

Increasing the award limit for the Financial Ombudsman Service

Policy Statement

PS19/8

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This relates to

Consultation Paper 18/31
which is available on our website at
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1 Summary

Introduction

- 1.1** In Consultation Paper (CP) 18/31, we proposed a new rule in the Dispute Resolution sourcebook (DISP) to increase the Financial Ombudsman Service's ('the ombudsman service') award limit from £150,000 to £350,000. This would apply to complaints referred to the service from 1 April 2019 about acts or omissions by firms from the same date.
- 1.2** For complaints referred to the service from 1 April about earlier acts or omissions, we proposed to increase the award limit to £160,000. We also proposed new rules to ensure both limits kept pace with inflation in future.
- 1.3** In this Policy Statement (PS) we summarise and respond to the feedback received in over 130 responses to CP 18/31. We have considered this feedback, and further developed our understanding of the potential impact on certain sectors, particularly the financial advice market. However, this has not changed our view. We are, therefore, implementing our proposals as consulted on.

Who this affects

- 1.4** This PS should be read by:
- all firms and other financial businesses covered by the ombudsman service's compulsory jurisdiction (CJ) and voluntary jurisdiction (VJ)
 - consumer groups
 - financial services and other industry representative bodies
 - professional indemnity insurance (PII) insurers and brokers
 - legal services providers
- 1.5** This PS will also be of interest to:
- people and businesses who can complain to the ombudsman service, such as individual consumers and micro-enterprises
 - the small and medium-sized enterprises, charities, trusts and personal guarantors who will be able to complain to the ombudsman service from 1 April 2019 (see PS18/21)

Background

- 1.6** The ombudsman service's award limit sets the maximum amount of financial compensation that the ombudsman service can require firms to pay when it upholds complaints against them. There is no limit on the amount the service can recommend and firms can choose to pay the difference.
- 1.7** CP 18/31, published in October 2018, was the first review of the ombudsman service's award limit since 2010, when we increased the original limit from £100,000 to £150,000. This increase, which came into force in 2012, was based on general price inflation to ensure consumer protection was maintained in real terms.
- 1.8** In CP 18/31, we said we considered the £150,000 award limit to be inadequate in light of the data on the number and value of 'high value complaints' handled by the ombudsman service.
- 1.9** We defined high value complaints as complaints where the service decided that fair compensation exceeded the award limit. We determined there could be around 2,000 such complaints each year. We estimated the shortfall in redress due to the award limit could be as high as £113 million each year. We calculated this as the difference between the amount of compensation the service could require firms to pay and what it determined was due.
- 1.10** Complaints above the current award limit typically involve insurance that protects consumers from a significant loss, advice on long-term investments that provide an income in retirement, or the investments themselves. They also include relatively large commercial loans where the affordability of repayments can have a significant impact on the viability of the business that borrowed the money.
- 1.11** Generally, the value of these products and services does not reflect the complainant's disposable income and whether they could afford to complain about the product in the courts. For example, a person's cash equivalent pension transfer value (CETV) should be seen in the context of their annual income for many years to come, rather than their disposable income. Even though the CETV can often be several hundred thousand pounds.
- 1.12** We therefore said it was unlikely that the less sophisticated financial services users eligible for the ombudsman service could afford to pursue firms through the courts for the full amount of compensation they are due.
- 1.13** Accordingly, for high value complaints, the misconduct that caused the complaint could have a serious impact on the complainant's life if they cannot obtain fair compensation from the ombudsman service because of the award limit, and cannot afford to go to court.

What we are changing

- 1.14** Following consideration of the feedback and further analysis of the potential consumer benefits and market impacts, we have made final rules fully implementing the proposals we consulted on.

- 1.15** Therefore, on 1 April 2019, the ombudsman service's £150,000 award limit will change to:
- £350,000 for complaints about acts or omissions by firms on or after 1 April 2019
 - £160,000 for complaints about acts or omissions by firms before 1 April 2019, and which are referred to the ombudsman service after that date
- 1.16** Additionally, from 1 April 2020 onwards, both award limits will be automatically adjusted on 1 April to ensure they keep pace with inflation, as measured by the Consumer Prices Index (CPI).
- 1.17** For any complaints referred to the ombudsman service before 1 April 2019 the limit will remain at £150,000.

How it links to our objectives

- 1.18** Our strategic objective is to ensure the relevant markets work well. To advance our strategic objective we have 3 operational objectives. Our new rules will advance our operational objectives in the following ways:
- secure an appropriate degree of protection for consumers by
 - ensuring more complaints against financial services firms receive fair compensation when the firm has not acted fairly and reasonably
 - strengthening firms' incentives to improve their conduct in instances that could lead to a complaint where fair compensation exceeds £150,000
 - enhance the integrity of the UK financial system by helping to build consumer trust through improved consumer protection and standards of conduct
 - promote effective competition in the interests of consumers, because:
 - firms that cause substantial financial harm to consumers will have to pay more redress because of poor conduct, meaning firms with better conduct may be able to outcompete them
 - consumers will know that all firms will be required to pay higher amounts of compensation in the event of a dispute, rather than this being at individual firms' discretion

Outcome we are seeking

- 1.19** Because of our changes, more complainants who are eligible for the ombudsman service will receive the full amount of compensation they are due when the service upholds their complaint. This includes individuals and small businesses, charities and trusts.
- 1.20** This will encourage firms to improve conduct – eg behaviour and product governance – in situations where compensation in the event of a complaint to the ombudsman service could exceed £150,000.

- 1.21** Ultimately, greater consumer protection levels and fairer financial services should improve trust in financial services and lead to greater participation in the market.

Measuring success

- 1.22** We will know our rules have been successful if:
- complainants who are due compensation between £150,000 and £350,000 receive all compensation due for complaints about a firm's act or omission after 1 April 2019
 - there are fewer unsuitable purchases, because firms are liable for a greater share of the costs of poor conduct and therefore improve their conduct, eg improved behaviour and product governance
 - effective competition in consumers' interests in financial advice markets is maintained

Summary of feedback and our response

- 1.23** We received 130 responses to CP 18/31. In Chapter 2 we set out in detail the feedback on our proposals and our response. The focus of feedback was, as expected, our proposal for a £350,000 award limit. Our proposal to ensure the award limits keep pace with inflation proved relatively uncontentious.
- 1.24** Most responses on the £350,000 limit proposals came from personal investment firms (PIFs), particularly small independent financial advisers (IFAs), and insurers providing professional indemnity insurance (PII) to these firms. These respondents did not support any increase to the ombudsman service's limit, mainly due to the potential impact on the PII market.
- 1.25** General insurers – the other main respondent group – tended to challenge us on whether such a large, single increase was necessary. They also questioned the ability of the ombudsman service to deal with more complex cases. There was qualified support from the banking sector for a £350,000 limit. Parliamentarians, and organisations representing consumers and non-financial small businesses advocated a higher limit than £350,000.
- 1.26** We provide a summary of the main points raised and our response below.

Our estimates of the volume and value of high-value complaints

- 1.27** We have addressed concerns about the accuracy of our high value complaint estimates in CP 18/31. We have worked with the ombudsman service to obtain more comprehensive data than we had when we developed our proposals. This includes data on complaints resolved 'informally' by case handlers, and we have adjusted our estimates of high value complaints in line with these. We have also reflected consultation feedback about legal claims that could switch to the ombudsman service under a higher limit.

- 1.28** Our analysis of this data has led us to revise our estimates of high value complaints significantly downwards – from around 2,000 to around 500 – compared to our original estimate in CP 18/31. We estimate that around three quarters of these 500 high value complaints will be covered by the £350,000 limit.
- 1.29** Because of there being fewer high value complaints, the value of liabilities above the current award limit (the 'redress shortfall' we referred to in CP 18/31) falls from the £113 million estimated in CP 18/31 to between £21.6 million and £47.6 million. We have included the lower end of the range because the redress of £47.6 million includes approximately £26 million worth of damages that may currently be awarded in legal actions and which may switch to the ombudsman service under the proposed award limit.
- 1.30** Between £11.3 million and £37.4 million of the above redress shortfall is potentially attributable to activities that would be currently underwritten by PII. We did not include a separate PII underwritten element in our original estimates. We have produced this estimate in response to consultation feedback that appeared to mistakenly assume the entire redress shortfall represented a liability for PII insurers.
- 1.31** Taking these revised estimates into account for our cost benefit analysis, we find that both the costs and the benefits of the policy are lower, with a reduction in net benefit from £36 million to between £11.8 million and £15.2 million.
- 1.32** As they result in significantly lower additional liabilities, we think the above revisions should help mitigate some of the concerns from PIFs and PII insurers about the impact of our original proposals on the cost and availability of PII.
- 1.33** To address these concerns further, shortly after our rules come into force, the ombudsman service will be publishing:
- information about additional governance arrangements that will apply to high value complaints
 - examples to help firms better understand how the service would determine whether it would be more appropriate for a complaint to be handled by the courts.

The Financial Ombudsman Service as an appropriate forum to resolve higher value complaints

- 1.34** We have considered respondents' concerns about whether the ombudsman service is an appropriate forum to resolve higher value complaints than those it currently considers.
- 1.35** Some of these respondents – generally those from the financial advice sector and their PII insurers – said only the courts should be able to deal with such complaints. Others expressed some concern the current capacity and capabilities of the ombudsman service to make decisions on these complaints.
- 1.36** As set out above, we are proceeding with our proposal for a £350,000 award limit. We consider that, under such a limit, the ombudsman service would still be able to meet its FSMA obligations to provide a scheme that resolves complaints quickly and with minimum formality by an independent person.

- 1.37** We explain in more detail in Chapter 2 why we do not think the courts can meet the needs of complainants who are eligible for the ombudsman service with high value complaints. Generally, this is because the court system is too expensive – even if upfront costs are removed by ‘no-win-no-fee’ charging arrangements – and too slow for these complainants.
- 1.38** We also consider that the service’s progress towards meeting the recommendations on complex complaints made by the recent independent review of the ombudsman service should help alleviate concerns about the service’s current and future capacity and capabilities.
- 1.39** We note respondents’ view that the ombudsman service’s ‘fair and reasonable’ standard creates significantly more uncertainty than if the service were to only apply the law. While many respondents made this point, none provided specific evidence of actual complaints, or types of complaints, where this had been the case.
- 1.40** Further, relevant consumer protection and regulatory law requires fair treatment of customers, so the law, in fact, requires a fairness standard. And, while the ombudsman service may depart from settled legal principles when deciding a complaint, it must make its reasons for doing so clear.
- 1.41** We received several requests for certain changes to the ombudsman service’s approach due to a higher award limit. Some requested an automatic right to an oral hearing for high value complaints. Others asked for additional guidance on how the service would decide whether a court would be better placed to deal with a particular dispute.
- 1.42** The DISP rules currently provide that an ombudsman will convene a hearing if it is necessary to fairly determine the complaint. However, as set out in paragraph 1.33, shortly after our new rules come into force, the ombudsman service will publish more information on additional governance arrangements for high value complaints. The service will also publish examples of where it has previously determined a court would be better placed to deal with a complaint.

