IRSG
INTERNATIONAL
REGULATORY
STRATEGY GROUP

INDEPENDENT REVIEW OF ADMINISTRATIVE LAW
Call for evidence

Does judicial review strike the right balance between enabling citizens to challenge the lawfulness of government action and allowing the executive and local authorities to carry on the business of government?

Submission of the International Regulatory Strategy Group in relation to the role played by judicial review in scrutinising the work of financial services regulators

1 Introduction

1.1 This submission:

This submission is made by the International Regulatory Strategy Group ("**IRSG**") in response to the call for evidence issued by the Independent Review of Administrative Law ("**IRAL**") panel.

1.2 Our experience and expertise:

The IRSG is a practitioner-led body comprising leading UK-based figures from the financial and related professional services industry. It is one of the leading cross-sectoral forums in Europe for our industry to discuss and act upon regulatory developments. We aim to engage proactively with governments, regulators and European/international institutions to promote an international regulatory framework that will facilitate open, competitive capital markets which enable the industry's customers and clients to have confidence in the products and services it is providing.

This response to the Call for Evidence is informed by the IRSG Architecture for regulating finance workstream, chaired by Julian Adams, M&G plc. The IRSG have previously published two reports on the UK's current regulatory framework, which can be found at https://www.irsg.co.uk/publications/the-architecture-for-regulating-finance-after-brexit-phase-ii and https://www.irsg.co.uk/publications/the-architecture-for-regulating-finance-after-brexit/.

We feel we can best use our expertise to assist the Call for Evidence by providing our collective view on the role that judicial review should play in ensuring appropriate financial market regulation and supervision. We have chosen to respond in general terms rather than addressing the specific questions in the Call for Evidence. We consider that judicial review is

an effective (and increasingly important) means of testing the legality of administrative decisions which should remain as accessible as possible to those affected by them. In the context of financial services, it plays a limited, but nonetheless important role in enabling firms to hold regulators to account. However, we consider that judicial review is both an unsuitable and incomplete means of ensuring full oversight of the work of organisations involved in regulating UK financial services activity (including the FCA, the PRA, the Bank of England, the Payment Systems Regulator and the Financial Ombudsman, together, the "**Financial Regulators**[1]"). It is unsuitable because, unlike other regulated sectors, the UK financial services regulatory regime places firms, the FCA and PRA in an ongoing relationship, the strength of which is likely to be damaged by engagement in adversarial litigation, and incomplete, because judicial review offers a binary remedy focused on illegality, irrationality or procedural impropriety, whereas comprehensive supervision of a regulator needs to encompass much more than this. For the financial services sector we would suggest instead that a statutory appeal and review regime, specifically tailored to the financial services sector, is a more appropriate and complete means of securing external scrutiny over the work of these regulators. We also recommend that a parliamentary committee with a mandate specifically focused on the regulators is established to ensure the broader range of financial regulatory activities are subject to meaningful scrutiny.

We would be pleased to discuss this response further with the IRAL if that would be helpful – [redacted]

2 The role of judicial review in scrutinising the work of Financial Regulators

2.1 The role of judicial review in preserving the rule of law and supporting growth

The existence of stable and predictable laws plays a key role in supporting economic growth. Business can only thrive where the law provides fairness and certainty, such that firms can plan their relationships with third parties based on clear and predictable expectations, rules and rights of redress. Judicial review plays an important role in facilitating challenges to the exercise of executive power (including that held by regulators), enabling businesses and individuals to hold those exercising public authority to account and helping to preserve the rule of law.

