



Financial Ombudsman Service

Plan & Budget 2002/03

For the year ending 31 March 2003



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Please send your comments by 21 February 2002 to

Jeremy Kean

Finance Director

Financial Ombudsman Service

South Quay Plaza

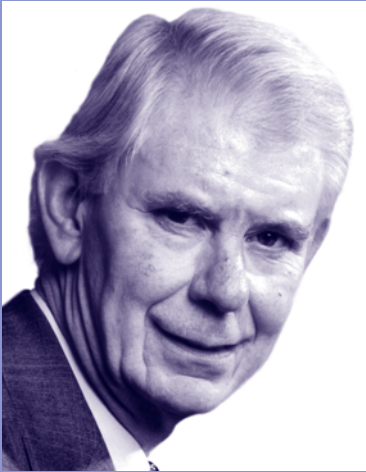
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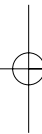
email jeremy.kean@financial-ombudsman.org.uk.

chapter one

foreword by the chairman



Andreas Whittam Smith
Chairman



This is the second year in which we have consulted on our plan and budget. As before, we are keen to hear from all those with an interest in the cost and efficiency of our service.

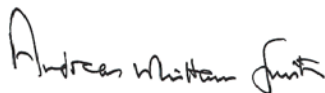
In the current year we have had to absorb the full impact of the endowment mortgage complaints generated by the flood of re-projection letters that investment firms have sent to their customers.

The coming year looks to be an uncertain one. HM Treasury's announcement – in December 2001 – that the Financial Services Authority (FSA) will regulate mortgage and insurance intermediaries, means that this area of complaint work will eventually come into our Compulsory Jurisdiction. It is still unclear whether, until then, it can be brought into the Voluntary Jurisdiction in the coming year. But whenever it comes, we can expect substantial increases in the volume of work.

In the short-term, next year's mortgage endowment re-projection letters could increase our workload. On the other hand, there are hopeful signs of a decrease in underlying complaint numbers. We aim to respond flexibly to any major alteration in the volumes of complaints we receive, but it is also important that we maintain a stable organisation.

When, in April 2000, we took over the administration of the schemes we inherited, the average unit cost per case had been £730 in the previous year – 1999/2000. We had immediately to invest substantial sums in the new organisation and the unit cost in 2000/01 rose to £753. Our aim was to bring down the unit cost to the level we had inherited – or below if possible. In the current year, we expect the unit cost to have reduced to £688. Of course, some of that reduction is attributable to the increased volume of complaints. But even if there is a flattening of complaint numbers, we hope to reduce the unit cost in real terms – by absorbing staffing cost increases and inflation – and by keeping the unit cost at the same level as in the current year – £688.

Our budget will require approval from the FSA, and we will report to the FSA on the response to this consultation when we seek final approval.



Andreas Whittam Smith

January 2002

chapter two executive summary

‘we have introduced our
new business process
and supporting
case-handling system’

introduction

- 2.1** The purpose of this document is to report on the performance of the Financial Ombudsman Service during 2001/02 and to consult on costs and funding for the year to March 2003. The Financial Services and Markets Act came into force in December 2001 and this will be the first year that we will recover our costs directly from firms by way of a general levy and case fees. The arrangements for the funding of the Financial Ombudsman Service were consulted on in consultation papers CP33 and 74 and finalised in the Policy Document, *Dispute Resolution: the Complaints Sourcebook*.
- 2.2** This document also consults on the rule to apply the relevant funding rules in the FSA Handbook, Module DISP Chapter 5, to the funding of the Voluntary Jurisdiction, from April 2002. This will be included in the Standard Terms (FSA Handbook, Module DISP, Chapter 4).
- 2.3** The focus of this year has been preparation for 'N2', the date when we assumed our full responsibilities under the Financial Services and Markets Act. This has included the introduction of a new business process and case-handling system, finalising new eligibility, process and funding rules, and harmonising ombudsman policy. We have also had to react to the high level of mortgage endowment complaints and to maintain quality targets in call handling and processing.

