Financial Ombudsman Service

a quick guide to …

calculating compensation for mis-sold mortgage endowments

This quick guide is for businesses who receive relatively few complaints about mis-sold mortgage endowment policies. It explains the standard way compensation is calculated – as set out by the regulator – where we uphold a consumer's complaint.

where can I find the rules on how to compensate a consumer?

The Financial Conduct Authority (FCA) sets out how businesses should calculate compensation in a guidance note called *Handling Mortgage Endowment Complaints*. This is Appendix 1 of the section called Dispute Resolution: Complaints (the "DISP rules") in the *FCA Handbook*. It is available online at http://fshandbook.info/FS/html/FCA/DISP/App/1

These rules are sometimes referred to as the "RU89" calculations. This is because they first appeared in a publication known as Regulatory Update No.89.

what is the standard approach to mortgage endowment redress?

Simply, you can calculate the consumer's loss by comparing their *current* position with the position they *would be in* if they had taken out a *repayment* mortgage instead.
In the most straightforward cases, you will need to compare:

1. the total amount the consumer has *actually* paid in endowment premiums and mortgage interest payments

   with

   the total payments they *would have* made on an equivalent repayment mortgage (and, if appropriate, any insurance premiums for life cover).

   This is the "payment" comparison part of the calculation.

   and

2. the current "surrender value" of the endowment policy

   with

   the amount of capital the consumer *would have* paid off an equivalent repayment mortgage by now.

   This is the "capital" comparison part of the calculation.

In most cases, we will assume that the equivalent repayment mortgage would have run for the same term as the endowment mortgage.

But where we think an endowment mortgage was inappropriately set up to run beyond the consumer's retirement, we may ask a business to make the comparison with a repayment mortgage over a shorter term –

that would have paid off the mortgage before retirement.

The overall loss to the consumer of taking out an endowment mortgage rather than a repayment mortgage will be the sum of the "payment" comparison and the "capital" comparison.

what if I think the consumer was better off with an endowment mortgage?

If the "payment" comparison shows that the consumer has paid *more* into their endowment mortgage than they would have paid into an equivalent repayment mortgage, you can reduce this loss by the amount of any gain you identify in the "capital" comparison.

But if the "payment" comparison shows that the consumer has paid less into their endowment mortgage than they would have paid into an equivalent repayment mortgage, we would not usually expect you to deduct the "savings" made from any loss you identify in the "capital" comparison.

The FCA Handbook has specific guidance about when businesses can take past "savings" into account when calculating a consumer's loss.

In our experience, it is rare for a firm to be able to show that taking these "savings" into account is reasonable.

In general terms, the guidance says that you can only take savings into account if the consumer has retained any money "saved" this way. In our experience, it is rare that a business to can show that taking these "savings" into account is reasonable.

what else does the compensation have to cover?

A consumer who decides to surrender a mis-sold endowment policy may need to take out new insurance – to replace the life cover that was previously included as part of the endowment.

If taking out this replacement life cover is more expensive now than it was when the consumer originally took out the mortgage, you should offer extra compensation to cover the extra cost.

If the consumer uses compensation you pay them– and/or money from surrendering the mis-sold endowment policy – to repay part of the mortgage loan, you should generally pay any early repayment fees charged by the mortgage lender.

Similarly, if the consumer decides to convert to a repayment mortgage with the same lender, you should pay any switching fees charged by the lender.

You may have to pay these early repayment fees or switching costs even if the redress calculations show that – overall– the consumer is no worse off as a result of being mis-sold an endowment policy. This will depend on the size of the costs compared with any gain shown by the calculations.

what if the consumer's circumstances aren't so straightforward?

Over the years, a consumer may have reviewed their circumstances and changed their mortgage arrangements – perhaps converting from an endowment mortgage to a repayment mortgage. Or they may have decided to pay off their mortgage early.

Taking these factors into account can make calculating compensation more complicated.

Our general approach to less straightforward situations is set out on our website at www.financial-ombudsman.org.uk/publications/technical_notes/mortgage-endowments.htm. But we look at the circumstances of each individual case when deciding how the consumer should be compensated.

how are the redress calculations run?

The standard approach described in this quick guide sets out a framework in which to run the specific calculations. But the calculations themselves are usually quite complex – and it is unlikely that they can be carried out manually.

Software packages specifically designed to carry out these calculations are available.

But if you receive relatively few complaints about mis-sold mortgage endowments, it may be easier to pay a specialist company to calculate compensation on your behalf.

We can't give you advice on whether to engage a company – or which one to use. But the Association of Professional Financial Advisers (www.apfa.net) and the Institute and Faculty of Actuaries (www.actuaries.org.uk) may be able to help.

www.financial-ombudsman.org.uk

visit our website for:

- news and frequently-asked questions
- information and updates
- technical information for businesses and help for consumers
- *ombudsman news* – our regular newsletter with case studies, features and commentary.

Compensation for mis-sold mortgage endowments can be complex. This quick guide gives only a limited explanation of some of the main points. It is not a definitive statement of the law, the rules or our approach.