Inflation-linked adjustments to the Financial Ombudsman Service’s award limit

- 1.43** We think the additional complexity due to multiple award limits that respondents said would be created by this proposal is manageable. It will also be time-limited as the diminishing ‘stock’ of pre-1 April 2019 acts or omissions reduces the number of potential complaints that the older limit would apply to. We also feel the additional complexity is proportionate to the benefits of ensuring the ombudsman service’s award limits keep pace with inflation.
- 1.44** We are therefore proceeding with our proposal for future, inflation-linked adjustments to the ombudsman service’s award limits for complaints about both pre- and post-1 April 2019 acts or omissions.
- 1.45** We are also proceeding with our proposal for a one-off increase to the £150,000 limit for complaints about pre-1 April 2019 acts or omissions that are referred to the ombudsman service after this date. We can now confirm that – as proposed in CP 18/31 – this increase will increase the limit for these complaints to £160,000 from 1 April 2019 onwards.

Impact of our award limit proposals on the professional indemnity insurance market

- 1.46** We accept respondents' views that there could be a material impact on the price and availability of PII cover for activities carried out by PIFs that are subject to the £350,000 award limit. For example, DB transfer advice provided after the in-force date of 1 April 2019. This could, in turn, have an impact on competition in relevant markets, such as by reducing choice or increasing prices for consumers.
- 1.47** We also note PII insurers' view that PII premiums will rise due to changes in the insurance market that have nothing to do with the ombudsman service's award limit. Feedback indicates PIFs who have already undertaken a significant number of DB transfers could face increases of up to 50%. Other PIFs and other retail intermediaries, such as general (non-investment) insurance intermediaries and mortgage brokers, could face increases of up to 25%.
- 1.48** We have focused particularly on how a £350,000 award limit affects the supply of defined benefit (DB) pension transfer advice. This is because:
- Consumers have a statutory right to transfer a DB pension, and there is a statutory requirement to take advice if they are transferring a cash equivalent transfer value of more than £30,000.
 - Concerns about the quality of DB transfer advice also appear to be a major factor in the positions insurers have taken in their feedback to us. These concerns are informed up by our supervisory work, which has found some firms may be giving unsuitable advice. However, these findings are based on targeted work and are not therefore representative of the market as a whole. Insurers indicated much higher potential premium increases for PIFs carrying out significant DB transfer advice business, compared to those who are not.
- 1.49** Although we do not expect it to materialise, we have modelled a 'worst-case' scenario, based on PII premium increases of between 200% and 500% forecasted by insurers. This contrasts with our own estimate of 140% based on our upper estimate of additional liabilities set out in paragraphs 1.27 to 1.31. Under this scenario, up to 1,000 'higher risk' PIFs could stop providing DB transfer advice under a £350,000 award limit because they would be unable to afford PII cover. We have no reason to believe these firms would also leave other areas of the advice market.
- 1.50** This would leave at least 1,500 'lower risk' PIFs still providing DB transfer advice. We think this is sufficient to meet demand, given the diminishing population of people with DB pensions and indications that DB transfer activity may have peaked. We believe this number of remaining firms would be sufficient to ensure competitive outcomes for consumers.
- 1.51** We would expect there to be an increase in the price of DB transfer advice if PII premiums significantly increased, or a significant number of firms stopped providing DB transfer advice. However, we think these increases will be relatively moderate and proportionate to the increase in consumer protection due to a higher award limit. We think that consumers will ultimately benefit if average quality rises across the market (as higher risk firms who can no longer obtain PII exit), even if prices also rise.
- 1.52** We stress that we do not think our worst-case scenario will materialise. As we explain in Chapter 2, this is because our scenario is based on targeted supervisory work and

is therefore not representative of the whole market. It is highly likely to significantly overstates the proportion of higher risk PIFs who may struggle to afford PII because of a £350,000 award limit. Additionally, higher risk firms may also have ways to offset the cost of significantly higher premiums and remain in the market.

- 1.53** We will continue to publish information about our view of markets that may have conduct issues and are therefore a concern for PII insurers. These should help insurers better understand the key risks in these markets, in addition to the information they collect from insureds themselves. Our recent policy work in the DB transfer area has provided greater detail on the steps advisers need to take to provide suitable advice.

Equality and diversity considerations

- 1.54** We do not consider that our rules adversely impact any of the groups with protected characteristics ie age, disability, sex, marriage or civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment.
- 1.55** Moreover, we believe there will be positive impacts for all consumers, including those with protected characteristics, because the ombudsman service is able to require firms to pay more compensation.

Next steps

- 1.56** If your firm is affected by these changes, you should ensure you meet the requirements by 1 April 2019.
- 1.57** We recognise that this is a reasonably short implementation period. However, we consulted on increasing the award limit on 1 April 2019 in CP 18/31, which was published in October 2018. This was so the change could come into force at the same time as the extension of the ombudsman service to larger SMEs, which we considered a logical approach. Firms should, therefore, already be planning for changes to the limit, with this PS serving as confirmation of what the change will be.
- 1.58** We advise firms to focus on the changes they will need to have in place on the day the new award limits come into force. These include:
- updating consumer-facing information about complaint handling procedures
 - ensuring they are using the most recent version of the ombudsman service's standard explanatory leaflet
 - ensuring complaint handling staff are aware of the increased limits

2 Feedback on our proposals and cost benefit analysis

- 2.1** This chapter summarises the feedback to the 19 questions we asked in our CP and sets out our response. We have structured this chapter using broad headings. This is due to the overlap between some of the questions, and because many responses made general comments rather than addressing specific questions. The headings may cover several questions, rather than dealing with each question in turn.
- 2.2** Most of the 130 responses we received were from financial services firms and financial services membership bodies, particularly personal investment firms (PIFs) and insurance companies providing professional indemnity insurance (PII) to PIFs. We give a list of the non-confidential respondents at Annex 1.

Our estimates of the volume and value of high value complaints

- Q1:** *Do you agree with our estimate of the volume of high value complaints, including the assumptions we have made? If not, are you able to provide any data to support your view?*
- Q2:** *Do you agree with our estimate of the value of high value complaints, including the assumptions we have made? If not, are you able to provide any data to support your view?*
- Q3:** *Do you agree with our assumptions about the volume and value of high value complaints that might be referred to the ombudsman service by newly-eligible SMEs? If not, are you able to provide any data to support your view?*
- Q4:** *Do you agree with us that, for the reasons given, the number of high value complaints that are not currently made to the ombudsman service because of the award limit is unlikely to be significant? If not, are you able to provide any data to support your view?*
- 2.3** In CP 18/31, we estimated that approximately 2,000 complaints upheld by the ombudsman service each year are 'high value complaints'. This means they result in recommendations by the service for compensation above £150,000. We based this on the average number of complaints resolved each year by the service between 2013/2014 and 2017/2018 (approximately 392,000 complaints) and the average uphold rate during that period (43%).
- 2.4** We then used data from the service on the value of compensation awarded in 'final decisions' to work out the number of upheld complaints where compensation exceeded £150,000 (ie complaints resolved by an ombudsman, rather than informally by case handlers).

- 2.5** For the substantial proportion of final decisions that have 'unknown' monetary compensation values we assumed these were distributed in the same way as final decisions with a specified value. These are cases where the decision specified the basis or formula for the calculation of compensation, rather than the actual amount. We took the same approach for complaints resolved informally by case handlers.
- 2.6** For complaints from the newly-eligible 'small businesses' we used the same estimate of between 5 and 50 high value complaints that we calculated for the cost benefit analysis (CBA) in CP18/3, which set out our proposals to extend access to the ombudsman service to these SMEs. This new category of small and medium-sized enterprises (SMEs) are due to become eligible complainants in April 2019.
- 2.7** High value complaints are recorded in the ombudsman service's data as simply 'over £150,000'. To work out the potential value distribution within this category, we used a sample of 40 high value complaints provided by the service. On this basis, we estimated that the 2,000 high value complaints represented a 'redress shortfall' of up to £113 million per year. This is the difference between the £150,000 firms must pay and the amount the service considers should be paid.

Feedback received

- 2.8** Several respondents suggested there were limitations to the data we used. They accepted our estimates because they did not have any data of their own to indicate that different volumes or assumptions would be more appropriate. Other respondents said they were concerned that we were proposing such a significant change to the ombudsman service's award limit based on such limited data.
- 2.9** Some respondents also said they disagreed with our assumption that the profile of complaints resolved by an ombudsman's decision was representative of those resolved by other case handlers. One membership body said that complainants are more likely to seek a referral to an ombudsman if the value is higher, so our figures may overstate the number of high value complaints. Another membership body echoed this, saying they would be concerned if less experienced staff were resolving the large number of high value claims implied by the data. Around 90% of all complaints to the ombudsman service are resolved informally by case handlers.
- 2.10** There were disagreements with our proposition that complainants with high value complaints will go to the ombudsman service whatever the award limit and would not go to court in the first instance. Some firms agreed that individuals who bring complaints themselves would probably do this.
- 2.11** However, some respondents noted that this may not be the case where complainants are represented by claims management companies (CMCs) or solicitors are involved. These third parties are more aware of the award limit and will tailor their approach accordingly.
- 2.12** Reflecting the above, one membership body said it was wrong to assume the ombudsman service would be the default option for high value disputes. This body said this was because of:
- the number of law firms operating 'no-win-no-fee' arrangements that made it possible to pursue these disputes through the courts was 'rapidly increasing'

- civil limitation periods that meant consumers who went to the ombudsman service first risked being time-barred if they needed to start a court claim following a decision from the service

2.13 We also received feedback from the PII industry about a potentially large number of claims, with an aggregate value of £70 million, that are currently being pursued through the courts. These claims would fall between the current £150,000 limit and the new £350,000 limit. Many of these claims are believed to relate to DB pension transfer advice and would be likely to switch to the ombudsman service under a higher award limit.

2.14 Other important comments on our estimates referenced:

- the risk of basing projections for future levels of high value complaints on current trends, with the growth in sales of high value self-invested personal pensions (SIPPs) highlighted as an important potential driver of high value complaints in future
- the need to account for the fact that many firms will pay the full recommended amount of compensation, rather than just the binding amount – this would mean our figure of a £113 million redress shortfall may be a significant overestimate
- the risk of using a sample of just 40 complaints to calculate the distribution of high value complaints
- the very large proportion of complaints where the value of monetary compensation awarded is 'unknown', given the fact that large numbers of complainants are being asked to accept – on a 'take it or leave it' basis – a decision without clear and certain information about the compensation they will receive (because the amount is left to the firm or a third party to calculate)
- a perception that the proposed increase to the award limit was, inappropriately, being driven by the needs of the newly-eligible SMEs

Our response

In CP 18/31, we recognised that our estimates of the volume and value of high value complaints were based on limited data and, therefore, involved making some assumptions.

