

# outlook

CREDIT UNION SPECIAL

The Newsletter for the Financial Services Compensation Scheme



## from the Chairman

We welcome this opportunity to explain to credit unions who we are and the benefits of belonging to the Financial Services Compensation Scheme.

One of the aims of the Scheme is to provide financial protection for some of the most vulnerable sections of society. These include people who are least able to bear the loss of their savings should a deposit taker fail.

Although the Scheme doesn't provide 100% protection, its existence helps to promote confidence in the sector.

We also want to ensure that relevant and timely information is easily available about our activities, and this newsletter is part of our programme for achieving that goal.

We are always open to suggestions on how we can improve our communications, and we look forward to any comments or suggestions you have for developing this.

If you would like more information about FSCS please visit our website, [www.fscs.org.uk](http://www.fscs.org.uk), or contact our Helpline on 020 7892 7300.

**Nigel Hamilton, Chairman**

## Welcome to the Financial Services Compensation Scheme

The Financial Services Compensation Scheme (FSCS) officially took over responsibility for compensation in the financial services sector from 1 December 2001, when the Financial Services and Markets Act (FSMA) 2000 came into force.

FSCS replaced eight existing schemes including the Deposit Protection Scheme, (which covered deposit takers), the Building Societies Investor Protection Scheme, the Investors Compensation Scheme (which covered

investment firms) and the Policyholders Protection Scheme (which covered insurance companies).

It is accountable to, but independent from, the UK's regulator, the Financial Services Authority (FSA) and funded by a levy on authorised firms.

The Scheme acts as a final safety net for consumers who have claims against regulated finance sector firms that are unable to pay them. This is generally because they have gone out

of business or are insolvent. We cover deposits, insurance and investments.

The protection isn't total - there are limits to the amounts of compensation we can pay (see page 3).

But the Scheme plays a vital role in reassuring consumers that if a financial services firm fails, they won't be faced with severe financial hardship or suffer total financial loss.

We look forward to welcoming credit unions into the Scheme.



**Chief Executive, Suzanne McCarthy. She welcomes deposit protection being extended to credit unions.**

**"Credit unions provide a vital service," she says.**

**"After 1 July 2002 their members can be confident that if a credit union fails, their deposits will be protected."**

## Where does the Scheme fit in?

**FSA, FSCS, FOS .. where does the Scheme fit into the regulatory world?**

The Financial Services Authority (FSA) is the UK's single regulator for the finance industry, created under FSMA.

FSMA also created a single Ombudsman Service and a

single Compensation Scheme.

The FSCS and the Financial Ombudsman Scheme (FOS) are separate bodies, independent from (but accountable to) the FSA.

FSCS is only triggered if there is a claim against a regulated firm which is

unable to pay claims against it (or likely to be unable to pay). For example when a credit union is insolvent.

The Financial Ombudsman handles complaints from consumers against 'live' firms - those that are still authorised and trading.

2 **How the Scheme will work**

3 **Compensation - the limitations**

4 **Introducing the Committees**

# FSCS board



Michael Blair, QC



Sarah Brown



Ken Culley, CBE



Graeme MacLennan



Luke March



Tim Vogel



John Young, CBE

The conduct of the Compensation Scheme is the responsibility of its Board of Directors, appointed by the Financial Services Authority (FSA).

Under the Financial Services & Markets Act 2000 (FSMA), the FSA appoints the Directors on terms which secure their independence from the FSA in the operation of the Scheme. The Chairman's appointment (and removal) is also subject to the approval of the Treasury.

FSCS is independent from the FSA, although accountable to it, and, ultimately, to the Treasury.

Board members (from top): Michael Blair, QC; Sarah Brown; Kenneth Culley, CBE; Graeme MacLennan; Luke March; Tim Vogel; John Young, CBE.

FSCS' Chairman, Nigel Hamilton, and Chief Executive, Suzanne McCarthy, are pictured on page one.

