

# Financial Services Consumer Panel

AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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Our ref: CP05/15\*\*\*

22 March 2006

Dear Bridget

## **Review of Compensation Scheme and Ombudsman Service Limits and Miscellaneous Amendments to the Compensation Sourcebook**

This is the Financial Services Consumer Panel's response to Consultation Paper 05/15\*\*\*, the Review of Compensation Scheme and Ombudsman Service limits and miscellaneous amendments to the Compensation Sourcebook. The Panel is grateful to have had the opportunity to participate in the FSA's preliminary discussions with stakeholders.

### **The Need for Limits**

We were pleased that the FSA agreed to our request to include in CP 05/15\*\*\* the option that there should be no limits imposed on payments by the Ombudsman and Compensation Schemes. This suggestion seems to have caused some surprise, but the reasons for this are straightforward.

So far as the Ombudsman Service is concerned, if a consumer loses out because of mis-selling then they should get everything back – without having to go to the Courts. The three Case Studies contained in the Consultation Paper, particularly Case Study A, demonstrate the consequences of having limits on awards.

Panel members are aware of individual cases where the £100,000 ceiling is already being used by firms to avoid their full responsibilities. Customers are told they must accept the £100,000 in full and final settlement, no matter how much more they lost, or the entire offer will be withdrawn, leaving them to sue, which of course they cannot afford to do as they have lost their savings through the original bad advice.

To sum up, if industry is confident that it can meet its obligations to consumers it has nothing to fear from unlimited Ombudsman awards.

As regards protection against the failure of a firm, consumers do not have access to information nor have the ability to make a judgement on financial soundness – that is the job of the FSA.

### **The Level of Limits**

Although we support the proposal that limits should be abandoned, we realise that this is unlikely to find support among other, non-consumer focused stakeholders. We have therefore gone on to consider at which level any limits should be set.

**Financial Ombudsman Service:** the limit on Ombudsman compensation of £100,000 was originally fixed in 1981 and was directly related to house prices at the time. The equivalent figure today would be many times that. In addition it is a matter of fact that inflation has eroded the real value of the limits over time. We do not see how there can be any argument against increasing limits substantially to offset this steady reduction in the real amount of compensation available to consumers today. For example, the Ombudsman limit of £100,000 should have almost tripled since 1981 just in order to keep pace with inflation.

**Financial Services Compensation Scheme:** as with the Ombudsman, inflation has significantly eroded the real value of compensation available. In addition we believe that the limit on compensation for deposits lost with failed firms should be increased still further. Increasing numbers of consumers, particularly older consumers, are moving out of equity based products into what are perceived as 'safer' deposit accounts. Consumers who sell their homes and wait before buying another are likely to have large sums of money on deposit with banks and building societies. The current maximum limit of £31,700 is far too low to accommodate these changes in consumer behaviour and the 10% reduction in cover of deposits between £2,001 and £33,000 should be removed. Similarly the overall investment compensation limit of £48,000 is too low, even when adjusted for inflation, bearing in mind current asset values and levels of individual investment.

The Panel recognises that there is a balance to be struck between the need to ensure that consumers are aware of the levels of compensation available to them and the need to build justified consumer confidence in the markets. We would not wish to see compensation levels used as a marketing tool and in any event we understand that comparison of levels of compensation available within different EU Member States is prohibited. Nevertheless the Panel believes that opportunities should be taken to include basic information about the level of compensation available from the Compensation Scheme in literature given to consumers engaging in financial services. For example, bank statements could include a single line of information about the limits on compensation available when a bank fails. This will help to prompt consumers to think about whether they should spread their money amongst a number of banks rather than keeping it in one place. Either consumers need to be clearly warned about deposits they have above the protected levels or the limit should be removed.

### **Compensation: Paying Less than the Full Claim**

The 90% limit for some Compensation Scheme payments should be removed. The rationale for imposing it, which hinges mainly on the need to discourage consumers

from doing business with firms in difficulty or that are otherwise 'risky', defies all logic. How can consumers possibly be expected to know whether the firm they are considering doing business with, perhaps buying house insurance, is not well capitalised, well run or has an unacceptable risk profile? Yet if the insuring company fails and the consumer makes a claim on the Compensation Scheme they are likely to suffer a significant financial loss.

### **Other Issues**

- When the Ombudsman finds in favour of a consumer, firms should be required to make payments swiftly and in full or face effective disciplinary action. In this respect we were pleased to see the Head of the FSA's Enforcement Division being quoted as saying that fines would be going up and firms' senior managers will be pursued more aggressively in future.
- In all cases we believe that changes to limits should apply to defaults declared and complaints made after the revision date.
- We agree that reviews should take place every three years. At that point limits should be increased to take account of inflation and consideration given to extending them still further.

Yours sincerely

A handwritten signature in black ink, appearing to be 'John Howard', written in a cursive style.

John Howard  
Chairman  
Financial Services Consumer Panel