

# **Institute of financial ombudsman: european models of functioning and introduction in Ukraine**

**Anna O. Horbova, Admiral Makarov National University of Shipbuilding**

**Volodymyr Galagan, National University of Kyiv-Mohyla Academy**

**Iryna Basysta, Lviv State University of Internal Affairs**

**Olena Riabchynska, Classical Privat University**

**Ashot Hayrapetyan, Legal Education and Rehabilitation Programs  
Implementation Center**

## **Abstract**

The article is devoted to the study of the features of the financial ombudsman institution. The thoughts of various scholars on the definition of financial ombudsman were disclosed. It focuses attention on the fact that in the European Union, the effective functioning of the mechanism for out-of-court settlement of disputes between financial institutions and consumers of their services is ensured in compliance with either certain legislative acts or relevant documents of a recommendatory nature. The two models of the functioning of the institution of financial ombudsman were outlined and the features of each of them were considered. In the study of the German model of the institution of financial ombudsman, its main advantages were emphasized. The questions about the introduction of the institution of financial ombudsman in Ukraine on the path to European integration were considered. In particular, some provisions of the Ukrainian draft law “On the establishment of a financial ombudsman”, aimed at further legislative consolidation of the legal status of a financial ombudsman and the specifics of such activities, were also considered. The feasibility of introducing the institution of financial ombudsman in Ukraine as an effective mechanism for out-of-court settlement of disputes between financial institutions and clients was determined.

## **Keywords**

**Institution of Financial Ombudsman, Financial Ombudsman, Financial Disputes.**

## **Introduction**

The rapid development of the financial services market, which is characterized by the emergence of new financial products, an increase in the number of consumers and access to global markets, necessitates the creation of effective mechanisms to ensure consumer rights. The choice of certain financial services does not always bring the desired result to the consumer, due to the lack of awareness of the financial product,

the inability to assess and predict risks or financial obligations, as well as to compare the conditions offered by various financial service providers.

The modern condition of development of both national and international law is characterized by the emergence of new trends in optimizing human rights mechanisms aimed at ensuring a decent level of protection of human rights and freedoms in any country. Among the effective mechanisms of such protection, an important place is given to the institution of the Ombudsman. The emergence of the institution of financial ombudsman is caused by the need to create an independent body, called upon to carry out pre-trial settlement of disputes arising between financial institutions and their clients (consumers of financial services).

Today, on the path of entry into the European Union, the issue of organizing the institution of a financial ombudsman in Ukraine has received considerable attention. The negative impact of the economic and political crisis on the banking sector causes the emergence of a growing number of disputes between banking institutions and their clients regarding the fulfillment of credit agreements, deposit agreements, recognition of certain banking transactions as invalid, and the like. The escalation of relations between banks and customers is due to the use of hard methods for resolving a large number of disputes. Among the latter can be noted the use of collection services, artificial bankruptcy of the borrower, return of funds through the sale of movable and immovable collateral, and the like. Achieving effective resolution of a dispute between a financial institution and a client through its pre-trial settlement is possible with the help of the financial ombudsman. Therefore, it is relevant to study the implementation of this institution in Ukraine, taking into account the European experience of its functioning in countries with developed banking systems.

## Literature Review

Trynchuk et al. (2018), studying the role of the financial ombudsman in consumer protection issues, define him as a civil or state official entrusted with monitoring the strict observance of laws, equity and interests of consumers of financial (insurance) services. Scientists point out a common feature of the services of many ombudsmen in Europe, which is that the involvement of a lawyer or a public authority (for example, a court) in a case terminates the activities of the financial ombudsman to resolve a financial dispute between a financial institution and a consumer.

In turn, Kolesnikov & Bocharova (2015) note that the financial ombudsman (financial ombudsman, from Swedish ombudsman-representative of interests) is an independent person who out-of-court resolves disputes between financial service providers and their clients. At the same time, a significant part of the work of the financial ombudsman is devoted to the consideration of complaints related to issues of the banking sector, the securities market and insurance services.

According to the study of the team of authors Ali et al. (2016) of the issues of the financial ombudsman institution, it can be concluded that its activity consists in the independent resolution of the dispute between creditors and consumers. Scientist's

draw attention to the fact that prior to applying to the services of a financial ombudsman, an internal resolution of a dispute by contacting a consumer to a creditor with a complaint is a priority. According to the activities of the financial ombudsman, it will resolve a number of issues related to problem banking assets without going to judicial authorities, as well as affect the level of violations committed by officials of banking institutions, including corruption violations (Reznik et al., 2017).