## Why do we exist?

### Promoting confidence and good practice

Our reason for existing is to pay compensation to consumers in the most cost effective way.

We'll compensate consumers if a bank, building society, credit union or insurance company collapses.

We'll compensate consumers if they've lost money after investing, for example, because they've been given bad advice by an IFA that's now gone out of business, or if an IFA disappears with their clients' money.

We're a safety net - a last resort and a lifeline for many.

But we will also ensure that we recover as much as we possibly can to lessen the burden on levy payers.

The presence of a compensation scheme helps to maintain a sense of confidence in the sector.

Compensation isn't unlimited, consumers have to accept some level of responsibility for their money and the decisions they take.

However, the presence of a compensation scheme promotes financial stability and lessens the risk of a single failure triggering a wider loss of confidence.

We appreciate that levy payers can feel that the good pay for the bad.

But without a scheme, consumer confidence in this vital sector would be threatened.

## Funding

Levy payers, depending upon their regulated permissions, are allocated to a contribution group, similar to the FSA's fee blocks, within a sub-scheme.

These sub-schemes are:

- accepting deposits
- insurance business
- designated investment business.

Credit unions will be within the accepting deposits sub-scheme.

For levying purposes, FSCS' cost structure comprises:

#### Management expenses

These are FSCS' overheads split between base costs and specific costs. All levy payers contribute to the base costs -

the costs of running the scheme.

Specific costs are the cost of assessing claims and making payments. These will be allocated to the relevant contribution group.

The Management Expenses Levy is subject to an annual limit, covered by annual consultation.

#### Establishment costs

All levy payers contribute to their share of establishment costs, which are being spread over three years from 1 December 2001.

#### Compensation payments

Firms within each contribution group will be

liable for the related compensation costs. Levy amounts will be based on the contribution group tariff.

Compensation levies are limited by reference to sub-schemes.

**Deposits:** firms pay no more than 0.3% of their protected deposits.

*You may be exempt*

Because the amount of any levy may be relatively small, some firms may be below the minimum payment level and be exempt from paying the levy.

For further information on funding, and how your credit union could be affected, contact our helpline.

# Making the Rules

**Under FSMA, the FSA were obliged to make the Rules for the FSCS. These set out the obligations of the Scheme, types of claim covered, who is eligible for compensation, the amount of compensation payable and how compensation may be calculated.**

FSCS covers claims against firms where they are unable, or likely to be unable, to pay claims against them.

In general this is when a firm is insolvent or has gone out of business. These are described by FSCS as being 'in default'.

The primary aim of the scheme is to provide protection for private individuals, although small businesses are included.

Larger businesses are generally excluded, aside from cover for compulsory and long term insurance policies.

There are limits to the amount of compensation payable.

FSCS will require assignment of rights from claimants which allows FSCS to try to recover funds both from the firm in default and third parties.

Any recoveries will be paid into the fund from which the compensation was paid.

## How the rules apply

In the majority of cases FSCS will be notified by the FSA that a credit union is insolvent.

### Default

However, before FSCS can pay compensation it will need to satisfy itself that the credit union cannot meet claims and then declare the credit union "in default".

This process of declaring the credit union in default opens the way for claims to be processed for payment.

Once the credit union has been declared in default FSCS will issue a press release. This should help to ensure that all those entitled to claim compensation are made aware that they can make a claim.

### Application form

Each member of the credit union will need to complete an application form to claim compensation.

In order for FSCS to issue these claim forms we will need up to date address details for each member of the credit union.

### Assistance

Members of a failed credit union will be able to contact

the FSCS Helpline for assistance in completing their claim application form.

### Proof of deposit

A member will be required to provide proof of their deposit with the failed credit union. FSCS will then verify this against the books and records of the credit union.

Once the level of compensation has been decided FSCS will issue an offer of compensation that will need to be signed by the member and returned to us.

### Offer

Once the offer has been returned FSCS will be able to make the compensation payment.

