



**Financial Services Compensation Scheme: changes to the  
Compensation sourcebook (CP12/7)**

**A response paper by the Futures and Options Association**

**APRIL 2012**

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### **1. Introduction**

- 1.1 This response is submitted on behalf of the Futures and Options Association (“the FOA”), which is the principal European industry association for 160 firms and organisations engaged in the carrying on of business in futures, options and other derivatives. Its international membership includes banks, financial institutions, brokers, commodity trade houses, energy and power market participants, exchanges, clearing houses, IT providers, lawyers, accountants and consultants (see Appendix 1).
- 1.2 The FOA membership includes a number of regulated firms which carry on derivatives business for retail customers, particularly spread betting firms. It is in this particular context that the FOA makes this response to CP12/7.
- 1.3 In general terms, the FOA supports the overall objectives of the FSA to:
- (a) provide the Financial Services Compensation Scheme (FSCS) with greater flexibility in dealing with compensation claims;
  - (b) reduce the lead time for claimants receiving compensation; and
  - (c) ensure higher levels of efficiency and cost effectiveness in handling claims.
- 1.4 The FOA recognises that the points made below are not the subject of specific questions, but believes that they merit consideration in terms of reviewing the formula for setting the levy for contributing firms to the Scheme:
- The FOA would urge the FSA to give consideration to including a risk-weighting measure in assessing levies as regards the risk posed by particular classes of firms on the Scheme, i.e. presumably there is now sufficient accumulation of claims data and of the sources and types of business that give rise to those claims to make this assessment
  - While the FOA supports the self-assessment process by which firms determine their eligible annual income upon which levies are based, it is important that FSA monitors that process to ensure that the relevant criteria are applied on an even-handed basis
  - The level of cross-subsidy should be reviewed periodically to ensure that it is kept to a minimum (reflecting also the need for levies to be risk-weighted)
  - The FOA should review the level of transparency and accountability that applies to the FSCS and its assessments and actions.

## 2. Responses to Specific Questions

- Q1. *Do you agree (i) with our proposal to give the FSCS more flexibility in quantifying claims, and (ii) that we should not extend the change to defaults that occur before the rule change comes into effect?*
- 2.1 Yes. The FOA believes it is particularly important that the FSCS has the right to pursue recovery of compensation claims from defaulting firms.
- Q2. *Do you agree with our proposal to simplify eligibility criteria?*
- 2.2 Yes, in principle. However, those listed in para 2.16 of CP12/7 may bear some of the responsibility for a firm going into default. The FOA would urge the FSCS to assess very carefully the eligibility status of such claimants where they have been intimately involved in the default of the firm in question and triggered claims against the FSCS, i.e. eligibility should not be assumed to lead automatically to payment of compensation without extensive due diligence.
- Q3. *Do you agree with our proposal to remove the requirement for the FSCS to obtain an application form?*
- 2.3 Yes, but it is important that claimants make some effort to apply for compensation and that it does not just become an automated payment. One of the key objectives of the FCA will be to ensure that customers are better informed about the risk of loss accruing from their transactions and to take that into proper account when determining their investment strategy. Automating the payout of compensation will simply further the view that “If I lose money, someone must pay” and do little to advance the cause of risk awareness. However, where the FSCS already has sufficient information for the purposes of determining eligibility, a short-form application form could be utilised to reduce the burden of completion and analysis and avoid the provision of superfluous information.
- Q4. *Do you agree with our proposal for FSCS to have the option of taking an automatic assignment of rights?*
- 2.4 Yes.
- Q5. *Do you agree with our proposal regarding compensation for shortfalls in client money?*
- 2.5 Yes, but there is likely to be a mismatch between the priority need for fast turnaround of portability for client money/collateral to support the porting of transactions and the ability of the FSCS to make an equally timely payout of compensation for a shortfall to the firm assuming responsibility for those ported positions. Presumably, client money would not be transferred in this way in the event of a customer exercising the right to liquidate a position and seek direct return of the client money.
- Q6. *Do you agree with our proposal to remove duplication in relation to declarations of default?*
- 2.6 Yes.

Q7. *Do you agree with our proposal to enable the FSCS, in certain cases, to pay compensation without fully or at all investigating the eligibility of the claimant and/or the validity and/or amount of the claim?*

2.7 The FOA is concerned over this proposal, insofar as the issue of eligibility lies at the heart of the role of the FSCS in terms of compensation payments. It is equally a concern that such an automated approach without the requisite degree of due diligence would encourage spurious claims to be made, some of which might result in an unmerited compensation payment.

2.8 The FOA is equally concerned that, in para 2.30, emphasis is placed on the fact that this kind of approach would be adopted “where the claims are small”, yet in para 2.31 and in the draft rule 12.2.10, emphasis is placed on where the costs of investigation would be “disproportionate to the benefits”. In other words, this could be applied to large, complex claims, where the investigation cost would be high. This surely would not be appropriate.

Q8. *Do you agree with our proposal for the rule to apply to acts or omissions or defaults before it comes into effect?*

2.9 As a matter of principle, the FOA does not agree with changes that have retrospective effect. As a result, the FOA does not believe that the new rule should apply to claims arising out of firms’ acts or omissions before the rule change takes effect without, at least, quantifying its impact on the amounts levied on firms and a “cap” has been set in determining where a claim is “small”.

Q9. *Do you agree with our proposal to clarify the deposits that the FSCS can protect?*

2.10 Yes.

Q10. *Do you agree with the proposed clarification to the COMP 16 disclosures?*

2.11 Notwithstanding the fact that deposits fall outside the remit of the FOA, a prohibition on providing the FSCS telephone number would, in effect, mean that regulated firms would become the first point of information on the FSCS. The FOA believes that this is inappropriate. Further, against the background of the importance of consumers being made aware of the FSCS, firms should be entitled to disclose its telephone number.

The idea of embargoing the provision of a telephone number because customers are confused about the role of the FSCS seems extraordinary. If that is the case, surely they should be entitled to telephone the FSCS to gain a better understanding about its role! Equally, if customers are confused because there is a lack of clarity about the information that is provided to them, then the proper course is to review the information to ensure that it is not misleading – rather than preventing firms from disclosing the telephone number of the FSCS to customers!

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