## Methodology

The methodological basis for the study of the characteristics of the institution of financial ombudsman is a set of dialectical, comparative and legal and structural and functional methods. The dialectical method allowed studying the essence of the concept of financial ombudsman as an independent person in resolving disputes arising between financial institutions and their clients (consumers of financial services). The comparative legal method was used to determine the specifics of the regulatory framework of the institution of financial ombudsmen in developed countries and to consider some provisions of the Ukrainian draft law aimed at further legislative consolidation of the legal status of the financial ombudsman. With the help of the structural and functional method, the advantages of the German model of the institution of financial ombudsman were identified.

## Findings and Discussions

In the European Union, the effective functioning of the mechanism of out-of-court settlement of disputes between financial institutions and consumers of their services is ensured in compliance with either certain legislative acts or relevant documents of an advisory nature. Among the latter, an important place is taken by the Commission Recommendation 98/257/EC of March 30, 1998 on the principles applicable to the bodies responsible for out-of-court settlement of consumer disputes, developed by the European Commission. In particular, in order to improve the functioning of the ombudsman system responsible for handling disputes with consumers, the implementation of their activities should comply with the principles of independence, transparency, competition, efficiency, legality and freedom of representation (Commission Recommendation, 1998).

The world practice identifies two models of the functioning of the institution of financial ombudsman: German and British. Therefore, it is important to consider the features of each of them.

Thus, the emergence of the first out-of-court procedure for settling disputes between banks and customers with the participation of the financial ombudsman took place in 1992 in Germany on the initiative of the Association of German Public Banks. It should be noted that in Germany there is no specialized regulatory framework for regulating the activities of the financial ombudsman. Therefore, such activities are carried out in compliance with the regulations developed by the Association of German Public Banks (Bundesverband Öffentlicher Banken Deutschlands, VÖB). According to the data posted on the official website of the Association, from January 2016 the ombudsmen

of the public bank were headed by Herbert Wagner, the Chairman of the Supreme Regional Court Hamm. D., and from February 2017-Jürgen Maroun, the President of the High Regional Court of Frankfurt am Main. It is important to pay attention to the fact that the assistance of the financial ombudsman is possible only if the client wants to file a complaint to the bank that participates in the dispute resolution procedures in VÖB. The complaint can be sent to the association by mail, e-mail or fax. It should be noted that the official website of the Association contains a template of an application complaint. Copies of all documents required for consideration of the application must be attached to the complaint (VÖB-Ombudsmann: information from official website of the Association of German Public Banks).

The German model of the institution of financial ombudsman provides for his/her appointment by the Board of the Association of German Public Banks on the proposal of the Association's management. The term of office of the Ombudsman is three years, but reappointment is also allowed. An important requirement for a financial ombudsman is the prohibition to be an employee of any banking union or credit committee within three years prior to appointment. As for the issue of early dismissal of the Ombudsman, the decision on this is also taken by the Board of the Association. However, for this kind of dismissal, there must be valid reasons, in particular, if he/she can no longer make decisions independently, he/she is not able to fulfill his/her duties for a long time. The decision of the financial ombudsman in the case of the value of the complaint subject to no more than 5,000 euros is obligatory for the bank. If the amount of the claim is bigger than the specified amount, then such a decision is not binding on both the bank and the client. The deadline for sending a consent with the decision of the Ombudsman to the Complaints Processing Center is six weeks, which begins after it is received by the parties. Upon the expiration of this period, the Center verifies the status of settlement of the issue and informs the relevant parties about it, and this concludes the procedure of out-of-court settlement of the dispute between the financial institution and the client (Stechyshyn, 2015).

Thus, according to the German model, the activities of the financial ombudsman are related to alternative or extrajudicial settlement of disputes through a neutral third party, the result of which are: (1) making a binding decision for one or both parties; (2) making optional offers for both parties; (3) enabling the parties to make their own decisions (Regulation of Banks and Financial Markets in Europe-Glossary, 2019). It should be noted that the costs associated with the consideration of the complaint by the Ombudsman are covered by the Association. Thus, the German model of the financial ombudsman institution operates with advantages in terms of speed of decision making and the possibility of free settlement of a financial dispute.