Since publishing CP 18/31, we have worked with the ombudsman service to obtain more comprehensive data than we had when we developed our proposals. This includes data on complaints resolved 'informally' by case handlers, and we have adjusted our estimates of high value complaints in line with these. This has reduced the estimated number of high value complaints compared to our original estimate in CP 18/31.

More significantly, we have taken on board the ombudsman service's view that we should consider basing our revised estimates on complaint volumes which exclude payment protection insurance (PPI) complaints. This is because PPI complaints – which account for most complaints

currently referred to the service – will be subject to a time-bar in August and are, in any case, less likely to be high value complaints.

While we accept that using a sample of 40 complaints to calculate the distribution of complaints recorded as 'over £150,000' is imperfect, the ombudsman service has said it has no reason to believe that the sample it provided was unrepresentative.

Finally, we have also factored in feedback from the PII industry about legal claims that could switch to the ombudsman service under a higher limit.

Taking all the above into account, we have revised our estimates as follows:

- volume of upheld high value complaints down from approximately 2,000 complaints to approximately 500 complaints per year
- value of liabilities above the current award limit (the 'redress shortfall' we referred to in CP 18/31) down from £113 million to between £21.6 million and £47.6 million, depending on whether claims that might switch from the courts are included in our estimates
- value of liabilities that is potentially underwritten by PII of between £11.3 million and £37.4 million depending on whether claims that might switch from the courts are included in our estimates

We have used the updated estimates above to model the impact of PII premium increases on PIFs, which we discuss elsewhere in this PS. As we are now estimating significantly fewer high value complaints, the additional liabilities to which PII insurers might be exposed is also significantly reduced compared to our estimates in CP 18/31.

We accept some firms do voluntarily pay compensation above the award limit, but it is not guaranteed. From a consumer protection standpoint, it is prudent to make policy based on the 'worst-case' scenario where firms do not make voluntary payments.

Similarly, we have used the higher estimates of the additional liabilities that would be created to arrive at an upper estimate of the impact of our proposals. (£47.6 million, of which £37.4 million attributable to PII-underwritten activities). It is an upper estimate, because some of the redress awarded in the court cases included is likely to be underwritten by PII.

Regarding future complaint trends, and SIPP complaint trends particularly, we understand from the ombudsman service that the volume of such complaints did increase significantly in the last reporting period. However, most of these related to advice from PIFs to invest with a specific discretionary fund manager. We think it is too early to know if this is indicative of a wider trend.

We do not agree our proposals are solely being driven by the needs of newly-eligible, larger SMEs. As these complainants are not currently

eligible for the ombudsman service, we lack robust data on the value of their complaints. Because of this, and other uncertainties, we have committed to reviewing the impact of the SME extension within 2 years of our new eligibility criteria coming into force. This will include an assessment of the adequacy of the award limit.

It is true that, among the significant drivers of high value complaints, there are products and services that are likely to be provided to micro-enterprises, ie the smallest businesses who are currently eligible complainants. These include loans (mean compensation of £291,000) and interest rate hedging products (mean compensation of £373,000). We think it likely that this trend will continue for newly-eligible SMEs, who are more likely to be at the micro-enterprise end of the SME spectrum than much larger, ineligible enterprises

However, other significant drivers of high value complaints include investment products that are typically provided to individual consumers, such as SIPP's (mean compensation of £241,000) and portfolio management (mean compensation of £378,000). We, therefore, consider that a £350,000 award limit can be justified in terms of the needs of businesses and individual consumers were eligible for the ombudsman service before the extension to larger SMEs.

The Financial Ombudsman Service as an appropriate forum to resolve higher value complaints

Q5: *Do you agree with our proposal to increase the ombudsman service's award limit to £350,000 for complaints about acts or omissions by firms on or after 1 April 2019?*

2.15 In this section, we consider feedback on our proposal to allow the ombudsman service to make binding awards of up to £350,000 for complaints about acts or omissions by firms on or after 1 April 2019. The figure of £350,000 reflected 2 important considerations, specifically our view that the ombudsman service's award limit should:

- cover a substantial portion of the high value complaints currently referred to the service, where the present award limit could prevent complainants receiving the full amount of fair compensation
- ensure complaints about higher value products and services can be fairly compensated, at least where the product has typical or average values – these tend to be insurance products that protect people in the event of a very significant loss, or long-term investment products that people rely on for retirement income

2.16 We based our analysis in CP 18/31 on the volume and value of complaints currently received by the ombudsman service where compensation above the current award limit is awarded. We also used our estimates of the complaints that might be referred by newly-eligible SMEs.

2.17 To validate our analysis of the ombudsman service's data we used data from other reputable sources, including the Association of British Insurers' rebuilding cost database and house price indices. We used this to consider the compensation amounts that products and services typically associated with high value complaints could result in.

2.18 We have separated feedback on the £350,000 award limit from our consideration of feedback on the £160,000 award limit we proposed for all other complaints. It is also separated from the feedback future inflation-linked adjustments to all award limits operated by the ombudsman service. This can be found in the next section.

2.19 We have also provided a separate section on feedback that related specifically to the impact of the proposed £350,000 limit on the professional indemnity insurance (PII) market.

Feedback received

2.20 Overall, respondents did not disagree that eligible complainants could be involved in complaints that significantly exceed the current award limit. They felt therefore, that, in principle, there was a case for us seeking to ensure these complainants could be fairly compensated for misconduct by firms. However, this did not necessarily mean they thought that the ombudsman service was the right mechanism for this.

2.21 Responses to this proposal generally fell into one of 3 groups:

- respondents strongly opposed to the ombudsman service being able to mandate compensation of up to £350,000 because of the approach to dispute resolution stipulated in the Financial Services and Markets Act 2000 (FSMA)
- respondents less concerned about the fundamentals of the ombudsman service's approach and focused instead on more operational aspects, including whether the service is currently equipped to handle more complex, high value complaints
- respondents that supported the proposed £350,000 limit and, in some cases, considered it insufficient

2.22 The first group consisted mainly of individual PIFs and PII insurers. The other respondents in this group included some large general insurance firms, and trade bodies representing PIFs and other retail intermediaries. In summary, the key points raised by this group were:

- the 'fair and reasonable' basis for the ombudsman service's decisions means its decisions do not create precedent for subsequent complaints in the same way that legal claims do –it is claimed that this reduces certainty, assisting in preventing similar disputes arising in future
- the ombudsman service's process has a perceived lack of rigour, particularly due to the absence of cross-examination and disclosure of documents
- firms lack a statutory appeal process against a decision by the ombudsman service other than judicial review, which is limited in both availability and function
- the absence of a 15-year 'long-stop' rule to time-bar complaints to the ombudsman service (as applies to civil actions in the courts)

- 2.23** The second group included other insurance companies and respondents from the banking and lending sectors. Most of these stakeholders agreed there was a case for a substantial increase to the award limit.
- 2.24** Banks aside, respondents in the second group did not necessarily agree with the size of the increase we had proposed, at least not in the short term. Where these respondents suggested an alternative limit, this did not exceed £250,000. In summary, the key points raised by this group included:
- some expressions about a lack of confidence in the ombudsman service to handle complex complaints
 - a belief that there should be tangible evidence of the ombudsman service having implemented the key recommendations on complex complaints in Richard Lloyd's independent review before substantially increasing the award limit
 - the current operational model of the ombudsman service does not make a distinction for complex cases – the same procedure is followed irrespective of the value of the case and without a structured way of ensuring higher value cases are handled by the most experienced staff
 - a significantly higher award limit – and therefore the prospect of higher compensation pay-outs – is likely to increase CMC activity in areas where there are a significant proportion of high value complaints, such as DB transfer advice
 - with a higher award limit, the ombudsman service will need to make greater use of its discretion to recommend that a complaint be considered by another forum (eg mediation or the courts) where its complexity means that it is not suitable for the quicker form of justice the service provides
 - the proposed changes ran counter to the 'growing tide against regulating for the middle classes' at the expense of the disadvantaged and vulnerable
- 2.25** The third group included organisations and parliamentarians responding on behalf of consumers and SMEs. These respondents supported the proposed £350,000 limit, but some argued we should go further:

- a membership body representing small businesses said the limit should be at least £500,000 to ensure the needs of such businesses would be met
- the All Party Parliamentary Group on Fair Business Banking said that, in principle, the amount of compensation the ombudsman service can award should not be limited, but if a limit was necessary then it should be no lower than £600,000.

Our response

Following careful consideration of feedback, we are proceeding with our proposal for a £350,000 award limit for complaints referred to the ombudsman service on or after 1 April 2019 and which relate to acts or omissions on or after that date.

We consider a limit of £350,000 appropriate because:

- It would ensure complainants receive the full amount of compensation the ombudsman service believes due in a clear majority (around 75%) of the 500 complaints we now estimate would be upheld the service each year where compensation exceeds the current award limit. This could equate to around £47.6 million in compensation, which may not currently be paid because of the current award limit.
- It is broadly consistent with the average amount of compensation awarded for products that feature most commonly in the 'over £150,000' compensation category. These include self-invested personal pensions (SIPPs), where mean compensation of £241,000 was awarded for complaints where compensation exceeded £150,000, portfolio management (£378,000), commercial loans (£291,000), and interest rate hedging products (£373,000).
- It is broadly consistent with our alternative assessment (ie using data sources other than the ombudsman service's) of the value of awards that higher value products and services could give rise to.

The damages threshold at which an out-of-court dispute resolution scheme, such as the ombudsman service, should have an appeals mechanism with judicial oversight is open to debate. However, a £350,000 limit is significantly below the roughly £600,000 (A\$1 million) limit recently implemented – in line with the recommendations of an extensive independent review – by the Australian Treasury for the new Australian Financial Complaints Authority (AFCA). Like the ombudsman service, AFCA has no external appeal process for financial services firms on the merits of a dispute. Australia is a relevant comparator in that, like the UK, it has a common law legal system.

We recognise that a significant number of respondents believe that only the courts should be able to award compensation between £150,000 and £350,000. Other respondents said they lacked confidence in the ombudsman service's ability to handle such disputes. We set out our view on these objections below.

We provide detailed comments on these concerns below. However, we are satisfied that, under a £350,000 award limit, the ombudsman service would still be able to meet its FSMA obligations to provide a scheme that resolves complaints quickly and with minimum formality by an independent person.

Characteristics of financial services disputes involving eligible complainants

Compared to the individual consumers and small businesses they serve, financial services firms tend to have greater knowledge and information about the often-complex products they sell. They also have access to greater resources to protect their interests in the event of a dispute. Such resources may come from within the firm, or because the firm holds PII.