2.2 Judicial review as a source of accountability from Financial Regulators

The UK regulatory system for financial services is based on the delegation by Parliament of extensive powers to regulators. These powers are flexible and, when combined with the

[1] Whilst the majority of the Bank of England's regulatory powers are exercised by the PRA, the Bank itself exercises regulatory functions, including under Part 18 FSMA 2000 and Part 5 of the Banking Act 2009.

principle of regulatory independence, give Financial Regulators significant freedom of action. Given the extent and potential impact of the delegated powers Financial Regulators exercise, regulated firms and other interested parties must have mechanisms available to scrutinise and review the exercise of these powers to ensure that they are not misapplied[2]. At present, this occurs mostly through the use of judicial review and reports by the Financial Regulators to HM Treasury setting out how they have discharged their statutory objectives and requirements. Regulators must also operate complaints schemes, with the Financial Regulators Complaints Commissioner empowered to hear unsuccessful companies and make recommendations.[3]

We have argued (in our January 2020 publication "The architecture for regulating financial after Brexit: Phase II) that none of the mechanisms listed above currently provide an effective check on the full range of activity of the Financial Regulators[4]. Judicial review provides an important route for financial market participants to challenge the means by which a regulator has come to a decision, its adoption of rules or its interpretation or application of existing rules and law. However, as we will argue in the remainder of this response, it addresses only a very narrow subset of the activity of Financial Regulators and is unsuitable to be extended beyond this. There are also limits on its availability. In terms of government oversight, there is no obligation on HM Treasury to act on the reports they receive from Financial Regulators. The Financial Regulators Complaints Commissioner has no powers beyond making recommendations (and has been particularly critical of the FCA's handling of complaints).[5]

The purpose of our response to this Call for Evidence, therefore, is to set out why we believe that judicial review currently does not provide full and effective scrutiny of the work of Financial Regulators and that a statutory appeal and review regime, specifically tailored to the financial services sector, is a more appropriate and complete means of securing external scrutiny over the work of these regulators.

2.3 Limitations of judicial review as a means of securing accountability or scrutiny in the context of financial services

2.3.1 Ongoing relationship

Judicial review is an inappropriate tool with which to hold Financial Regulators to account as firms operating in the sector need to preserve an ongoing working

2 See further The architecture for regulating financial after Brexit: Phase II, para 2.3.1.

3 Ibid para 2.3.2. Note however that these complaints schemes are limited – they do not, for example, cover the exercise by the FCA and PRA of their legislative functions.

4 Ibid para 2.3.3

5 See further the Complaints Commissioner's 2019/20 Annual Report.

relationship with their regulator. This is perhaps the most significant barrier to the regular use of judicial review as a means of checking the exercise of regulatory power in this context. The need for authorised firms to maintain a positive relationship with the regulators responsible for their authorisation and ongoing supervision is a unique aspect of the financial services sector. Its importance cannot be overstated.

Unlike many other sectors, firms providing financial services have a close relationship with their regulators. The Financial Services and Markets Act obliges the FCA and PRA to ensure that regulated firms continue to act in accordance with relevant regulatory principles and rules. This requires a continual dialogue between firms and their relevant regulator[6]. Although the level of face-to-face communication varies depending on the size of the firm, all regulated firms are expected to engage with their regulator on an open and co-operative basis. Maintaining an effective ongoing relationship with the regulator is therefore essential if a firm is to continue to offer financial services. This militates significantly against entering an adversarial court dispute with that same regulator in which an allegation of an overreach of power or misinterpretation of the law must be made.

The role of the Financial Regulators in the authorisation and supervision of authorised firms places both sides in a relationship for as long as the organisation in question wishes to conduct authorised business in the UK. This deters firms from using judicial review, as most are unwilling to risk damaging their ongoing relationship with the regulators by pursuing a judicial challenge. This is evident if one compares the relatively low number of judicial review cases involving the financial regulators with the relative frequency with which firms in other sectors judicially review decisions by other regulators (for example, Ofcom, in the communications sector or Ofwat in the water sector).

Most forms of judicial review require parties to adopt an adversarial approach which necessarily nominates one side as the 'winner' and the other the 'loser', on the assumption that at the end of proceedings parties will have no future contact. Its binary nature excludes all notion of conciliation. The experience of our members is that judicial review applications are rarely settled ahead of litigation. Parties are unwilling to compromise in respect of what are often public law rights or propositions which will set a precedent for the industry. This is not a position that a firm wishing to

[6] The conduct of regulated firms is supervised by the FCA. Prudential supervision may be by the FCA or PRA. depending on the significance of the firm. Payment Services firms are also supervised by the PSR.

continue conducting financial services business in the UK is voluntarily going to adopt vis a vis the regulator whose authorisation is essential if it is to continue trading.