In the UK, the institution of ombudsman provides for an independent public institution funded by public funds; that is the difference from the German model. A characteristic feature of the institution of financial ombudsman in this country is that it is created at the initiative of the state and carries out its activities in accordance with the requirements of the Financial Services Act (2012). For the opportunity to work with retail customers, UK banks are obliged to provide the latter with an opportunity to resolve disputes out of court.

It is important to emphasize that the right to use the services of the British financial ombudsman is given not only to individuals, but also to legal entities, in particular, organizations and charitable foundations, whose annual turnover is less than £ 1 million. Moreover, as for the limit amount of the binding decision of the financial ombudsman, it is £100,000. Given that the amount of claims for financial disputes between financial institutions and clients that are resolved with the participation of the financial ombudsman is significant, then out-of-court resolution of such disputes requires a long period and averages six months (Creutzfeldt, 2016).

It is also necessary to determine the nature of the decision of the financial ombudsman for the applicant and the person against whom the complaint was filed. Thus, for the applicant the decision of the financial ombudsman is not binding. In case of dissatisfaction with the decision, the applicant may notify the ombudsman and resort to the consideration of the disputed issue in another way. In turn, for the person against whom the complaint was filed, the decision of the financial ombudsman can be either mandatory or advisory, depending on the decision made by the applicant: agree or refuse to resolve the issue by the ombudsman (Kirkham, 2016).

In Ukraine, the initiation of the creation of a financial ombudsman institution was proposed in the Comprehensive Program for the Development of the Financial Sector of Ukraine until 2020, approved by a resolution of the Board of the National Bank of Ukraine dated June 18, 2015. One of the measures to increase the effectiveness of protecting the rights of consumers of financial services and investors is the creation of a financial ombudsman institution, whose function will be the alternative (out-of-court) resolution of disputes between financial institutions and their clients-individuals. At the same time, the Comprehensive Program also contains a requirement for the development of the Law of Ukraine “*On the institution of financial ombudsman*” (Board of the National Bank of Ukraine, 2015).

The draft law “*On the institution of financial ombudsman*” No. 8055 was registered in the Verkhovna Rada of Ukraine on February 22, 2018. According to the explanatory note to the draft law, the latter is called upon to introduce a mechanism for out-of-court settlement of disputes arising among consumers of financial services by their suppliers. In particular, there are also statistics on the implementation of the mechanism of out-of-court settlement of disputes in the EU countries, working in 24 of 28 states. Attention is drawn to the fact that the creation of an effective consumer protection regime is one of the key elements in building a developed financial market, the basis for increasing the volume of credit, the growth of the economy and the welfare of citizens (Verkhovna Rada of Ukraine, 2018).

The draft law No. 8055 provides the basic principles of the functioning of the financial ombudsman institution, among which are the principles of independence, fairness and impartiality, the principle of a single window for consumers to deal with financial issues, transparency and publicity, competence, speed and comfort for the consumer, proportionality and accessibility. An important attention should be paid to the principle of accessibility, which provides for the financing of the activities of a financial ombudsman institution through contributions from financial service providers and fees

for resolving a dispute (Verkhovna Rada of Ukraine, 2018). As can be seen in the listed principles, fixing them in the draft law fully takes into account the requirements of the Recommendation 98/257/EC.

## Recommendations

The feasibility of introducing the institution of financial ombudsman in Ukraine as an effective mechanism for out-of-court settlement of disputes between financial institutions and clients is to protect consumers of financial services, simplify the process of resolving financial disputes and minimize the costs of it, reduce the number of lengthy litigation and the like. Of the two studied models of the institution of financial ombudsman, the German model can be effective for Ukraine. This is explained by the fact that such a system is characterized by short-term settlement of out-of-court disputes between financial institutions and consumers of their services, as well as convenience for resolving disputes regarding insignificant amounts. Such out-of-court settlement of financial disputes is beneficial not only for financial institutions and their clients, but also for the entire judicial system.

## Conclusion

As a result of the study of the features of the existing models of the financial ombudsman institution, it should be noted that on the way to European integration, the introduction of such an institution in Ukraine is a pressing issue. Given the positive experience of European countries in developing standards of a civilized market, the functioning of the institution of financial ombudsman in Ukraine can help increase the level of consumer confidence in financial services in financial institutions. Therefore, for the Ukrainian financial (insurance) market, the adoption of the law of Ukraine “*On the institution of financial ombudsman*” remains relevant. A new independent and impartial institution of financial ombudsman can be an effective system in resolving disputes between financial institutions and their clients by peaceful means, which will relieve the work of the courts in handling such disputes.

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