Additionally, financial services disputes typically arise because the customer believes the actions of the firm have lost them money. For example, due to a firm's unsuitable investment advice or its refusal to pay an insurance claim. If the amount at stake is large, the customer's ability to withstand this loss while the dispute is resolved is likely to be limited. For financially distressed business customers, a long wait could mean the chance of commercial recovery is lost and businesses become insolvent.

It is, therefore, essential that financial services dispute resolution mechanisms reflect the key characteristics of financial services disputes. In our view, this means they need to provide quick, low-cost access to justice.

The drawbacks of the court system

Some respondents feel strongly that complaints where compensation could exceed the current award limit should be subject to the 'highly forensic processes' of the courts, with full guarantees of due process rights.

However, such a process would be very costly, given the need for all parties to be legally represented to ensure a fair hearing. Some respondents felt that 'no-win-no-fee' arrangements enable consumers and businesses to obtain legal representation at no upfront cost. However, this tends to defer, not reduce, the high cost of litigation. Those who win a case in court would still face a significant, potentially unaffordable reduction in the compensation they receive.

Under so-called conditional fee arrangements (CFAs), success fees payable by the client can be up to 100% of the solicitor's normal fees. Under so-called damages based agreements (DBAs), the client may have to pay up to half of the sum recovered from the losing party.

Under CFAs and DBAs, all other disbursements (eg court fees, expert fees etc) are payable regardless of the success of the claim. These costs can be significant. For example, the court fee alone for starting a claim of over £10,000 is 5% and fees are only capped (at £10,000) once the value of the claim goes over £200,000.

The courts also take a long time to resolve individual disputes, particularly if decisions are appealed. As noted by the recently published Review into the complaints and alternative dispute resolution (ADR) landscape for the UK's SME market, the average time between issue of claim and hearing in the small claims track of the court system is currently 33 weeks, and between issue and trial in the fast and multi tracks 57 weeks.

By comparison, the ombudsman service's data show the service resolved almost three quarters of non-PPI complaints within three months during the last reporting period, although this fell to just over half for complex complaint areas, such as investment and pensions complaints. Since 2015/2016, the service has resolved over 95% of non-PPI complaints within 12 months.

Concerns about 'fair and reasonable' as a basis for resolving disputes

The basis of the ombudsman service's decisions is subjective. FSMA requires the service to 'determine complaints by reference to what is, in the opinion of the [individual] ombudsman, fair and reasonable in all the circumstances of the case'.

However, we do not agree that this should create significantly more uncertainty than if the service were to only apply the law. While many respondents made this point, none provided specific evidence of actual complaints, or types of complaints, where this had been the case. We also note that:

- When we, or the ombudsman service, have asked for such evidence in the past, such as during our engagement with the industry on the Financial Advice Market Review (FAMR), it has not been provided.
- In February 2017, the Administrative Court concluded (in *R (Aviva Life & Pensions (UK) Ltd) v Financial Ombudsman Service*) that the ombudsman service can depart from settled legal principles, or make a finding clearly different to what the outcome would be in law. It must, however, make its reasoning for the overall decision sufficiently clear for the parties to understand why.
- Relevant consumer protection and regulatory law requires fair treatment of customers, so the law, in fact, requires a fairness standard.

In themselves, the ombudsman service's data on uphold rates do not suggest a 'fairness bias' in favour of complainants. In 2017/2018, the service upheld 34% of complaints overall. In complaint areas that respondents particularly focused on – investment and pensions complaints and complaints about IFAs – the uphold rate is lower, at 28% and 33% respectively.

We accept that the ombudsman service does not create legal precedent – it cannot do this because it is not a court. However, we do not agree with the view that firms and PII insurers are unable to anticipate the service's decisions with a reasonable degree of certainty.

Compliance with rules and guidance in DISP should help firms understand how the service is likely to respond to different complaints. Firms are required to take 'all relevant factors' into account when resolving complaints (DISP 1.4.1R), which may include guidance published by the service (such as illustrative case studies in Ombudsman News) and previous decisions on similar complaints received by the firm.

In high risk areas, such as DB transfer advice, we have carried out significant outreach work with firms on our expectations, and have involved the ombudsman service at every stage of this work.

Concerns about the capability and capacity of the Financial Ombudsman Service

Some respondents expressed concern about the capability and capacity of the ombudsman service to make decisions on complex, higher value complaints.

The ombudsman service was independently reviewed in 2018. Overall, the independent reviewer concluded that the service 'provides an effective and essential service for many thousands of people'. The independent reviewer did identify some areas where the ombudsman service could improve to ensure that it can retain public confidence.

The independent reviewer made several recommendations. These included to:

- identify gaps between existing capabilities and what is needed for the future, including in relation to case-handling, developing casework approaches, knowledge support, training and quality assurance
- plan for continuous improvement to ensure that the quality of casework, including complex cases, is sufficiently robust and consistent
- carry out an assessment of the effectiveness of quality assurance, the scope for improved data collection and analysis, and identify how the quality assurance function could be improved
- ensure a continuing role for assurance checks by experienced and knowledgeable staff at arm's length from the primary decision-making teams, focused on the greatest risks

The ombudsman service has taken these recommendations forward and reported on progress in its recent plan and budget consultation. The FCA Board has also been monitoring the ombudsman service's progress towards meeting the review's recommendations through the regular oversight progress.

Our assessment of this progress was a key factor in our decision to confirm extension of the service's jurisdiction to larger SMEs, and has been equally important in considering whether the service's award limit should be significantly increased.

Changes to the ombudsman service's approach

Consultation feedback included changes that could help improve stakeholder confidence in the ombudsman service's approach, beyond those being implemented by the service in response to the independent review.

Oral hearings

Some stakeholders called for an automatic right to an oral hearing in cases where a higher value award might be made. We understand the concern about how a higher award limit might be applied, and a desire to ensure that there is consistency and fairness.

The ombudsman service is an informal alternative dispute resolution mechanism. Cross examination under oath is generally unnecessary and contrary to the minimum formality which FSMA stipulates. The rules currently allow for an oral hearing. If an ombudsman concludes a hearing is not needed for procedural fairness, then the ombudsman will make a judgement without one. In deciding whether to hold a hearing, the ombudsman will consider the European Convention on Human Rights.

An automatic right to an oral hearing, as desired by some stakeholders, would require a rule change and formal consultation. The ombudsman service has told us that, if a higher award limit were agreed, it would be preferable to introduce additional governance arrangements for high value complaints. This would include senior oversight, to ensure that higher awards were applied with appropriate checks and balances.

Shortly after our rules come into force, the ombudsman service will publish information about these additional governance arrangements.

Guidance on when it would be more appropriate for the courts to handle a complaint

In response to respondents' request for further guidance, the ombudsman service will also be publishing examples of instances where it has decided that it would be more appropriate for a complaint to be handled by the courts.

Claims management companies

Many CMCs help to secure redress for customers, including those who might otherwise not have made a claim. Our Financial Lives survey indicates that 67% of customers who used a CMC over the last 3 years to make a financial services claim, wouldn't have done so without a CMC.

CMCs can also act as an effective check and balance against poor practice by firms. Through our regulation of the sector, we want CMCs to be trusted providers of high quality, good value services.

Inflation-linked adjustments to the Financial Ombudsman Service's award limit

- Q6:** *Do you agree with our proposal to automatically adjust, in line with general price inflation, the ombudsman service's award limit for complaints about acts or omissions on or after 1 April 2019 every year from 2020 onwards?*
- Q7:** *Do you agree that the measure of general price inflation used to automatically adjust the ombudsman service's award limit for complaints about acts or omissions on or after 1 April 2019 should be the CPI?*

Q8: *Do you agree with our proposal for a one-off adjustment, reflecting general price inflation between 2015 and 2019, to the ombudsman service's award for complaints about acts or omissions by firms before 1 April 2019?*

Q9: *Do you agree with our proposal to automatically adjust every year from 2020 onwards, in line with general price inflation, the ombudsman service's award limit for complaints about acts or omissions before 1 April 2019? 26 CP18/31 Annex 1*

Q10: *Do you agree that the measure of general price inflation used for both the proposed one-off and automatic adjustments to the ombudsman service's award limit for complaints about acts or omissions on or after 1 April 2019 should be the CPI?*

2.26 In this section, we consider our proposal to automatically adjust the ombudsman service's award limits for complaints about pre- and post-1 April 2019 acts or omissions in line with CPI inflation. Automatic adjustment would ensure these award limits broadly retain their value in real terms in future without the need for further consultation. These adjustments would take effect from 1 April 2020 onwards.

2.27 We also consider our proposal for a one-off, inflation-based adjustment to the award limit for complaints about pre-1 April 2019 acts or omissions (currently £150,000). This is to compensate for the real terms decline in the value of the limit since around 2015.

Feedback received

2.28 A few respondents consider the current £150,000 award limit excessive. However, most agreed with the principle of inflation-linked adjustments in future, and considered the CPI to be an appropriate basis for this. Obviously, respondents who did not support the proposal for a £350,000 limit, also did not support applying future inflation-linked adjustments to that limit.

2.29 Some respondents who supported the principle of inflation-linked future adjustments expressed reservations about the practicalities, including:

- additional complexity and confusion for firms and consumers due to the ombudsman service having multiple award limits
- the potential for disputes about when an act or omission occurred
- the proposed frequency of increases, with biennial reviews seen as achieving a better balance between ensuring the award limit retains its value in real terms and keeping the number of award limits that could potentially apply to a complaint to a minimum
- rising overheads due to the need to regularly update terms and conditions and consumer-facing information, which could disproportionately impact smaller firms
- how adjustments to the award limit would be communicated to stakeholders

- what our approach would be in the event of the CPI figure being negative (ie deflation)
- that the proposal to round down the inflation-adjusted limit to the nearest £5,000 could negate any prospective increase

2.30 There was also a reasonable level of support for the one-off increase to the current £150,000 award limit. Those who disagreed tended to refer to the presumption that legislation (including FCA rules) should not be applied retrospectively.

Our response

We are proceeding with our proposal for future inflation-linked adjustments to the ombudsman service's award limits for complaints about both pre- and post-1 April 2019 acts or omissions.

We are also proceeding with our proposal for a one-off increase to the £150,000 limit for complaints about pre-1 April 2019 acts or omissions that are referred to the ombudsman service after this date. Following publication of [the CPI for January 2019](#), we can now confirm that – as proposed in CP 18/31 – this will increase the £150,000 limit to £160,000.

We accept that the ombudsman service having multiple award limits is likely to cause some confusion, which is not ideal. However, we were clear in CP 18/31 that it is not a reasonable use of our powers under FSMA to apply an above inflation increase to complaints about firms' acts or omissions that occurred in the past. As such, bringing in a £350,000 award limit for complaints about future events makes it necessary to have a separate award limit for complaints about past events.

We do not agree the one-off increase to the current £150,000 award limit on 1 April is at odds with the presumption against retrospective application of legislation. This is because it will simply ensure that the £150,000 award limit is increased to what £150,000 is worth today (ie we have not changed the value of the award limit in real terms).

