Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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Dear Jenny

CP09/11* FSCS temporary high deposit balances and implementing changes to the Deposit Guarantee Schemes Directive**

This is the Financial Services Consumer Panel's response to the proposals in Chapter 2 of CP09/11*** that relate to Financial Services Compensation Scheme (FSCS) protection for temporary high balances. The Panel has already responded to Chapter 3 of the CP which deals with the implementation of changes to the Deposit Guarantee Schemes Directive.

We are pleased that the FSA has pressed ahead with this consultation now rather than waiting for the outcome of EU discussions. The current deposit protection limit is insufficient to protect individuals who are in receipt of a large sum of money which has to pass through the banking system before it is used or invested. The loss of these monies – such as out of court settlements and pension fund lump sums - would be devastating to the individuals involved. Recent market events have demonstrated that consumers cannot take the safety of their money for granted. Even those who understand the need to spread large sums amongst a number of accounts might struggle to identify banks who are separately authorised and where accounts would not be aggregated in the event of a failure.

We welcome many of the proposals in this paper, although as we have explained below we would like to see further categories of cash sums included and an extension of the proposed time limits.

Our responses to the detailed questions in the paper are set out below.

Q1: ***Do you agree that we should make rules to provide an enhanced level of protection, above the current £50,000 limit, to temporary high balances? Please explain the reasons behind your answer.***

Yes. Without enhanced protection for temporary high balances consumers would be exposed to a risk of significant detriment that they could not avoid or mitigate. Many consumers are involved in occasional financial transactions which must be cleared through the banking system, such as a property sale or redundancy payment, as outlined in the consultation paper. Financial losses in such cases are likely to be catastrophic for the individuals involved and there is in our view an unarguable case that protection must be provided. We see no alternative to the use of rules to provide such protection as there is no evidence of a workable market solution becoming available.

Q2: ***If your answer to Q1 is 'yes' do you agree that the extent of coverage of temporary high balances should be decided in accordance with the general principles set out in paragraph 2.9?***

We agree that the extent of the coverage should be guided by the principles set out in the paper, although we do not think that the list of temporary high balances set out in paragraph 2.10 goes far enough.

`Q3: ***Do you agree that FSCS protection should apply only to items on a defined list of specified types of temporary high balances? If you believe temporary high balances should be defined in some other way, please specify what you think this is.***

The Panel has considered whether the transactions could be better identified by way of the application of the principles alone, but on balance we believe that there should be a prescribed list. A principles-based approach could lead to confusion and uncertainty amongst banks/deposit-takers, as well as amongst consumers.

Q4: ***Do you agree that FSCS protection should be limited to temporary high balances, whether held in consumers' own accounts or in client accounts, arising in connection with:***

a) house sales relating to a consumer's primary residence and property bought for dependent relatives, for use as their primary residence;

b) pension lump sums;

c) inheritance;

d) divorce settlements;

e) redundancy payments;

f) proceeds of pure protection contracts (term, critical illness and income protection insurance, where there is no investment element); and

g) court awards and out-of-court settlements for personal injury?

If not, please give your reasons.

We agree that all temporary high balances arising in connection with the circumstances listed in question 4 should be covered by the extended protection provisions, whether they are held in consumers' own accounts or in client accounts, or by trustees. The list of payments should be subject to periodic review.

Q5: ***Do you believe any other types of payments should be added to the list of items covered? If so, please say what these are, and why.***

Yes. There are other types of payment which meet the criteria set out in the paper that are not listed above. These include:

- Life cover payments from pension lump sums
- Lump sum proceeds of Self Invested Personal Pension Plans held prior to disbursement/purchase of an annuity
- Proceeds of life policies which include an element of investment. We note the comments in the paper about the application of the limit on investment compensation in respect of these polices. However, the primary function of a life policy with an investment element can often be life cover, with the investment itself being an attractive but secondary feature of the policy. As such the proceeds of such polices otherwise seem to meet all the criteria set out in CP09/11*** and we see no logical reason why they should not be covered. The loss of the policy proceeds could be every bit as catastrophic as the loss of the proceeds of pure protection policies
- Proceeds of buildings insurance
- Payments awarded by employment tribunals.

Q6: ***Do you agree that FSCS protection for temporary high balances should generally be limited to a maximum of £500,000? If not, please give your reasons and say what limit(s) you think there should be instead.***

In our response to the earlier consultation CP08/15*** we sought a limit of £1mn with provision for routine review or uplift. Consequently we are disappointed that the proposed limit is only half that figure with no automatic process for review. To support the FSA's proposal it is stated in paragraph 2.15 of the paper that the £500,000 limit would cover 95.5% of house sales. However a £1mn limit would protect far more individuals – the proportion of houses in England and Wales selling for over £1mn was only 1% (footnote 9 to the consultation paper). There is no evidence in the paper that a limit of £1mn rather than £500,000 would place an unreasonable burden on fee payers and we would like the FSA to reconsider its proposed limit, or at least conduct further research to demonstrate the effectiveness of a £500,000 limit for consumers. We are still of the view that there should be an automatic review process – perhaps a form of index linking - to ensure that the figures involved keep pace with economic changes.

Q7: ***Do you agree that court awards and out-of-court settlements for personal injury should be covered for an unlimited amount, as an exception to the general rule?***

We fully support this proposal.

Q8: ***Do you agree that FSCS protection for temporary high balances should generally be limited to six months from the date at which the balance was***

paid? If not, please give your reasons and say what time limits you think should apply instead.

The general limit (please see also our response to question 10) should be twelve months. The proposed six month limit is not long enough to accommodate, for example, individuals who sell their home and move into rented accommodation while looking for another home. A twelve month limit would also help executors, administrators and trustees who are tracing beneficiaries/realising assets.

Q9: ***Do you think that there are any characteristics of particular types of temporary high balances which suggest that these should be covered for a shorter, or longer, period than six months? If so, please say what these characteristics are and say what time limits you think should apply instead.***

As we have said, the general limit should be twelve months, with the exception of court awards and out-of-court settlements (see question 10 below).

Q10: ***Do you agree that court awards and out-of-court settlements for personal injury should be covered for 18 months from the date at which the balance is paid, as an exception to the general rule?***

We would prefer a limit of two years for court awards and out-of-court settlements, where the recipients or their representatives may take some time to invest the monies or find appropriate accounts over which to spread the funds received.

Q11: ***Do you agree that inheritances should be covered from the date of death of the deceased person until six months after probate is granted, as an exception to the general rule?***

The limit, which we recommend should be twelve months rather than six, should run from the date of death.

Q12: ***Do you agree that the FSCS protection for temporary high balances held in client accounts should be identical to that for such balances held in consumers' own accounts? If not, please give your reasons.***

We agree. Any other approach would effectively be unfair to consumers who are represented by a professional adviser such as a solicitor.

Q13: ***Do you agree that inheritances should be covered for a maximum of £500,000 for each identified beneficiary, or £500,000 for the whole estate if the beneficiaries have yet to be identified, as an exception to the general rule?***

Inheritances should be covered per beneficiary, or for the whole estate pending identification of the beneficiaries.

Q14: ***Do you have any comments on the draft disclosure wording in paragraph 2.29?***

The draft disclosure wording is too long and is potentially confusing. It should be made shorter, simpler and the different levels of protection should be illustrated by examples.

Yours sincerely

Acting Chairman, Financial Services Consumer Panel