key points of the current year 2001/02

- 2.4** A summary of the key points of the current year – 2001/02 – is as follows:
- a) new complaints** There are indications that the level of new complaints is finally slowing. Overall, we are still forecasting an increase of 21% in new complaints in 2001/02 compared with the previous year, largely due to mortgage endowment complaints. The number of new complaints overall is still increasing, but the last few months have seen a perceptible slow down in the rate of increase, which is welcome news.
- b) case closures** During the year, we have introduced our new business process and supporting case-handling system. Developing a new system poses a significant risk for any organisation but despite the inevitable disruption, we still expect to achieve our 2001/02 case closure forecast of 38,500.
- c) unit cost** In our plan and budget for 2001/02, we forecast a fall in the unit cost from £764 to £688. In cash terms, this was a decrease of £76 (allowing for inflation, it was a decrease of around £100). At present, we expect to meet the target of £688.

2.5 As we look towards 2002/03, our main area of uncertainty is the level of new complaints. At present, we have differing indicators as to the future trend. As mentioned above, there are indications of a slowdown in the level of new complaints reaching us, but several other factors – discussed in Chapter 5 – suggest that this might not be a long-term trend.

**key points
for the
budget year
2002/03**

2.6 Key points for the budget year 2002/03 are as follows:

- a) **new complaints** Given the uncertainty over the level of new complaints, we have assumed that there will be no significant change in the number of new complaints – so the number of new cases is expected to be 37,500. But we have also tested two alternative scenarios: a 10% increase and a 10% fall in new cases.
- b) **productivity** Our assumption for the base case of ‘no growth’ is that we will continue to improve productivity. Overall, we aim to increase productivity by 25% in the three years from 2000/01 to 2002/03. This will result in case closures for 2002/03 rising to 40,000.
- c) **service quality** Following the introduction of our new business process and introduction of the new case-handling system – and the changes associated with N2 – it is important that we introduce formal internal quality control benchmarks from the beginning of the next financial year. These will include quality measurements for both decisions and process and will enable us to monitor the expected improvements in the timeliness and quality of our casework.
- d) **budget and unit cost** The result of these assumptions is a total budget for 2002/03 of £28.2m, an increase of 2.2% over the current year. The forecast unit cost remains in line with this year – in absolute terms – at £688 (*ie* £27.5m costs before interest, divided by the forecast 40,000 case closures). This represents a fall, allowing for inflation, of £20 after absorbing the improved timeliness and service efficiency standards noted above, staff salary increases, and a higher depreciation charge.

conclusion

2.7 We welcome any comments on the different aspects of the plan, its assumptions, the level of the case fee and the tariff for the Voluntary Jurisdiction. We also welcome any comments on the proposed additional rule in the Standard Terms for funding the Voluntary Jurisdiction. Any comments on the general levy tariff rates and establishment levy should be made to the FSA, as these matters form part of the FSA’s consultation document, CP119.

chapter three
performance
during the
current year

‘our activities have
concentrated on
preparing for N2’

introduction

- 3.1** Our activities during the year have concentrated on preparing for N2. Although the Financial Ombudsman Service has been operating to all intents and purposes as one entity, in reality it has operated under service level agreements on behalf of the existing schemes. At N2, these arrangements fell away and the Financial Ombudsman Service now operates under its own statutory powers.
- 3.2** The key activities of the year so far have been as follows:
- 3.3 achievement of targets** During a year that has seen considerable challenges with the introduction of our new casework system and business process, and the change associated with N2, we are on target to meet our anticipated number of case closures and our budget for the unit cost.
- 3.4 preparations for N2, including the harmonisation of ombudsman policy** Previously the ombudsmen within the Financial Ombudsman Service operated using different sets of rules, depending on the scheme to which an individual complaint related. Our panel of ombudsmen have met regularly to discuss issues that will arise after N2 and ensure that decisions will be consistent, fair and reasonable across the Financial Ombudsman Service.
- 3.5 finalisation of new eligibility, process and funding rules** In conjunction with the FSA, we have already consulted on draft funding rules and these rules have been published in 'virtual final' form. Rules covering internal complaints-handling procedures, jurisdiction, and investigation procedures have also been made, after consultation with the industry. HM Treasury has made rules relating to transitional arrangements, which extend the scope of our powers to include complaints about pre-N2 business. This will enable us to have a 'seamless' transfer between the old schemes and the new service. Without this, the situation would have been complex, and confusing for consumers.
- 3.6 close co-operation with the FSA on mortgage endowment redress policy** Following the FSA's publication of its regulatory guidance on mortgage endowment complaints, we published an assessment guide detailing the new procedures and the tools we use when considering mortgage endowment complaints. This guide not only helps speed up the process for the cases we deal with, it also enables firms to understand our approach and the amount of compensation we may award, making it easier for them to settle cases satisfactorily themselves, without the need for our involvement.
- 3.7 a pre-N2 focus on communication with the industry, including the publication of *ombudsman news*** Our aim as far as the industry is concerned has been to ensure N2 brought no surprises. To help firms and consumer bodies fully understand the changes coming at N2, we organised training events, workshops and seminars. We produced a