We recognise there may be also scope for confusion as the £160,000 and £350,000 limits increase with inflation in future. To mitigate this, we have constructed our rules so that, from 1 April 2019 onwards, complainants and firms will only need to consider 2 things. These are: when the act or omission occurred (ie before or on/after 1 April 2019); and the award limit relevant to that act or omission date that was current in our rules at the time the complaint was referred to the ombudsman service.

We will publish a table on our website so firms, complainants and organisations representing businesses and consumers can see which limit applies at any time. From 2020 onwards, this table will be updated at the beginning of March each year. Firms may choose to refer to this table in consumer-facing information as a way of managing their overheads.

We accept that multiple limits could increase the likelihood of disputes about when an act or omission took place. This is particularly the case if the time in question is around when the £350,000 limit was introduced, given what might be at stake in terms of what the ombudsman service can require firms to pay.

However, we think such disputes are an acceptable price to pay so the service can award higher amounts of compensation, and that the amounts it can award are maintained in real terms. We note the service already considers this factor when it decides whether a complaint is time-barred, so it is not a new issue. Finally, we note that the complexity will be time-limited as the diminishing 'stock' of pre-1 April 2019 acts or omissions reduces the number of potential complaints that the older limit would apply to.

Finally, it is true that the effect of rounding inflation-linked changes down to the nearest £5,000 could negate any prospective increase in some years. However, as inflation generally increases over time and the reference date for our adjustments is fixed at January 2019, it is likely that any such effects will be corrected in subsequent years.

Although we could, as one respondent suggested, round down to a lower interval (such as the nearest £1,000), this is likely to result in very precise values that may be difficult for firms and consumers to recall.

Impact of our award limit proposals on the professional indemnity insurance market

Q12: *Do you agree with our assessment of the impact of our award limit proposals on the professional indemnity insurance market?*

Q13: *Do you have any analysis or evidence to present in relation to how the costs of professional indemnity insurance (PII) might change if the ombudsman service's award limit is raised to £350,000?*

- 2.31** To trade, PIFs are required to maintain PII which provides an adequate level of cover and meets minimum levels of indemnity (between €1.5m and €2.6m depending on the firm's activities). As most PIFs are small, being able to obtain affordable PII cover is critical. PII insurers are, obviously, under no obligation to provide their product.
- 2.32** PIFs are also required to hold regulatory capital (£20,000 or 5% of annual investment business income) to absorb losses and to meet claims against them. This includes awards made by the ombudsman service.
- 2.33** Where PIFs have exclusions or an excess greater than £5,000 in their PII policies our rules in the Interim Prudential sourcebook for Investment Business (IPRU-INV) require them to hold additional capital. The amount of capital firms must hold depends on their income.

2.34 We said in CP 18/31 that it was possible PII premiums would rise as the amount of compensation the ombudsman service can require firms to pay rises. We recognised that this could be particularly challenging for small PIFs, as PII premiums are a higher proportion of their total income. We noted the risk of such firms withdrawing from certain parts of the advice market, such as defined benefit (DB) pension transfers, if they were no longer able to get affordable PII. This could weaken competition in those parts of the market.

2.35 Overall, we estimated an increase in PII costs of £77 million. This figure is net of the total compensation of £113 million that we estimated would be paid to complainants under a £350,000 award limit. However, we said £77 million is likely to be an overestimate. This is because not all claims will be insured or fully insured, as we do not require PII cover for all regulated activities.

Feedback received

2.36 We received a substantial amount of feedback from PII insurers and brokers and retail intermediaries – predominantly PIFs – on the specific questions we asked about the impact of our proposals on PII.

2.37 Insurers told us that PII premiums will rise even without any change to the ombudsman service's limit. Feedback indicates PIFs who have undertaken a significant number of DB transfers could face increases of up to 50%. Other PIFs and other retail intermediaries, such as general (non-investment) insurance intermediaries and mortgage brokers, could face increases of up to 25%.

2.38 These increases are likely to reflect the hardening PII market (see below). In the case of PIFs with significant DB transfers on their books, insurers appear to have growing concerns about the number of potentially unsuitable DB transfers that may have already taken place (which would not be subject to the £350,000 limit).

2.39 Our decision in November 2018 to ban PII policies which contain exclusions for the insolvency of the policyholder or any third-party claim against the policy is also likely to be a factor in these planned rises. It will be some time until we can judge the actual impact as the rule is not yet in force.

2.40 Based on the consultation responses received and other stakeholder engagement, we believe the following represents a fair summary of the general position of PII insurers:

- The PII market has been hardening for some time. Non-US PII is the second-least profitable class at the Lloyd's of London insurance market. 62% of Lloyd's syndicates writing non-US PII have made an aggregate loss over the last 6 years, and several have left the market. PII for PIFs is also a relatively concentrated market: according to one insurer, there are over 60 PII insurers, but fewer than 10 provide cover for PIFs.
- As capacity contracts due to worsening macroeconomic conditions, insurers are likely to reduce their exposure regardless of our proposals. One broker told us in December that several insurers had already reached their premium capacity for 2018-19, and capacity was likely to reduce in 2019/2020.
- A £350,000 award limit would materially increase their exposure to complaints about DB transfer advice because:

- there is evidence of lower proportions of suitable advice for DB transfers compared to the wider market for pensions advice, such as accumulation advice and retirement income advice
 - the volume of DB transfers has increased sharply since 2016 – the first full year following the 'pension freedom' reforms, when there were around 60,000 transfers – and currently stands at around 100,000 per year
 - transfer values are high, at an average of £400,000
 - based on the ombudsman service's data, the average compensation award for an upheld high value complaint about a self-invested personal pension (SIPP) is around £240,000, with a range of between £155k and £400k – this is a common investment vehicle for a DB transfer and therefore a reasonable proxy for a DB transfer advice complaint
- Insurers' concerns about their exposure to DB transfer advice complaints are compounded by 2 wider factors, which, they say, make it difficult for them to plan the outcome of their involvement in the PIF segment with a reasonable degree of certainty:
 - firstly, they see the ombudsman service's 'fair and reasonable' standard as a source of significant uncertainty compared to the courts (a view that we do not agree with – see above)
 - secondly, the ombudsman service being a 'risk-free' option for complainants, increases complaint volatility, due to the activities of claims management companies in encouraging consumers to raise complaints when they otherwise may not have

2.41 Some insurers consider the current £150,000 award limit too high. However, the general view is that the ombudsman service's relatively restricted award limit allows insurers to balance the factors set out above with the certainty they need to participate in the PIF segment.

2.42 A significant increase in the ombudsman service's award limit, insurers say, would threaten that balance. A membership body representing PII insurers told us that the proposed increase to the award limit would make an 'already unattractive' class of business 'even less attractive'. They felt it would cause an already limited PII market to shrink further.

2.43 Some individual insurers conceded that changes to the ombudsman service's approach could address concerns about the perceived inconsistency of the service's approach. These were the introduction of an automatic right to an oral hearing for higher-value complaints, and the provision of further guidance on how the service would decide if the courts were better placed to deal with a complaint.

2.44 When presented with the prospect of a £350,000 award limit, insurers clearly indicated that, if they were going to remain in the market, significant premium increases were likely.

2.45 The insurers who provided feedback indicated increases of between 200% and 500% for PIFs carrying out DB transfer advice. This would be likely to make PII for this type of business unaffordable for many PIFs and would cause them to leave the market for this kind of business after the date such an award limit came into force. Insurers told us they would do this by continuing to underwrite business subject to the previous limit,

but would apply exclusions or (for PIFs who could afford higher premiums) differential premiums to business taking place after the increase.

Our response

The consultation feedback has improved our understanding of the potential impact of our proposals on the PII market compared to when we published our proposals.

This feedback has led us to focus particularly on the impact of possible changes in the PII market on the supply of DB transfer advice. This is because consumers have a statutory right to transfer a DB pension, and there is a statutory requirement that they take advice if they are transferring more than £30,000.

However, if PIFs cannot obtain PII cover then we do not consider that they would be providing DB transfer advice in a way that protects consumers' interests. We explain this point in the discussion of policy exclusions, below.

Concerns about the quality of DB transfer advice also appear to be a major factor in the positions insurers have taken. For example, insurers indicated much higher potential premium increases for PIFs carrying out significant DB transfer advice business, compared to those who are not.

In summary, we think that under a 'worst-case' scenario, involving modelling estimates of PII premium increases provided by insurers, up to 1,000 'higher risk' PIFs could stop providing DB transfer advice under a £350,000 award limit. This would be because they would be unable to afford PII cover. We do not believe these firms would also exit other areas of the advice market.

This would leave at least 1,500 PIFs still providing DB transfer advice. We feel this is sufficient to meet demand, particularly given the following factors:

- the diminishing population of people with DB pensions
- indications that DB transfer activity may have peaked, although could remain at current levels (approximately 150,000 people seeking advice each year) for a few years
- growing awareness of our starting assumption for advice, which is that most people are better to stay in their DB pension over the long term
- availability of tools, such as the Money and Pension Service's Retirement Adviser Directory and similar commercial initiatives, that help consumers locate firms providing DB pension transfer advice in person and by phone or online

We also think this number of firms should be sufficient to encourage competition. Any price increases for consumers due to higher PII premiums are likely to be moderate and proportionate to the increase in consumer protection due to a higher award limit.

However, we stress that we do not think our worst-case scenario will materialise. This is because, as we explain below, we have made assumptions using data from targeted supervisory work that is very likely to significantly overstate the proportion of higher risk firms in the market as a whole who may struggle to obtain PII because of a £350,000 award limit. Firms may also have ways to offset the cost of significantly higher premiums and remain in the market.

We explain how we have arrived at the above conclusion below. We do not respond to feedback about the ombudsman service's approach to dispute resolution as we cover this issue elsewhere in this PS.

Our competition duty and Government recommendations about economic policy

Under FSMA, we are required to advance our competition objective meaning that we must promote effective competition in the interests of consumers. In addition, to this objective, we also have a competition duty. Our competition duty states that we must discharge our general functions in a way which promotes effective competition in the interests of consumers, so far as is compatible with acting in a way which advances our:

- consumer protection objective ('securing an appropriate degree of protection for consumers', or
- integrity objective ('protecting and enhancing the integrity of the UK financial system')

As a matter of policy, we normally choose the most pro-competitive measure open to us if it is compatible with our duties as a whole. Our competition duty means that competition is an integral part of our thinking.

The Treasury has recommended that, when we consider how to advance our objectives, we should, where relevant and practical, take account of a number of aspects of the Government's economic policy. Competitiveness is one of these aspects and in particular, the Government's objective that 'better outcomes for all consumers [should be secured] through improved competition in the interests of consumers'.