2.3.2 Procedural barriers

Even if a financial services firm wants to pursue judicial review of a Financial Regulator, the cost of doing so makes this a difficult remedy for smaller businesses to access. This is particularly the case following Treasury Solicitor Guidance[7] in 2010 which suggests that, in order to discharge the Duty of Candour, defendants must conduct an exercise that comes close to satisfying the requirements of standard disclosure in civil litigation – a time consuming and expensive exercise. The type of alternative appeal structure we outline below would be more accessible for small and medium-sized financial services firms than the existing judicial review procedure.

In addition, for those applications that make it through the permission stage, full argument may reduce important points of principle to relatively small, fact-specific points. These have limited broader application nor are they likely to improve, in more general terms, the efficacy of a Financial Regulator.

2.3.3 The use of expert evidence

Comprehensive scrutiny of the exercise of powers held by Financial Regulators requires a broader understanding of financial services law and the wider purpose of financial regulation. In civil litigation, where judges require additional information to determine a case, they will admit expert evidence. However, expert evidence is rarely admitted in judicial review cases as it is generally not reasonably required to enable a court to assess the merits of a decision. Where expert evidence is required (as it might be in some cases involving financial services) its deployment can be problematic. Oral evidence is unusual in judicial review cases, so expert evidence is not tested through cross examination. In addition, if a judicial review case concerns an issue on which it was reasonable for experts to have disagreed, as a general proposition an argument that a decision was irrational will fail. In cases concerning complex areas of law such as financial services, however, there will almost always be scope for even the most qualified experts to disagree, yet the decision may still have been ultra vires on the facts. Whilst this will not be an issue in every judicial review of a Financial Regulator, the approach to expert evidence demonstrates the limits of this remedy in a financial services context.

7 Treasury Solicitor Guidance on the Duty of Candour and Disclosure in Judicial Review Proceedings

2.3.4 The nature of the remedy

Judicial review is a specific, narrowly circumscribed remedy which focuses solely on the legality of a single point in time decision, in terms of either the procedure by which it was made, the outcome, or both. This makes it an unsuitable mechanism for ensuring the level of comprehensive scrutiny of all aspects of Financial Regulators' work required if investors and society are to have confidence in the financial regulatory system. Whilst it enables clear cases of the ultra vires exercise of regulatory powers to be challenged, relatively few regulatory decisions will be sufficiently flawed to fall within this category. There are many ways in which a regulator might be failing in its operations that fall short of illegality, irrationality or procedural impropriety, yet this is all the judicial review allows to be assessed. We expect more from our regulators than simply getting the law right and acting in accordance with it.

There is also an argument that the limited grounds for challenge as part of judicial review are difficult for a court to apply to much of the work of regulators, including the Financial Regulators. Illegality is difficult to apply to an organisation that makes and interprets many of its own rules. Similarly, procedural impropriety is difficult to judge when the Financial Regulators largely set their own processes. Irrationality is difficult for a court to apply as it is part of a regulator's role to judge what is relevant[8]. Judicial review of Financial Regulators is therefore arguably not the right mechanism for assessing whether they are acting in a fair and proportionate way.

In formulating regulatory policy, governments and regulators must balance a range of different interests and policy objectives. Financial stability must be considered alongside the protection of consumers, ensuring market stability, preserving and enhancing the attractiveness of the UK as a place to do business, and the lowering of barriers to entry to promote competition in the domestic market. These same interests will need to be considered and balanced when assessing how well a Financial Regulator is doing its job. Judicial review was not designed to secure this kind of balance and is ill-suited to doing so. It allows for only two competing viewpoints to be considered (the applicant's and defendant's) and demands that only one can triumph.

[8] See further the comments of Sir John Donaldson MR in *R v Panel on Take-overs and Mergers ex p. Guinness plc* [1991] 1 QB 146.

We consider that a different structure is required if we are to factor in broader regulatory or socio-economic concerns into the review of a regulator's actions (see further below).