range of technical briefing notes and updates and helped firms distribute over 1.5 million copies of our new complaints leaflets. In addition, we launched a monthly publication, *ombudsman news*, containing case studies and commentaries on topical subjects.

3.8 the introduction of our new business process and case-handling system

Our new unified case-handling system was implemented on time and within budget during the summer of 2001. At the same time, we introduced a new, consistent business process across the case-handling divisions, enabling us to improve our productivity and service quality levels. It will also give us the flexibility to move staff across divisions, where necessary, if there are changes in the balance of the workload.

3.9 an emphasis on complaint prevention Our technical advice desk now deals with around 400 calls a week, mostly from professional complaint-handlers in firms. Firms report that the advice we provide enables them to resolve many complaints themselves, without the need for our direct involvement. In addition, staff in our customer contact division (the division that deals with customers' initial telephone calls or letters) do not simply answer enquiries and process complaints. They actively seek opportunities to resolve disputes at this early stage. Where this can be done, we avoid the need to pass on the complaints to our case-handling divisions for investigation. This helps reduce costs for firms and for ourselves.

3.10 A summary of current forecast workload is as follows:

summary of workload

	2000/01 Actual	2001/02 Budget	2001/02 Forecast
Cases at 1 April	11,800	15,300	14,700
New cases	31,300	38,000	38,000
Closed cases	28,400	38,500	38,500
Cases at 31 March	14,700	14,800	14,200
No of weeks' work outstanding	20	22	20
Productivity *	3.3	3.5	3.7

* Productivity is defined as the number of cases closed per case-handler per week

new cases

- 3.11** At the end of November 2001, the number of new cases was 29% higher, on a comparable basis, than in the previous year. This rate of increase over last year is unlikely to continue for the rest of the year; there was a sharp increase in new cases in the second half of last year, which has now flattened off.
- 3.12** If we simply extrapolate the current average weekly new case figure for the balance of the year, we come to a full year figure of around 39,000. However, we are seeing a slowing down in the rate of increase in new cases. Our current best estimate is therefore in line with the original forecast figure of 38,000, which we gave in last year's Plan & Budget.

productivity and timeliness

- 3.13** At the end of November 2001, our cumulative case closure figure was 24,900. This averages at just over 700 a week. However, this period includes the introduction of the new case handling system. If we just look at the 10 weeks from the beginning of October 2001, the average weekly closure rate has been around 780, representing a productivity rate of around 3.8 cases per case-handler each week. This compares with the average productivity rate last year of around 3.3 and signifies an excellent recovery rate so soon after the introduction of the new process and system.
- 3.14** At current levels, we should achieve a closure figure in the range of 37,500 to 38,500. Clearly, if the level of new cases falls sharply in the last quarter of the year, there may be a constraint on the number of cases that can be closed.
- 3.15** As far as timeliness is concerned, our target in 2001/02 is to complete 70% of cases within six months of the date when we formally accepted them as eligible cases. At present, we are exceeding this target – completing 73% of cases within this timescale. However it must be borne in mind that the closure time is also affected by factors outside our control, for example, awaiting replies from consumers, member firms, or technical experts.

expenditure

- 3.16** The approved 2001/02 operating cost budget for the Financial Ombudsman Service (before financing) was £26.5m. We expect costs for 2001/02 to be in line with this budget. A summary is set out in appendix D.

unit cost

- 3.17** The target unit cost for 2001/02 was £688 (operating costs divided by case closures). At present we are still on course to achieve this figure. If there were a sharp falling away of new cases in the last few months of the year, that could result in our failing to attain this target.