Accordingly, a potential concern for us is that a £350,000 award limit would increase the cost of PII and cause too many PIFs to stop providing DB transfer advice to sustain effective competition in that part of the advice market. In the first instance, this could mean the supply of advice does not meet consumer demand. This would have serious implications given the competition-related duties outlined above.

It might also give the remaining firms enough market power to cause consumer harm. This could include charging consumers an inflated price, providing a poor quality product or service, or both. However, as we discuss elsewhere in this section, we consider that, even under our worst-case scenario, the number of firms potentially remaining in this part of the advice market currently appears sufficient to prevent this happening to a significant extent.

Risk profile of personal investment firms

To assess this risk, we have considered what proportion of firms currently providing DB transfer advice might be considered relatively low risk or relatively high risk by PII insurers. This has helped us understand the proportion of firms that may or may not be able to get affordable PII cover if a higher award limit increased insurers' exposure to the costs of providing redress for unsuitable advice.

The previous phases of our supervisory work have resulted in 4 out of 13 firms up to October 2017 (31% of firms assessed) and 4 out of 18 firms stopping providing DB transfer advice in our work between October 2017 and December 2018 (22%).

The 31 firms we looked at in these phases were considered higher risk to begin with. So, generalising from the sample of 31 firms we looked at to the approximately 2,500 firms currently providing DB transfer advice is highly likely to significantly overstate the number of firms that insurers might consider higher risk in the event of a much higher award limit. However, post-pension freedoms DB transfer advice is a relatively new part of the advice market, so we do not currently have better data on the suitability of advice across the market.

Given the uncertainties, we think it appropriate to construct a likely worst-case scenario for modelling the impact of the potential premium increases resulting from a £350,000 award limit. We have therefore based our analysis on 40% of firms in the DB transfer advice market being high risk.

Modelling the impact of premium increases

We modelled the impact of premium increases of 139% (rounded to 140%), 200% and 500% using data from the Retail Mediation Activities Return (RMAR). This is the core regulatory data return submitted by firms who provide intermediary services, such as investment advice. It includes data on PII premiums, revenue and profitability.

The 140% increase is based on our revised estimates of additional PII-underwritten liabilities of up to £37.4 million that would be created if the limit increased to £350,000. This is an upper-bound estimate, because it assumes £26 million of redress currently awarded in court cases, some of which will already be underwritten by PII. These liabilities result in an additional annualised PII premium of £69.7 million and net PII-related costs of £32.3 million (ie net of £37.4 million redress reimbursed by insurers).

The increases of 200% and 500% reflect the range of insurer-provided estimates of premium increases for PIFs undertaking significant DB transfer advice business. We have not been able to reconcile such increases with our estimates of additional liabilities. We assume they reflect factors that are not accounted for in our model (because they are not due to the increased award limit), such as challenging wider market conditions or the apparent lower profitability of this class of PII.

Table 1 shows the impact of these increases on PIFs with 2-5 advisers, which is the most common size of firm according to RMAR data. Importantly, the model assumes no pass-through of higher PII costs to consumer prices. As we discuss below, this may not be the case in practice.

Table 1: Estimated impact of different premium increases on 2-5 adviser personal investment firms

PII premium increase	Median premium before	Median premium after	Median retained profit margin before	Median retained profit margin after (assumes no pass-through of higher PII costs to consumers)	Difference in profit margin	Change in profit margin
140%	£3,400	£8,000	10.3%	7.9%	-2.4 percentage points (pp)	-23.2%
200%	£3,400	£10,100	10.3%	6.9%	-3.4pp	-33.1%
500%	£3,400	£20,100	10.3%	2.1%	-8.3pp	-80.0%

Our model also assumes the same premium increase will apply to all firms. This is also unlikely in practice because we assume insurers will price their premiums according to the risk profiles of the individual firm.

To account for this, we have assumed – in line with the need to consider a worst-case scenario – that the 40% of PIFs (approximately 1,000 firms) which are higher risk attract the maximum premium increase cited by insurers of 500%, and the 60% which are lower risk attract the lower rate of 200%.

As shown in Table 1, under this scenario, there is likely to be an adverse impact on higher risk PIFs who incur a notional 500% premium increase in our model. Many such firms may not be able to afford PII for future DB transfer business without taking significant measures to offset the implied reduction in retained profit margin.

In our view, consolidating with other PIFs to improve profitability through economies of scale (including in procurement of PII) could be one option for higher risk PIFs. Another option may be to reduce dividend payments. Pass-through of PII costs to consumers may also be an option. However, this may mean higher risk PIFs incurring large premium increases may not be able to compete on price with lower risk PIFs who incur smaller increases.

Firms without the above options are likely to have to stop providing DB transfer advice. We would be concerned about an approach where firms continue to carry on significant higher risk business, such as DB transfer advice, by holding additional capital in place of PII. As we discuss below, we think this 'alternative' strategy is not a viable way to remain in the market, as it is unlikely to promote outcomes that are in consumers' interests.

According to our model, a notional 200% premium increase would have a material impact on lower risk PIFs. In practice, such firms will probably be able to offset this impact by passing some additional PII costs through to consumers.

While the impacts in Table 1 assume no cost pass-through, the statutory requirement for consumers to take regulated advice essentially makes the DB transfer advice a 'captive market'. Firms' ability to pass cost increases through to consumers is, therefore, already greater than for business lines that are not captive markets.

Potential impact on consumer prices for defined benefit transfer advice

We think price increases by PIFs who remain in the market are likely to be moderate, even if we assume no other off-setting factors such as reduced dividend payments or efficiency gains.

In our June 2017 consultation on DB transfer advice (CP 17/16), we estimated the average cost of a personal recommendation to transfer a DB pension to be £3,250. Applying the retained profit figures in Table 1, currently around £335 of this (10.3%) would be the PIF's retained profit.

A 200% increase in the cost of PII, would reduce the PIF's profit to £224 (6.9%). So, to maintain the pre-increase profit margin, a £3,250 fee would have to increase by around 3% (an increase of around £111). For comparison, a 500% premium rise would result in an increase of around 8% (£267).

Our retained profit margin figures apply to all activities the firm may be carrying out, rather than DB transfer advice specifically. DB transfer advice is one of the riskier activities a PIF might carry out. It is possible the PIF may therefore seek a greater return, meaning any price increase due to PII premium changes would be larger.

We stress again that we do not think our worst-case scenario will materialise. We note that the increase of 140% we calculated is based on a high estimate of the additional PII-insured liabilities that a £350,000 award limit would create, and is, therefore, already likely to be an upper bound.

We also stress that a DB transfer represents an irreversible transfer of risk from a pension scheme to a typically financially unsophisticated individual with no previous experience of making investment decisions. We think that consumers will ultimately benefit if average quality rises across the market (as higher risk firms who can no longer obtain PII exit),

even if prices also rise. Our recent policy work in the DB transfer area has provided greater detail on the steps advisers need to take to provide suitable advice.

Policy exclusions

Our rules in IPRU-INV state that a firm's PII policy 'must not be subject to conditions or exclusions which unreasonably limit its cover' (IPRU-INV 13.1.20R).

PIFs can hold policies that exclude activities the firm is carrying on, or has carried on in the past, if the firm holds additional capital to meet their potential liabilities in the absence of PII cover (IPRU-INV 13.1.21R). Additional capital means the amount of capital above the minimum amounts in the table at IPRU-INV 13.1.23R. In cases where a firm holds additional capital for this reason, the amount it must hold depends on its income.

Guidance on these rules (IPRU-INV 13.1.22G) states that:

- we would be unlikely to consider it reasonable for a firm's policy to exclude activities that the firm is carrying on or has carried on in the past
- firms should hold more than the minimum amount of additional capital if such an amount would be insufficient given the individual circumstances of the firm

Despite being permitted by our rules, our concern is that holding additional capital resources in place of PII may be a particularly inappropriate approach where a firm's policy excludes riskier, higher value activities, such as DB transfers. This is because a PIF's self-assessment of potential liabilities for determining how much additional capital it should hold might not match a PII insurer's more rigorous analysis of the underlying exposure.

This approach could, therefore, provide less consumer protection than PII. It could result in more firm failures and affected consumers having to seek compensation from the FSCS, which operates a lower limit than the ombudsman service.

We consider the best means of dealing with this risk is to supervise against it. We prefer this approach rather than attempting to create rules to prevent firms from abusing this approach.

One way we could do this is to consider whether we should improve the quality of our RMAR data on firms' PII, for example by making minor amendments and additions to Section E of the RMAR return. We intend to use the new data on firms' PII and use of additional capital to assess whether our existing prudential rules and guidance are effective.

Impact of our award limit proposals on the Financial Ombudsman Service, individual firms and the Financial Services Compensation Scheme

Q11: *Do you agree with our assessment of the impact of our award limit proposals on the ombudsman service?*

Q14: *Do you agree with our assessment of the impact of our award limit proposals on individual firms?*

Q15: *Do you agree with our assessment of the impact of our award limit proposals on the Financial Services Compensation Scheme?*

Q18: *Do you agree with our view that the award limits for the ombudsman service and the FSCS should not be aligned?*

2.46 We recognised in CP 18/31 that, if the ombudsman service has the power to require firms to pay substantially higher amounts of compensation, stakeholders must be confident it has the skills and expertise to decide such complaints fairly and reasonably.

2.47 However, we also recognised that there is no limit on the compensation the ombudsman service can recommend and its grounds for refusing to deal with a complaint are rather limited. We said the service should already be ensuring it has the skills and expertise necessary to determine any complaint from currently eligible complainants quickly. This must be done with minimum formality, and with reference to what, in its opinion, is fair and reasonable in all the circumstances of the case. We also noted that higher value complaints will not necessarily be more complex.

2.48 If the ombudsman service did require further resources specifically because of our proposals, we said these should not be significant. This is because most of the complaints covered by the proposed higher limit were within £50,000 of the existing limit, in terms of compensation awarded (ie compensation between £150,000 and £200,000).

2.49 Our primary concern for individual firms was the indirect impact of our proposals due to increased PII premiums. We have considered the PII implications of our proposals in an earlier section.

2.50 Regarding the Financial Services Compensation Scheme (FSCS), we said that:

- Firms may fail if they cannot afford to pay higher awards made by the ombudsman service because of our proposals. The risk of failure is likely to be limited to smaller firms, as they are less resilient to large awards.
- It is not obvious to us that the ombudsman service's award limit and the FSCS's compensation limit should be aligned. This is because the FSCS is a compensation scheme of last resort, unlike the ombudsman service. It acts as a backstop and requires active firms to pay compensation for failed firms. The ombudsman service requires active firms to pay compensation to their own customers for their own failings.