In addition, an effective vehicle for scrutinising the work of Financial Regulators would also enable interested parties to challenge regulatory inaction, prompting positive change. For example, it is important that Financial Regulators keep their rules under review and that those which are no longer needed are removed or reformed. Whilst inaction can be challenged under judicial review if the decision not to act is irrational or unlawful, this sets the bar higher than is required for the effective scrutiny of Financial Regulators. Approaches to individual areas of financial services work or sectors may also need to be revised as markets develop. Judicial review does not provide any mechanism for triggering proactive steps like this – it is solely focused on decisions that have already been taken.

Proper oversight of the Financial Regulators also requires the ability to consider whether a wide variety of external and internal decisions and procedures are operating effectively and in line with the relevant regulator's objectives. Over-reliance on a mechanism that rests on the evaluation of one 'point in time' decision as a means of securing scrutiny and accountability of Financial Regulators (as judicial review does) risks over-extrapolation leading to inaccurate conclusions. The focus on a single decision judicial review precludes further systemic review of the operation of the organisation or the root cause of an issue. A more effective means of reviewing the full range of work of Financial Regulators would involve a procedure that produces a thorough, more inquisitorial examination of the functions of the organisation. This would allow for decisions to be reviewed in a holistic way and would, crucially, preserve the ongoing relationship between regulated firms and the Financial Regulators.

2.4 A new approach to scrutinising the Financial Regulators

Ensuring the sound operation of the Financial Regulators, for the benefit of all market participants, is a complex operation. It requires a system that can offer more than binary decisions on specific points provided following a judicial review hearing. It should be able to offer complex and often multifaceted solutions to improve the operation of modern financial services regulation.

Outside of financial services, the decisions of several economic regulators are reviewed and appealed according to bespoke statutory regimes and determined by specialist bodies,

including the Competition and Markets Authority and Competition Appeals Tribunal[9]. These regimes generally preserve the ability to challenge the decisions of a regulator on the same terms as judicial review (albeit before a specialist panel or tribunal). They may also go further than this, in some cases offering a full merits review of decisions. They offer the advantage of scrutiny by an expert body which understands both complex technical issues and the broader financial and economic context. As they are not limited to the narrow grounds permitted in judicial review, such bodies are better able to mitigate the risk of unfair or disproportionate decisions (against either a regulated firm or its competitors), the application of retroactivity to the interpretation of the rule book and regulatory capture (where the balance tips too far in favour of regulated firms and insufficient weight is given to consumer interests). The decision-makers' expertise would reduce the need for expert evidence and their more informal nature offers the ability to minimise procedural hurdles. Whilst they would not entirely remove the delicate issue of preserving financial services firms' ongoing relationships with the Financial Regulators, it is submitted that the offer of an alternative mechanism for challenge before specialists might provide a more appropriate forum for disputes.

2.5 Conclusion

Judicial review plays an important and significant role in holding those exercising executive power (including Financial Regulators) to account. It is vital that it remains open and accessible to any firm or member of the public with sufficient standing to bring a claim. Its utility in the context of financial services, however, is limited by firms' unwillingness to enter into an adversarial legal process against a regulator with whom they must have an ongoing (and vitally important) supervisory relationship. In addition, the grounds of review are narrow, focusing solely on the legality of decisions of the Financial Regulators. This makes judicial review an unsatisfactory means of comprehensively scrutinising the full spectrum of financial regulatory activity.

We do not, for the reasons listed above, consider that judicial review can or should be deemed an appropriate vehicle to facilitate the necessary broader scrutiny of the Financial Regulators. If the current framework for applying scrutiny and accountability to the actions of the Financial Regulators is to be improved, a bespoke, specialist body of the type we suggest above would offer a more positive and effective means of fully supervising the Financial Regulators.

[9] For example, decisions of the communications regulator Ofcom may be challenged before the Competition Appeal Tribunal and/or the High Court. Under the Financial Services (Banking Reform) Act 2013, certain decisions of the Payments Systems Regulator are appealable to the CMA.