A summary of the current forecast for 2001/02 is as follows:

	Half Year £m	Budget £m	Forecast £m
Operating costs	12.9	26.5	26.5
Financing costs	0.4	1.1	1.1
Total costs	13.3	27.6	27.6
Case closures		38,500	38,500
Unit cost*		£688	£688
<i>*Unit cost is calculated before financing charges</i>			

3.18 If new cases fell away sharply in the final quarter, we would seek to make short-term savings in order to get as close as possible to the target of £688.

conclusion

3.19 In both our process and our decisions, we have tried to balance the importance of speedier complaint-resolution with the need to provide a quality service. With the aim of achieving this, we have slightly reduced the rate of increase in our productivity and timeliness targets for 2002/03.

chapter four business plans

‘we plan to improve the business process in the light of practical experience, and to further refine our benchmarks for quality and timeliness’

introduction

- 4.1** The first year of our operation was concerned with laying the foundations for the combined ombudsman service. The current year, as we have already noted, has seen us implementing a new business process and unified case-handling system and achieving an increased level of productivity and improved timeliness – despite the disruption. Our key tasks for 2002/03 will be to stabilise the case-handling system and business process following the rapid change of the last two years, and to focus on quality and timeliness.

key tasks

4.2 key tasks in the coming year

a) establish the level of service that users expect of us and refine our targets in the light of this research

We have begun by undertaking a consumer satisfaction survey and by researching the demographic profile of our customers. We will combine these results with other research on the financial services industry and use the information we gain to help us establish quality benchmarks.

b) further develop our new business process and system

Having brought together the business processes from the old schemes and implemented a new unified case-handling system, we plan to improve the business process in the light of practical experience, and to further refine our benchmarks for quality and timeliness. We also propose to enhance our new case-handling system, giving it greater functionality, and adding document imaging.

c) flexible working

As we develop as a single operation, we will need the flexibility to move resources across the organisation to deal efficiently with changes in the balance of our workload. We have begun a project to review our structure and working practices to ensure we perform as efficiently as possible. This will involve a continuing investment in staff training and effective 'knowledge management'.

d) independent assessor

The board of the Financial Ombudsman Service has appointed an independent assessor, Sir Edward Osmotherly, to deal with any complaints we have not been able to resolve concerning the service we provide when handling complaints against firms (our standards of courtesy, efficiency, timeliness *etc*). We are committed to operating a swift and open process for dealing with such complaints, and the feedback they provide will help us improve the way in which we operate.

e) service quality and best practice We are undertaking a project that will look at all aspects of the way we work, taking the best practice from each of our divisions, and setting new targets in relation to the way we handle complaints. This will include the usual indicators such as timeliness and productivity, but will also focus on the clarity and accessibility of the way we communicate.

f) training and development We continue to make training and development a priority. By the end of 2001/02, we expect to have undertaken the equivalent of approximately 2,500 days of training. This includes training on the new rules, use of new technology and managing change. We are now able to offer accredited management development for new managers and, as part of our commitment to equality of opportunity for all our employees and the users of our service, we have undertaken diversity awareness training. We intend to continue with a high emphasis on training, and will focus in particular during the coming year on developing the skills of managers and of those whose work entails resolving complaints over the telephone.

conclusion **4.3** The key task has been to keep the level of productivity above those of the old schemes, while introducing the new case-handling system and business process. We have done this at a time when the numbers of new cases have been rising significantly. The challenge now is to harness the new system and process to give improvements in the quality and timeliness of our work.

chapter five
complaint
trends

‘it is difficult to predict the
pattern of complaints’

new complaints

5.1 introduction

Our working assumption for 2002/03 is that the overall number of new complaints will be at a similar level to the current year. We have tested two additional scenarios, one assuming the number of new cases will be 10% above that for the current year 2001/02 and another assuming it will be 10% lower. A summary of the latest forecast and budget is as follows:

New complaints	2000/01 Actual	2001/02 Forecast	2002/03 Nil Growth	2002/03 Increasing Complaints	2002/03 Falling Complaints
Insurance	6,559	7,000	7,600	8,400	6,900
Banking and loans	6,153	6,500	7,000	7,750	6,300
Investment	18,635	24,500	22,900	25,350	20,800
Total	31,347	38,000	37,500	41,500	34,000

5.2 It is difficult to predict the pattern of complaints. The last few weeks of 2001 have seen a marginal slowdown in the number of complaints. Whether this is a temporary blip or a continuing trend is hard to judge at this stage. We summarise below the external and internal factors which may determine the pattern of complaints. We also summarise the current position on the Voluntary Jurisdiction.

external factors

5.3 A number of external factors can affect the level of complaints. These include:

- a) **industry action** Firms may be more proactive in dealing with complaints, resolving them successfully before the stage where they would otherwise be referred to the ombudsman. Both we and the FSA have been encouraging this approach. Our monthly publication, *ombudsman news*, sets out our general approach to particular types of cases and provides firms with useful guidelines. The FSA complaint-handling rules that came into force at N2 should improve industry standards.
- b) **mortgage endowments** Firms' actions in sending out re-projection letters will have a critical effect on the level of new complaints in 2002/03. At present, we are assuming some increase in complaints resulting from re-projections in the first quarter of 2002.
- c) **N2** We have always assumed that there will be some increase in complaints from the publicity surrounding N2.

d) falling stock markets and investment returns This may well lead to an increasing number of complaints. In particular, it is likely that mortgage endowment re-projections will show larger shortfalls.

internal factors

5.4 There are also internal factors that will influence the level of cases.

5.5 new business process The staff in our customer contact division receive and screen complaints before they become 'cases' (and therefore chargeable) and are passed on to a case-handling division. We are training these staff to resolve relatively straightforward complaints at the earliest possible opportunity. This may help to reduce the future level of chargeable cases.

5.6 new eligibility rules The new rules widen the scope of eligible complaints in a number of respects. Many more firms come within our scope and new activities (insurance of small businesses, and securities and share dealing) come within an ombudsman scheme for the first time. This could have an upward impact on case numbers.

5.7 new rules definition of chargeable case The main impact of the new case-fee arrangements will only be felt from April 2002. Cases will become chargeable at a different (and – by comparison with some former schemes – earlier) point in the process. Our best estimate is that this will initially have an upward impact, possibly followed by a decrease as firms get used to the new arrangements. Some volatility is expected.

voluntary jurisdiction

5.8 We had expected to be extending the Voluntary Jurisdiction to new sectors and had envisaged that this would have a business and financial impact in the year 2002/03. However, in December 2001 HM Treasury announced major policy decisions that will affect our plans. It is clear that general insurance intermediaries and mortgage brokers will eventually fall within our Compulsory Jurisdiction. Whether they may be brought within the Voluntary Jurisdiction before then remains to be considered. We had expected mortgage lenders to join the Compulsory Jurisdiction in mid-2002 but it will now be delayed. However, our Voluntary Jurisdiction is open to such lenders and we will welcome those who wish to join.

a) consumer credit firms We intend to discuss with trade associations and regulators the possibility of consumer credit members joining the Voluntary Jurisdiction.

b) insurers and banks from the European Economic Area (EEA)

We have consulted on allowing EEA insurers and banks that sell into the UK consumer market to join the Voluntary Jurisdiction. We expect the immediate effect will be to allow five or six insurers, mainly based in Ireland, to continue to be covered by the ombudsman service.

consumer contact division

5.9 customer contact division (CCD)

We expect the number of consumers contacting us by telephone or letter to rise by 11% this year. However, we expect the level of contact to remain at a similar level next year.