Feedback received

Impact on the Financial Ombudsman Service

- 2.51** Respondents from the financial services industry were not convinced that the ombudsman service currently has the resources it needs to deal effectively with high value complaints. They also disagreed that high value complaints would not necessarily be more complex.
- 2.52** Several respondents pointed to the concerns raised by the March 2018 Dispatches investigation, including on speed and quality of casework, issues relating to leadership, technology and costs, and future resourcing.
- 2.53** Some respondents from the financial advice sector said that the service had lost a significant number of experienced and specialist staff from the pensions and investment area in recent years. They doubted its ability to compete in the market for replacements.
- 2.54** A membership body representing PII insurers said it was not fair and reasonable for the ombudsman service to consider such complaints on paper alone and without expert input. They felt it inappropriate for an ombudsman to determine a high value pension transfer complaint when the individual ombudsman was less experienced and less qualified than the adviser being complained about.
- 2.55** The body said that a significantly higher award limit would require greater consideration by the ombudsman service of expert evidence – either from the parties to the complaint or by consulting external experts. Alternatively, the body said, the service would need to employ additional, skilled ombudsmen with appropriate qualifications and experience for dealing with complex products.
- 2.56** Some respondents said they were concerned that the ombudsman service would take the same approach to resolving complaints regardless of the value. They commented that court processes become increasingly rigorous according to the value of the claim.
- 2.57** Respondents also said that, even if complaints did not become inherently more complex as their values increased, the amount of money at risk would incentivise firms to defend complaints more vigorously. This could extend to more judicial reviews of the way the ombudsman service had reached its decisions.
- 2.58** A membership body representing small businesses said the ombudsman service needed to be ready for greater involvement of legal representatives and the deployment of technical arguments to refute complaints.

Impact on the Financial Services Compensation Scheme

- 2.59** Several respondents expressed concern that the costs of firms who fail because they cannot afford to pay compensation awarded by the ombudsman service would have to be picked up by other firms in the market. A membership body representing PIFs cited the difficulties the FSCS faces enforcing PII contracts of firms who have defaulted.
- 2.60** The other main comment on the impact on the FSCS was that the proposed £350,000 limit would significantly increase the existing discrepancy between the ombudsman service's award limit and the FSCS's compensation limits.

For claims in the investment advice area the FSCS compensation limit as of 1 April 2019 is £85,000. Given the average size of firms and the potential value of disputes,

the prospect of firm failure in this market may be the highest. However, respondents who pointed to this discrepancy tended to agree with us that the limits operated by the two organisations should not be aligned.

Our response

We deal with respondents' concerns about the appropriateness of the ombudsman service's approach for high value disputes, and its capacity to deal with such disputes in our response to feedback on the proposal for a £350,000 award limit.

In summary, we do not believe the courts provide a viable alternative for those classed as eligible complainants, and that the ombudsman service is an appropriate alternative.

We recognise that a significantly higher award limit is likely to incentivise firms to defend complaints more vigorously, including greater involvement of legal representatives. If a firm wishes to incur these additional costs then that is essentially a matter for the firm. These costs cannot be recovered from the complainant if their complaint is not upheld. The ombudsman service's process is designed to be inquisitorial rather than adversarial and should not require complainants or defendants to be legally represented.

Regarding the greater prospect of judicial review, it is essential that any public body can be held accountable for its decisions. We consider the need for accountability outweighs the additional costs that may result from more frequent judicial reviews of the service's decisions.

Regarding the discrepancy between the ombudsman service's award limit and the FSCS's compensation limit, we consider the limits should not be aligned as the organisations serve different purposes.

Our cost benefit analysis

Q19: *Do you agree with the costs, benefits and transfers we have identified? If not, please explain why.*

- 2.61** Elsewhere in this chapter, we have discussed feedback on the estimates and expected effects included in the CBA in CP 18/31 and provided our responses to this feedback. We do not repeat this discussion here. Instead, we summarise our previous and current estimates in table form to highlight the differences in total net benefits (or costs) under different assumptions.
- 2.62** In Table 2, we summarise how we described and valued the non-negligible quantifiable costs and benefits of our proposals in CP 18/31. Cost figures are shown in brackets, benefit figures without brackets.

Table 2: Significant quantifiable costs and benefits per year, £m

	Description	CP 18/31	This PS
Costs	Additional PII costs to insure against an increase in the size of awards made by the ombudsman service (net of redress payments insured) <i>(plus transfer from additional redress payments by firms to consumers due to a higher award limit)</i>	(77)	(9.8) to (32.3)
Benefits	Additional redress payments due to a higher award limit	113	21.6 to 47.6
	Net benefit	36	11.8 to 15.2

Note: In this PS the annual additional PI cost is calculated using a claims ratio of 63% from ABI data and a broker premium of 17.5%. Eg the upper bound is calculated as $£37.4m/0.63*1.175 - £37.4m = £32.3m$. In CP 18/31 the annual additional PII cost is calculated using a claims ratio of 63% only. We have included the broker premium following feedback from PII insurers that most PII policies are purchased via brokers. As some PII policies will be purchased without brokers, our total PII premium will, therefore, be an overestimate. The PII premium is a transfer between the firms and their insurers. The net benefits are lower bounds (where all PII costs are passed on to consumers). If firms absorb some of these costs, the net benefits would be higher.

2.63 In addition, the new rules have non-quantifiable benefits because consumers will be more appropriately compensated for their loss (ie restitutive justice). In addition, the greater expected amount of redress awarded to consumers increases the incentives for firms to assess and, if required, improve their conduct and product governance. This should reduce the number of problems with financial products and services provided to consumers. These non-quantifiable benefits – which we discussed in CP 18/31 – remain unchanged.

2.64 For completeness, we have also provided a list of negligible costs and benefits in Table 3 (largely unchanged from CP 18/31).

Table 3: Negligible impacts

	Description
Costs	Negligible familiarisation (ie one-off) costs because the amount of additional information firms must consider to understand the change in the rules regarding the ombudsman service’s award limit is minimal.
	No change to ongoing administrative complaints handling costs because there will be no change to the way firms are required to handle complaints.
	No significantly higher costs for the ombudsman service due to an increase in the number of complaints because the number of additional complaints is relatively small.
	No significant impact on the ombudsman service due to the need to bring in additional skills or expertise because the service should already have the skills and expertise in place to deal with complaints of any value.
Benefits	Lower costs to firms, due to reduced need for external assistance in ombudsman service complaints compared to court cases (not included in CP 18/31).
	Lower cost of getting redress for the minority of eligible complainants who, due to the current limit, may take firms to court to be fairly compensated.

Feedback received

2.65 Respondents made the following comments on our CBA:

- our estimates of higher PII costs had been produced with insufficient engagement with the PII industry
- we had not taken sufficient account of:
 - future complaint trends, particularly the impact of the growth in SIPPs
 - the cost of external assistance that firms may seek in preparing their response to the ombudsman service
 - the cost increases for the ombudsman service and firms because there will be more challenges to case handler decisions and more referrals to ombudsmen
 - the differential impact on mutual societies, because any additional redress costs would be passed on to customers because they cannot be absorbed by reducing profits and shareholder dividends

Our response

We believe the information obtained through the consultation process is sufficient for us to understand the potential impact on the PII industry. We have set out our detailed views on this in a separate section of this chapter.

Regarding our CBA estimates, the key change is that we have revised our estimate of net PII-related costs significantly downwards from £77 million to £32.3 million. This is a consequence of the changes we have made to our estimates of high value complaints and the portion of the overall redress shortfall that we think is likely to be underwritten by PII (£37.4 million).

Regarding future complaint trends, and SIPP complaint trends particularly, we understand from the ombudsman service that the volume of such complaints did increase significantly in the last reporting period. However, most of these related to advice from PIFs to invest with a specific discretionary fund manager. We think it is too early to know if this is indicative of a wider trend.

On the costs of external assistance that firms might incur, the ombudsman service takes an inquisitorial approach to dispute resolution so the parties should not need external assistance. Should they currently seek such assistance for court cases, their costs should fall.

On the potential for more complaints being resolved by ombudsmen, the data from the ombudsman service used to revise our high value complaint estimates shows that fewer high value complaints than we had assumed are resolved by case handlers. As such, we do not consider there will be a material impact from additional referrals to ombudsmen.

Regarding mutual societies, we do not consider the differential impact referred to above to be specific to the change we proposed to the

award limit. In our view, wherever a regulatory intervention increases costs for mutual societies these costs will inevitably be absorbed by customers. This is simply the nature of mutual societies.

Other issues related to the Financial Ombudsman Service's award limit

Q16: *Do you agree with our decision to rule out having different award limits for different types of complaint or complainant? If not, why do you think there should be different limits?*

Q17: *Do you agree with our view that there should be a limit to the amount of compensation the ombudsman service can require firms to pay to complainants? If not, how – if at all – would the ombudsman service's approach to dispute resolution need to change for it to be able to require firms to pay any amount of compensation?*

2.66 We said there should not be different limits for different types of complaint or complainant, even though we may have the option to set such limits under our powers. We said complainants should not be entitled to different amounts of compensation because of who they are or what they are complaining about.

2.67 We also noted more practical risks, such as different limits being difficult for complainants and firms to understand, and increased costs for the ombudsman service from potential judicial reviews on the boundaries between complaint or complainant types.

2.68 We also said that there should be an award limit. This is because, without the ability to appeal a determination, it would not be appropriate to expose firms to unlimited liability. We said the award limit also provides certainty for firms and their PII insurers on the extent of their liability, at least as far as the ombudsman service's decisions are concerned.

Feedback received

2.69 Respondents generally agreed with our view that the ombudsman service should operate with a single award limit. However, some respondents from the financial advice sector considered the proposed £350,000 limit a direct consequence of the extension of the service to larger SMEs, charities and trusts, and said we had not properly considered the impact on the market for financial advice.

2.70 Virtually all respondents agreed that there should be an award limit, although – as set out elsewhere in this PS – views differed on what the limit should be.

Our response

Given the general agreement with our positions on the need for a single award limit, we have no further comments. We address the concern about the influence of the extension of the ombudsman service to larger SMEs, charities and trusts in an earlier section.

3 Next steps

What you need to do next

- 3.1** If your firm is affected by these changes, you should ensure you meet the requirements by 1 April 2019.
- 3.2** We recognise that this is a reasonably short implementation period. However, we consulted on increasing the award limit on 1 April 2019 in CP 18/31, which was published in October 2018. This was so the change could come into force at the same time as the extension of the ombudsman service to larger SMEs, which we considered a logical approach. Firms should, therefore, already be planning for changes to the limit, with this PS serving as confirmation of what the change will be.
- 3.3** We advise firms to focus on the changes they will need to have in place on the day the new award limits come into force. These include:
- updating consumer-facing information about complaint handling procedures
 - ensuring they are using the most recent version of the ombudsman service's standard explanatory leaflet
 - ensuring complaint handling staff are aware of the increased limits

Annex 1

Compatibility statement

1. In CP 18/31 (Annex 3) we gave our view of the compatibility of our proposed changes to the Financial Ombudsman Service's ('the ombudsman service's) award limit with our statutory and other obligations.
2. Overall, we were satisfied that the proposed changes were compatible with our general duties in accordance with section 1B of FSMA, having regard to the regulatory principles in section 3B.

