Governance & Professionalism Policy
Financial Conduct Authority
12 Endeavour Square
London E20 1JN

FCA
Smaller Business
Practitioner Panel

8 March 2022

Dear Sir/Madam,

SBPP RESPONSE TO DP21/5: COMPENSATION FRAMEWORK REVIEW

It is the Panel's view that a review of the compensation framework is very much needed, and is, in fact, one of the most important pieces of work coming from the FCA as it impacts on all areas of the industry. It is a complex 'Pandora's Box' and we are aware that the different stakeholders have very different views. However, unless the framework is urgently addressed the financial services industry will continue to be fundamentally undermined, as the current system is not working. We welcome the explicit linkages in the discussion paper to the new consumer duty work, and the FCA's pensions, consumer engagement and consumer strategies as these are closely linked and will need to be considered together in order to achieve good consumer outcomes.

We agree with the principles of the review and welcome the FCA's emphasis that the FSCS is a 'fund of last resort'. The system is there to deal with the big issues but is currently fundamentally unfair – for example penalising those who have chosen never to advise on DB transfers or unregulated products. Our view is that a risk-based assessment of products would be a good start – if a firm sells a product, what liability would it have?

Coordination

We very much support the commitment to coordination across regulatory partners, including the consumer investment coordination group, and would welcome more information about how this will operate. The role of the Financial Ombudsman Service (FOS) in particular is key to the operation of the system, as well as the extent to which government is prepared to step in if other parts of the framework fail. We encourage the regulatory family to be bold with its solutions. For example, in the credit union sector, small credit unions fail, and a simple solution would be to make it easy for customers to transfer to another. However, the FSCS does not have the powers to do this. A change in the rules would be a simple solution here.

The firm failure process and the link with PII

There is a continuum of resources which come into play when a firm failure occurs. Initially a firm has its own capital. Beyond the firm's own capital, there is its PII insurance. We encourage the FCA to work with the PII insurers to ensure they have the best possible data and understanding of the market to ensure that the supply of cover is both appropriate and affordable. Then, and only then, should firm failure fall back on the FSCS, which has now grown beyond its original remit and requires unsustainable levels of funding. As the FCA and FSCS's own figures show, it is clear that a very small number of firms in this sector have caused the greatest number, and highest value, of claims. Given the crossover between all these different initiatives we would like to see how the FCA is linking together its work across the piece, taking into account where the market failures are occurring, with an overall objective of ensuring the market functions well in the event of firm failure

Scope and the FCA's perimeter

We believe that the system should cover regulated advice for regulated products. The majority of firm failures reaching the FSCS relate to unregulated products. We believe the FCA should make it clearer for investors who wish to take risks with unregulated products that they would not be protected. FSCS should not have a role when investors make a high-risk, unregulated investment and lose out.

Whistleblowing

It is true that some firms continue to give poor advice. However, more could be done to act more quickly on whistleblowing which would reduce harm and the pressure on the compensation scheme.

We encourage the FCA to engage with the industry as much as possible during this discussion period, encouraging individual firms, trade bodies and HM Treasury to become involved. We would be happy to be involved further.

Yours faithfully,

[Signed]

Marlene Shiels
Chair, FCA Smaller Business Practitioner Panel