	2000/01 Actual	2001/02 Forecast	2002/03 Budget
Calls to dedicated telephone lines in our customer contact division	221,000	250,000	250,000
New written complaints	67,000	70,000	70,000

5.10 We have made a considerable investment in skills training for our consumer consultants and are beginning to see the benefits of this expenditure. Our intention is to resolve as many complaints as possible in our customer contact division, to avoid them becoming chargeable cases. We are at present developing a range of key indicators to measure our performance in this area.

insurance division

5.11 insurance division – analysis of new complaints

5.12 The increase in complaints has been reasonably stable over the last few years.

	2000/01 Actual	2001/02 Forecast	2002/03 Budget	% Increase 2001/02 over 2000/01	% Increase 2002/03 over 2001/02
Motor	1,989	1,800	1,900	(10)	6
Buildings/contents	1,795	1,850	1,950	3	5
Loan protection	711	750	850	5	13
Travel	778	800	900	3	13
Other	1,286	1,800	2,000	40	11
Total	6,559	7,000	7,600	7	8

5.13 The expected reduction in the number of complaints involving motor insurance reflects our intention to resolve more straightforward issues, such as motor valuation, at the initial contact stage. We expect a slight increase in loan protection complaints to reflect the probable increase in claims during an economic slow down. Travel claims have been rising for some time and the terrorist attacks in the USA are likely to exacerbate the position.

5.14 The increase in other complaints this year reflects mainly the inclusion, for the first time, of critical illness and permanent health insurance complaints – these will account for about 500 cases this year. In addition, a growth in the number of people taking out medical expenses policies has driven an increase in the number of complaints about these policies. In 2002/03 we expect to see the first commercial disputes coming forward for resolution. The impact of this is uncertain at present but we have assumed that we will deal with no more than 400 cases on commercial disputes in the first year.

5.15 banking & loans division – analysis of new complaints

banking and loans division

	2000/01 Actual	2001/02 Forecast	2002/03 Budget	% Increase 2001/02 over 2000/01	% Increase 2002/03 over 2001/02
Current accounts	793	1,050	1,040	32	(1)
Deposit/Savings accounts	1,679	1,450	1,600	(14)	10
ISAs	0	30	40	–	33
Loans secured on land	2,499	2,950	2,900	18	(2)
Other loans	664	620	870	(7)	40
Other	518	400	550	(23)	38
Total	6,153	6,500	7,000	6	8

5.16 The increase in the number of new complaints has begun to level off compared with previous years.

5.17 The current year has so far seen a reduction in the number of complaints about TESSAs, but this has been offset by complaints about dual variable-rate mortgages and downgraded accounts. Individual Savings Accounts

(ISAs) have yet to be the source of a significant number of complaints and the ISA complaints we do receive tend to involve investment-based ISAs, so they are dealt with in our investment division.

- 5.18** It is possible that the new time limits relating to the transfer of bank accounts will give rise to additional complaints.
- 5.19** Credit unions will join the Financial Ombudsman Service from 1 July 2002, which may produce additional complaints relating to deposit/savings accounts. We are forecasting that the number of mortgage complaints will remain fairly stable.
- 5.20** Complaints about 'other loans' are likely to increase, particularly from small businesses, especially if there is a downturn in the UK economy.

5.21 investment division – analysis of new complaints

investment division

	2000/01 Actual	2001/02 Forecast	2002/03 Budget	% Percentage 2001/02 over 2000/01	% Increase 2002/03 over 2001/02
Mortgage endowment	9,067	13,900	12,400	53	(11)
Endowment/whole life	3,363	2,400	2,400	(29)	0
Personal pensions	2,545	4,800	4,500	89	(7)
PEP/ISA	268	1,100	1,300	310	18
Other	3,392	2,300	2,300	(32)	0
Total	18,635	24,500	22,900	31	(7)

- 5.22** During this year we have felt the full impact of the increase in complaints relating to mortgage endowments which, at their peak, accounted for approximately 60% of all new complaints. These complaints now account for approximately 50% of all new complaints and we expect a further reduction in 2002/03, as most firms have implemented procedures to streamline their complaints-handling in accordance with the regulator's guidance. However, as mentioned earlier, the new round of re-projection letters that firms will be issuing to policyholders this year is likely to result in further complaints to the ombudsman.

5.23 Following the House of Lords decision on the treatment of Equitable Life guaranteed annuity rate (GAR) pension policies, we have seen an increase in complaints from consumers with non-guaranteed policies from companies *other than* Equitable Life, which have also sold GAR policies.