The FCA's objectives and regulatory principles

3. We have a general duty to discharge our general functions, such as rule-making, in a way that is compatible with our strategic objective of ensuring the relevant markets function well, and which advances at least one of our consumer protection, market integrity or competition operational objectives. In line with this, we have not changed our assessment in CP 18/31 that increasing the ombudsman service's award limit would:
 - secure an appropriate degree of protection for consumers by ensuring more eligible complainants will receive fair compensation when they have not been treated fairly and reasonably by firms
 - strengthen firms' incentives to resolve complaints quickly and informally, or to avoid them altogether, in turn helping to build consumer trust in the integrity of the industry
 - support our duty to promote effective competition in the interests of consumers, because:
 - firms that cause substantial financial harm to consumers will have to pay more redress because of poor conduct, meaning firms with better conduct may be able to outcompete them
 - consumers will know that all firms will be required to pay higher amounts of compensation in the event of a dispute, rather than this being at individual firms' discretion (and therefore not knowable at the time of purchase)
4. Due to the consultation feedback on the potential impact of our proposals on the cost and availability of professional indemnity insurance (PII) for personal investment firms (PIFs), we have further considered our competition duty, particularly in relation to the defined benefit (DB) pension transfer advice market. As we explain in our response to the feedback on this issue, while it is possible the number of firms in this market will fall significantly because of our intervention, we consider the number of firms remaining should be sufficient to ensure competitive outcomes for consumers.
5. Regarding our duty to have regard to the regulatory principles set out in section 3B FSMA, we consider our assessment of our proposals in CP 18/31 still stands.

Government recommendations about economic policy

6. We also had due regard to the recommendations made by the Treasury under section 1JA FSMA about aspects of the economic policy of Her Majesty's Government.
7. In particular, we considered that, for the reasons set out above, increasing the ombudsman service's award limit supported the Treasury's recommendations relating to better outcomes for consumers.

Expected effect on mutual societies

8. Despite the feedback at paragraph at 2.65, our view remains that increasing the ombudsman service's award limit would not have a significantly different impact on mutual societies compared to any other type of firm responding to a complaint from an eligible complainant.

Equality and diversity

9. We are required under the Equality Act 2010 to 'have due regard' to the need to eliminate discrimination and to promote equality of opportunity in carrying out our policies, services and functions. As part of this, we conduct an equality impact assessment to ensure that the equality and diversity implications of any new policy proposals are considered.
10. The outcome of the assessment in this case is stated in paragraphs 1.54-1.55 of Chapter 1.

Legislative and Regulatory Reform Act 2006 (LRRRA)

11. The LRRRA principles and Regulators' Code do not apply when we are making rules. So, they did not apply to CP 18/31, nor do they apply to this Policy Statement.

Annex 2

List of non-confidential respondents

Able Financial Ltd

Accounting Angels Limited

Adam Samuel

ADD Wealth

Advance Investments Ltd

AGB Financial Services Ltd

All Party Parliamentary Group on Fair Business Banking

Amar Financial Services

AMR Financial Management Ltd

Anders Bayley Scott Ltd

Andrew Heptinstall IFA

Artisan Financial Ltd

Assicurazioni Generali

Association of British Insurers

Association of Financial Mutuals

Association of Mortgage Intermediaries

Attivo Financial Services

AV Trinity

Bradstyle Ltd

British Insurance Brokers Association

Broker Network

Cameron Trinity Limited

Castle Financial Services

Central Wealth Planning Ltd

Coleman Financial Services Ltd

Compliance and Training Solutions Ltd

Compliance News Ltd

Congruent

Connells Limited

Councillor

Cranwell James Financial Planning Ltd

CS Financial Solutions

Derek Bradley

DGS Independent Financial Advisers Ltd

Doug Brodie

Eden Independent Financial Advisers Ltd

Elementary Financial Planning

Facts & Figures

Federal of Small Businesses

Field Hamlin

Finance and Leasing Association

Financial Services Consumer Panel

French & Associates Ltd

Funding Circle Ltd

Gladstone Brookes

Gresham Financial Limited

Guardian Financial Planners Ltd

Hartley Wadsworth & Partners

HCR Independent Financial Advisers Ltd

HKA (FS) Ltd

IMLA

Indigo Financial Advice Ltd
Informed Financial Planning
International Underwriting Association
InvestAcc Ltd
Jackson Jeffrey Independent Financial Services
Landmark Financial Planning
Later Life Asset Management Ltd
LFP Financial Planning and Wealth Management
Libertatem
Lumley Baxter
Manor IFA Ltd
Moneyology
Novus Wealth Management
Oakland Financial Management Ltd
Philip J Milton & Company Plc
PIMFA
Protection and investment ltd
PW Financial management Limited
Richmond House Wealth Management
Rod Leonard
Rosemount Independent Financial Advisers Ltd
Rt Hon Caroline Flint MP and Nic Dakin MP
Sense Network
Simple Solutions Financial Management Ltd
Sims Financial Planning
Society of Pension Professionals
Sound Advice Financial Management

Strategic Investment Solutions Ltd.
Stuart Binns & Associates
Taylor Made Financial Planning LLP
Tenet Group Ltd
Thameside Financial Planning Ltd
The On-Line Partnership Limited
The Wealth Group
Thomas Ryan
threesixty Services LLP
Throgmorton Financial Services Ltd
Tim Hines
True Bearing Chartered Financial Planners
UK Finance
Valid Path Ltd
Verity Wealth Management LLP
W Denis Financial Services Ltd
Whiting & Partners Wealth Management Ltd
Winterbourne Trustee Services Limited
WRS Fornham Financial Management Ltd
XL Independent Financial Advisers Ltd
Yellowtail Financial Planning
Zurich

Annex 3

Abbreviations used in this paper

AFCA	Australian Financial Complaints Authority
CBA	Cost benefit analysis
CETV	Cash equivalent transfer value
CFA	Conditional fee arrangement
CJ	Compulsory Jurisdiction
CMC	Claims management company
CP	Consultation Paper
CPI	Consumer Prices Index
DB	Defined benefit
DBA	Damages based agreement
DISP	Dispute Resolution sourcebook
FCA	Financial Conduct Authority
FSCS	Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
IFA	Independent financial adviser
IPRU-INV	Interim Prudential sourcebook for Investment Business
LRRA	Legislative and Regulatory Reform Act 2006
PIF	Personal investment firm
PII	Professional indemnity insurance
pp	Percentage point
PPI	Payment protection insurance
PS	Policy Statement

RMAR	Retail Mediation Activities Return
SIPP	Self-invested personal pension
SME	Small and medium-sized enterprise
VJ	Voluntary Jurisdiction

We have developed the policy in this Policy Statement in the context of the existing UK and EU regulatory framework. The Government has made clear that it will continue to implement and apply EU law until the UK has left the EU. We will keep the proposals under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework in the future.

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Appendix 1

Made rules (legal instrument)

FINANCIAL OMBUDSMAN SERVICE (AWARD LIMIT) INSTRUMENT 2019

Powers exercised by the Financial Ombudsman Service

- A. The Financial Ombudsman Service Limited makes and amends the Voluntary Jurisdiction rules and guidance, and fixes and varies the standard terms for Voluntary Jurisdiction participants as set out in the Annex to this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 227 (Voluntary Jurisdiction);
 - (2) paragraph 8 (Guidance) of Schedule 17;
 - (3) paragraph 18 (Terms of reference to the scheme) of Schedule 17; and
 - (4) paragraph 22 (Consultation) of Schedule 17.
- B. The Financial Ombudsman Service Limited notes that, for the avoidance of doubt, the Transitional Provisions at TP 1.1 in the Annex below apply equally to the Voluntary Jurisdiction of the Financial Ombudsman Service Limited and the Compulsory Jurisdiction.
- C. The making and amendment of the Voluntary Jurisdiction rules and guidance and the fixing and varying of the standard terms for Voluntary Jurisdiction participants by the Financial Ombudsman Service Limited is subject to the approval of the Financial Conduct Authority.

Powers exercised by the Financial Conduct Authority

- D. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions of the Act:
- (1) section 137T (General supplementary powers); and
 - (2) section 229 (Awards).
- E. The rule-making powers listed above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.
- F. The Financial Conduct Authority approves the Voluntary Jurisdiction rules and guidance to be made and amended and the standard terms for Voluntary Jurisdiction participants to be fixed and varied by the Financial Ombudsman Service Limited under this instrument.

Commencement

- G. This instrument comes into force on 1 April 2019, immediately after those changes made by the Small Business (Eligible Complainant) Instrument 2018 (FCA 2018/61) (FOS 2018/7) come into force.

Amendments to the Handbook

- H. The Dispute Resolution: Complaints sourcebook (DISP) is amended in accordance with the Annex to this instrument.

Notes

- I. In the Annex to this instrument, the “note” (indicated by “**Note:**”) is included for the convenience of readers but does not form part of the legislative text.

Citation

- J. This instrument may be cited as the Financial Ombudsman Service (Award Limit) Instrument 2019.

By order of the Board of the Financial Conduct Authority
28 February 2019

By order of the Board of the Financial Ombudsman Service Limited
6 March 2019

Annex

Amendments to the Dispute Resolution: Complaints sourcebook (DISP)

In this Annex, underlining indicates new text and striking through indicates deleted text.

3 Complaint handling procedures of the Financial Ombudsman Service

...

3.7 Awards by the Ombudsman

...

Money awards

...

- 3.7.4 R (1) The maximum money award which the *Ombudsman* may make is: ~~£150,000.~~
- (a) £350,000 for a *complaint* concerning an act or omission which occurred on or after 1 April 2019; and
- (b) £160,000 for a *complaint* concerning an act or omission which occurred before 1 April 2019.
- (2) On 1 April each year, for *complaints* referred to the *Financial Ombudsman Service* on or after this date up to and including 31 March in the following year, the amounts in (1)(a) and (b) are adjusted by:
- (a) applying the percentage increase in *CPI* between January 2019 and January of that year; and
- (b) rounding down to the nearest £5,000.

[Note: The maximum money award which the *Ombudsman* may make is set out in the table below. This Note will be updated before any new limit takes effect.]

date of act or omission \ date complaint referred	before 1 April 2019	on or after 1 April 2019
	before 1 January 2012	£100,000
before 1 April 2019 but on or after 1 January 2012	£150,000	n/a
on or after 1 April 2019	£160,000	£350,000

...

TP 1 Transitional provisions

1.1 Transitional Provisions table

(1)	(2) Material provision to which transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
...					
<u>52A</u>	<u>DISP 3.7.4</u>	<u>R</u>	<u>For a complaint referred to the Financial Ombudsman Service before 1 April 2019 but on or after 1 January 2012 the maximum money award which the Ombudsman may make is £150,000.</u>	<u>From 1 April 2019</u>	<u>1 April 2019</u>

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