THE LAW SOCIETY OF HONG KONG
香港律師會

# Consultation Paper on Financial Dispute Resolution Centre
# Submission of the Law Society

The Law Society supports in principle the establishment of the FDRC.

The Mediation Committee has reviewed the Consultation Paper in depth and has comments on the following matters:

- Would it be more appropriate to appoint an Ombudsman rather than establish the proposed dispute resolution by way of mediation and arbitration?
- The issue of quality control.

**Ombudsman or Arbitration?**

The Consultation Paper under paragraph 1.2 refers to a recommendation by the SFC to set up a Financial Ombudsman who '*has the power of ordering compensation*' and then discusses the Financial Ombudsman Services provided in the UK in paragraph 1.5. Although the Consultation Paper discusses the dispute resolution processes adopted by foreign jurisdictions, it does not address the key issue – is an Ombudsman a better option?

The Law Society notes the services provided by ombudsmen in other jurisdictions (paragraph 1.6), and expresses serious reservations that establishing an ombudsman to deal with financial disputes the appropriate way forward.

The Law Society considers the dispute resolution method comprising of the three tiers of 'negotiation - mediation – arbitration' to be the better option.

We fully support the inclusion of bilateral negotiation and mediation as the first and second tier of dispute resolution mechanism. The financial ombudsman services set up in the UK and Australia contain a mediation element.[1] Even if a claimant takes his case to the court, under Judiciary's Practice Direction 31, he will probably be encouraged to mediate first.

[1] See paragraphs 2.2, 7.1, 7.2, 7.5, 8.1 -8.9, Terms of Reference, Financial Ombudsman Services (Australia), January 2010; See also ss.228-232, Financial Services and Market Act 2000 (c.8) of UK.



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We have compared the powers and functions of an ombudsman and an arbitrator in an attempt to evaluate which is the better option:

**Ombudsman**

An Ombudsman is neither a consumer champion nor an industry trade body;

(a) he is independent and impartial.

(b) he may be a specialist or he may obtain expert advice where appropriate.

(c) when deciding on disputes and the remedies an Ombudsman is entitled to take into consideration the following:
- legal principles, industry codes and guidance, industry practice, and in some cases previous decisions.
- require parties to provide information he considers necessary; (non-compliance may lead to adverse consequences, including an intervention by the court)
- when making a determination, the ombudsman needs to provide in writing the conclusion, remedies, and the reason for his determination and cite the information relied on to reach the Determination. (By legislation, a Determination is a final decision and is binding upon the financial services provider if the Applicant accepts the Determination).

**Arbitration**

An arbitrator is an independent and impartial umpire who will decide on a dispute.

(a) The arbitral tribunal is required to act fairly and impartially as between the parties, giving them a reasonable opportunity to present their cases and to deal with the cases of their opponents.[2]

(b) It is not bound by rules of evidence and should use procedures appropriate to the particular case to avoid unnecessary delay.[3]

(c) When conducting arbitration proceedings, an arbitrator enjoys wide powers including but not limited to directing the discovery of documents or the delivery of interrogatories; taking initiative in ascertaining the facts and the law relevant to the proceedings and granting interim injunctions or directing other interim measures to be taken.[4]

(d) An award, order or direction made or given in relation to arbitration proceedings is enforceable in the same way as a judgment, order or direction of the Court. An arbitral award is final and binding upon all parties to the dispute.[5]

In terms of functions, we consider there is no difference between an arbitrator and an ombudsman as both are acting as an umpire to decide a dispute based on the parties' submissions. Their approaches to dispute resolution are very similar. *In terms of power, however, an arbitrator enjoys much wider power than an Ombudsman as stipulated in the respective legislation.* Unlike an Ombudsman's Determination, which is non-binding until the Applicant accepts it, an arbitral award is final and binding on all parties and it is an alternative to lengthy and costly litigation.

We note the Government will be introducing an Arbitration (Amendment) Bill to thoroughly update our legislation and so there would be no need to establish a

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[2] Section 2GA (1)(a), Arbitration Ordinance (Cap 341)

[3] Sections 2GA (1)(b) – (2), Arbitration Ordinance (Cap 341)

[4] Section2GB, Arbitration Ordinance (Cap 341)

[5] Section 2GG, Arbitration Ordinance (Cap 341)



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new legal framework for a financial ombudsman and as arbitration is a fee-charging service, the probability of abuse is reduced whilst those of a financial ombudsman are free and thus open to abuse and a drain on resources.

The Law Society also considers the creation of a financial ombudsman will cause confusion – too many regulatory bodies. We have the SFC and HKMA to deal with issues in relation to regulatory breach and their role is clearly distinguished from dispute resolution. The introduction of an ombudsman will blur the lines - an ombudsman will replicate the power of a regulator to investigate but at the same time will be charged with the function of dispute resolution. The task of resolving disputes will dilute the concept of an "Ombudsman" to order remedy based on its findings and the power to investigate, mainly to find fault, will jeopardise the neutral settlement process.