5.24 We expect pension review complaints to continue at about the same level as in 2001/02 and they are included with all other personal pension complaints.

conclusion

5.25 Against this uncertain background, we have decided simply to assume the similar forecast figure as the current year. However, we have also assessed the impact of two alternative scenarios – firstly, a higher growth in new cases of 10%, and secondly, a reduction in new cases of 10%.

chapter six
productivity,
timeliness and
service quality

‘we have increased our
productivity and
improved our timeliness’

introduction

- 6.1 The key feature of the current year has been that we have increased our productivity and improved our timeliness, despite the inevitable disruption caused by the introduction in June 2001 of our new unified case-handling system and the accompanying changes in our work processes needed for N2. For 2002/03 our focus will be on making further improvements to the quality and timeliness of our service.

key assumptions

- **increase in productivity** An increase in productivity to 4.1 cases per case-handler each week. This represents an overall 25% increase in productivity over the three years 2000/01 to 2002/03 – from 3.3 cases per case-handler each week in 2000/01 to a planned 4.1 figure next year.
- **increase in closures** Despite the reduction in the number of case-handlers, the improvement in productivity results in an increase in closures from 38,500 to 40,000.
- **improvements in timeliness** An improvement in the timeliness targets for 2002/03 – 75% of cases should be completed within six months of the date when we formally accepted them as ‘cases’ – at present our target is 70% of cases. We will also aim to close 100% of cases within 12 months and will report to the board all cases which exceed this target. It is important to emphasise that the length of time it takes to close a case often depends on the speed with which customers and firms respond to our enquiries.
- **reduction in work in progress** As part of the drive to improve quality, it is critical to reduce the amount of work in progress to a lower level. This allows us to improve timeliness and document management. The base budget assumes a ‘work in progress’ figure of 11,700 by March 2003. This represents a 2,500 fall on the estimated March 2002 figure of 14,200.
- **a step-up in internal service-quality standards** The drive for increased productivity and the introduction of new processes has led to some inevitable ‘frayed edges’ in terms of internal quality benchmarks. From the beginning of the next financial year, we intend to introduce formal internal quality measurements, with audit checks on decisions and process.

alternative scenarios

- 6.2 In the two alternative scenarios, we have made the following assumptions:
- **higher growth in new complaints** If new complaints rise by 10% to 41,500, our assumption is that case closures will be 43,500, compared with the base assumption of 40,000.
 - **a reduction in new complaints** If new complaints fall by 10% to 34,000, our assumption is – given the work in progress at the beginning of the year – that case closures will be 38,000.

summary forecasts

6.3 A summary of the three closure scenarios is set out in this and the following paragraph. Closure forecasts and productivity levels are as follows:

Case closures	2000/01 Actual	2001/02 Forecast	2002/03 Nil Growth	2002/03 Increasing Complaints	2002/03 Falling Complaints
Insurance	7,138	7,400	7,900	8,600	7,500
Banking and loans	6,056	6,600	8,100	8,800	7,700
Investment	15,206	24,500	24,000	26,100	22,800
Total	28,400	38,500	40,000	43,500	38,000
Productivity*	3.3	3.7	4.1	4.1	4.1

**Productivity is defined as the number of cases closed per case-handler each week*

6.4 The current and proposed timeliness targets for the three scenarios, together with the year-end levels of work in progress, are set out below.

	2000/01 Actual	2001/02 Forecast	2002/03 Nil Growth	2002/03 Increasing Complaints	2002/03 Falling Complaints
Numbers of cases at year end	14,700	14,200	11,700	12,200	10,200
Cases at year end:					
number of weeks' work	24	20	16	16	17
Closed within 6 months	65%*	73%	75%	75%	80%
Closed within 12 months	90%*	95%	100%	100%	100%

**Estimated*

conclusion

6.5 Whether new complaints fall, rise or remain relatively static, we aim to increase productivity, improve timeliness and achieve a reduction in the level of work in progress. This will be accompanied by the introduction of formal quality control benchmarks for decisions and process.