### Methods of payment

FSCS is currently considering the most appropriate way of paying compensation and this will ultimately depend on the circumstances of each individual.

Where possible FSCS will issue a cheque, but it is considering alternatives for those members who do not have a bank or building society account.



## The limitations

There are limits to the cover the Scheme provides. Consumers do have to accept they should take some responsibility for their money and the decisions they make. The Scheme is only triggered when a financial services firm is unable, or likely to be unable, to pay claims against it.

The maximum levels of compensation are:

- **Claims against deposit takers**

£31,700 (100% of £2,000 and 90% of the next £33,000).

- **Claims against investment firms**

£48,000 (100% of £30,000 and 90% of the next £20,000).

*The Scheme covers two kinds of loss:*

When an authorised investment firm goes out of business and cannot return investments or money.

Loss arising from bad investment advice, or poor investment management.

Investments covered include: stocks and shares;

unit trusts; futures and options; personal pension plans and long-term policies, such as endowments.

- **Claims against insurance companies**

*Long-term insurance* (e.g. pensions and life assurance): 100% of the first £2,000 plus 90% of the remainder of the claim.

*General insurance:* compulsory insurance (e.g. third party motor): 100% of the claim.

non-compulsory insurance (e.g. home and general): 100% of the first £2,000 plus 90% of the remainder of the claim.

**The actual level of compensation paid will depend on the claim.**

## Protection for credit union members will benefit the sector

Membership of FSCS will benefit credit unions and their members, according to Chief Executive Suzanne McCarthy.

“The existence of a safety net should encourage more consumers to use the services credit unions provide,” she says.

“In a world where people on low incomes can be ‘excluded’ from access to high street bank or building society accounts, credit unions have a valuable service to offer,” she says.

Suzanne is a guest speaker at a number of credit union conferences this year,

including the Scottish League Annual Conference, held in Perth in March, and ABCUL’s annual meeting in April.

“It is vital that those working in credit unions understand the value of the Scheme and what it means to their members,” says Suzanne.

“We need to let those people who use credit unions know what protection is available,” she says.

FSCS has produced a consumer guide to the Scheme. For copies call our Helpline on 020 7892 7300.



## Understanding the industry

One of our main aims is to foster understanding and awareness amongst all our stakeholders.

FSCS has set up three Industry Committees covering deposits, insurance and investments.

Two experienced industry practitioners have been co-opted onto each Committee, and the Committee members may invite other industry experts to advise them from time to time.

### Deposit-taking Industry Committee

Ken Culley (Chairman)  
Michael Blair, QC  
Sarah Brown  
Suzanne McCarthy

Co-opted members:  
Gordon Pell, RBS  
Matthew Wyles, Portman Building Society

### Insurance Industry Committee

John Young (Chairman)  
Nigel Hamilton  
Suzanne McCarthy

Co-opted members:  
Stephan Pater, Royal & Sun Alliance  
Iain Lumsden, Standard Life

### Investment Industry Committee

Graeme MacLennan (Chairman)  
Suzanne McCarthy  
Tim Vogel

Co-opted members:  
Allan Daffern, IFA  
Chris Lyttelton, NCL Investments Ltd

### So what do the Industry Committees do?

- Look at issues affecting industry which could impact on the Scheme.
- Review the flow of work and likely future workload for the Scheme.
- Monitor the Scheme’s relationship with levy payers.

If you have a particular issue you would like an Industry Committee to look at, please write to the Committee Chairman at the address below.

# Tell us what you think

## We’d like to hear from you!

Any comments or issues you’d like to raise? Write to Heather Tilston, at:

Outlook, FSCS, 7th Floor, Lloyds chambers, 1 Portsoken St, London, E1 8BN  
e-mail [Heather.Tilston@fscs.org.uk](mailto:Heather.Tilston@fscs.org.uk)

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[WWW.FSCS.ORG.UK](http://WWW.FSCS.ORG.UK)

*Outlook is published by the Financial Services Compensation Scheme*