Based on these observations, **the Law Society takes the view the current proposal on FDRC is a better option than setting up a Financial Ombudsman.**

**Consultation Question 2**

*Do you support the idea of putting in place a dispute resolution scheme for financial services by way of mediation and arbitration?*

**Answer: The Law Society agrees but with the rider that, the public needs to be educated on the differences on the legal implications of a mediated settlement and the arbitral award, their effects and enforceability. We presume this will be one of the tasks of the Investor Education Council.**

**Quality Control**

**(a) Process Quality**

**Chapter 3** of the Consultation Paper discusses the dispute resolution procedure of the proposed FDRC; the proposal is to model it on the *Lehman Brothers-related Investment Products Mediation and Arbitration Scheme*. We note issues with the bankruptcy of Lehman Brothers is unique.

The Law Society has the following concerns on this model:

1. The Scheme deals primarily with a single line of products, namely "mini-bonds" entered into by the parties under largely similar circumstances and were 'one-off' in nature. The Scheme does not cater for other financial disputes which may involve multiple issues. As the Consultation Paper specifically excludes cases with systemic concerns from FDRC's jurisdiction, it follows the FDRC is unlikely to deal with repetitive disputes with a single issue similar to that of the mini-bonds.

2. The Consultation Paper fails to address the issue of "***power imbalance between the parties***". In cases where parties have huge differences in technical knowledge, financial resources and relevant information on the matter under dispute, a real concern is whether any negotiated settlement between an individual and a financial institution has been reached because of "coercion". In order for a mediation to succeed parties need to have sufficient information and advice, without which it will not be possible to make an informed decision on settlement. It is not the duty of the mediator



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to give advice and maintaining neutrality is of paramount importance if the mediator is to maintain the integrity of the process.

We note the commentary on arbitrations, and wish to point out that as some financial disputes involve the issue of credibility it would be necessary to conduct hearing and call for witnesses as 'paper arbitrations' will be inappropriate in such cases.

**Consultation Question 4**

*Do you have any views on the proposed process of the FDRC?*

**Answer: The Law Society takes the view that the FDRC dispute resolution process, if it is to succeed, should be flexible and should deal with disputes involving more than single-issue complaints. The proposals on the FDRC should be reconsidered and further consideration given to the following:**

- **increase the time allowed for intake and preparation so that risk factors can surface**
- **provide parties with the opportunity to seek information and advice in order to prepare for negotiations**
- **it should not be the sole responsibility of the intake officer to review the dispute**
- **appointed mediators should take a more active role and take control of the disputes at a much earlier stage in order to prepare the parties for the mediation. This allows rapport building between the mediator and the disputants and will speed up the mediation process**
- **mediators can also help prepare the mindset of parties to effectively take part in the mediation process**
- **create a Panel of lawyers to provide assistance to complainants in order to facilitate the mediation process**

**(b) Confidentiality**

The Law Society has grave concerns on the extent to which any data is disclosed as *confidentiality is an overriding principle of mediation.* If details such as settlement terms are disclosed, applicants may treat such cases as a precedent and will bargain according to the "benchmark" provided in the data. Should this occur it will breach one of the core values of mediation, namely *each case should be dealt with according to the specific needs of the parties.*

The financial market in Hong Kong is small and if the summary refers to the subject matter of the dispute, parties can be easily identified resulting in a breach of privilege and confidentiality and thus undermine the mediation process as a whole.

It should be noted that it is *not the duty of a mediator* to report regulatory breaches to SFC or HKMA. If this is expected of mediators in the new scheme it will seriously jeopardize the integrity of a mediator who would be placed into a conflict of interest position and thus undermine the mediation as parties would not disclose information which could otherwise facilitate settlement.



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**Consultation Question 9:**
*Do you agree that the FDRC should regularly disclose summary data in relation to the cases it has handled without naming the relevant parties?*

**Answer: The Law Society considers that data on the number of mediations conducted and the number of cases settled can be collected for statistical purposes when the FDRC reports to Legco.**

**(c) Quality of Mediators and Arbitrators**

A crucial aspect of quality control is the standard of mediators and arbitrators. As discussed earlier, the arbitrator will have to direct evidence and discovery and thus requires specialist knowledge. As a mediator, he may deal with a variety of people ranging from sophisticated investors to laypersons. As there are so many financial products and services it is important that the mediator should have a general understanding of the dealings between the parties which will assist with an efficient dispute resolution process. **The Law Society recommends that a training and assessment mechanism be established to ensure the quality of mediators and arbitrators and consistency of standards. This will help build public confidence in the mediation services and maintain the credibility of FDRC.**

**The Law Society of Hong Kong**
**Mediation Committee**
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**134228**



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