented by a letter (according to their role) and a number. *Executives* are assigned the letter E, *Ombudsmen* the letter O, *team managers* and their assistants the letter M, and members of the FOS *support* units the letter S. I have also interviewed a number of low-level adjudicators, but specific quotations from these interviews are not cited in this article.

2 There are no formal statistics regarding the overall number of complaints and the ratio of appeal to the FOS. The estimated figures rely on interviews and internal FOS research.

4 For analysis of the retail investment sector and its regulation, including the requirements of “advice suitability,” see Black (1997) and Clarke (1999). For the implications of these concepts for complaint handling, see Samuel (2005).

5 It is noteworthy that although such two-tier structure differed from the classic ombudsman model in which one person—the ombudsman—makes all decisions possibly with the aid of a cadre of assistants (e.g., Hill 2002), it was not unique to the FOS (see Seneviratne's [2002, 224–5] discussion of the British Local Government Ombudsman).

6 A single-premium bond is an investment wherein the policyholder pays a lump-sum premium at the outset of the policy term in expectation of returns at the end of the policy's term in line with the performance of the fund in which the money is invested.

7 Endowment mortgages were life assurance policies that became popular in the 1980s as a means for repaying house mortgage loans. As a result of lower than expected investment returns, most of these policies did not grow enough to allow policyholders to repay their mortgages. In 1999, the FSA's predecessor asserted that endowment mortgages were prima facie an unsuitable means for mortgage repayment. This resulted in a massive volume of consumer complaints and rapid increase in the FOS' caseload.

8 Precipice Bonds was a popular term attached to a variety of high-risk single-premium bonds.

9 The FOS' executives predicted that the increase in the volume of endowment mortgage complaints would be temporary and were therefore disinclined to fully match it with an expansion in staffing. Consequently, they had an interest to restrict the number of complaints of this kind that were reaching the FOS.

10 The FOS did not (and could not) inspect firms' handling of their own complaints. Hence, all that interviewees could assert was that in response to their threats, similar complaints did not reach the ombudsman. This may have been because the firms compensated all similar complaints or because they were inclined to redress those who threatened to take their complaint further to the FOS.

11 Firms' uncertainty was further related to the FSA's asserted shift to “principles-based regulation” and its “Treating Customers Fairly” initiative in particular, the discussion of which is beyond the scope of this article.

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