chapter seven
cost
effectiveness

‘for 2002/03 we
estimate that our unit
cost will remain at
around the same level in
money terms’

introduction

7.1 Our plan is to build a cost-effective and responsive ombudsman service. An increasing workload will require additional resources, but we intend to measure our cost effectiveness by looking at unit costs on a year on year basis. We gave a commitment in last year's *Plan & Budget* that the unit cost would not rise above £688. If volumes fell, we aimed to make sufficient savings to keep to our agreed target. But if this should happen mid-way through the financial year, we would need a period of time to achieve those savings. This remains our approach.

measurement of unit cost

7.2 We calculate the current measure of unit cost by taking the aggregate costs of the organisation (before financing costs) and dividing by the number of cases closed in that year. We noted in last year's *Plan & Budget* that this can be a misleading measure of cost effectiveness, particularly if we resolve a higher number of complaints in our customer contact division so they do not go on to become chargeable cases.

7.3 Since the customer contact division plays a key role in settling cases at an early stage (before they become chargeable), we are at present developing a range of key indicators to measure our performance in this area.

unit costs

7.4 In 2001/02 we expect the unit cost to fall from the 2000/01 figure of £753 to around £688, which is in line with the published budget. For 2002/03, we estimate that the unit cost will remain around the same level in money terms, which represents a fall of £20 in real terms. This is after absorbing the improved timeliness and service efficiency standards described above and the staff salary increase.

7.5 The unit cost is made up as follows: -

Build-up of the cost per case	Actual 2000/01 £	Forecast 2001/02 £	Budget 2002/03 £
Case-handling direct costs	387	354	344
Cost of complaints prevention			
customer contact division	74	66	65
technical advice/communications	25	23	22
Other			
support costs	90	70	69
management & board	24	16	15
best practice/management information system	0	9	12
premises & facilities	100	96	95
depreciation	53	54	66
Total	753	688	688

7.6 The fall in unit cost results from a combination of a productivity gain by the case-handling divisions and a volume gain from the spreading of support costs and premises costs over a wider volume of case closures.

7.7 The impact on unit costs of the two alternative scenarios would be as follows:

a) higher complaint levels The unit cost would fall to around £650, due to the volume gain from spreading fixed costs over additional case closures.

b) falling complaint levels As soon as it became clear that this was the position, we would have two options. We would consult the FSA and other stakeholders on which option to pursue. First, we could cut costs aggressively to maintain the £688 level – although the later the position became clear, the more difficult this would be. Second, we could allow the unit cost to rise to just above £700 (still below the £688 in real terms) in anticipation of the extended jurisdiction over the coming years.

conclusion

7.8 We are committed to our unit cost and productivity targets and believe they are entirely compatible with our desire to provide a quality service. We would like to hear of any additional measures we could usefully use.

chapter eight

budget 2002/03

‘our target was to bring our unit cost below that of the previous schemes during the year 2002/03. We have achieved this a year earlier than expected’

introduction

- 8.1** In last year's budget we saw 2001/02 as the transitional year and 2002/03 as the year in which our customers and the industry would see genuine returns in terms of quality and cost effectiveness.
- 8.2** Our target was to bring our unit cost below that of the previous schemes during the year 2002/03. We have achieved this a year earlier than expected. For 2002/03, with no increase in unit cost after absorbing salary increases and an increased depreciation charge, we aim to improve our service quality.
- 8.3** We expect expenditure for 2001/02 to be in line with budget at £27.6m. The budget for 2002/03 is £28.2m, an increase of 2.2%. The cost increase has been kept below the rate of inflation by holding the casework divisions to their unit cost level in 2001/02, and the support divisions to their cash spend during that year.

summary expenditure forecast and budget

- 8.4** A summary is as follows:

	2001/02 Forecast £m	2002/03 Budget £m
Staff and staff-related costs	19.4	19.9
Professional fees	0.5	0.5
IT running costs	0.6	0.5
Premises & facilities	3.5	3.5
Other costs	0.4	0.5
Depreciation	2.1	2.6
Operating costs	26.5	27.5
Financing costs	1.1	0.7
Total costs	27.6	28.2
Case closures	38,500	40,000
Unit cost*	£688	£688

**Unit cost is calculated before financing charges*

head count

- 8.5** Increasing productivity should allow us to reduce the 'full time equivalent' headcount by 12 from the previous year's budget to 458.

	2001/02 Budget	31 Oct 2001 Actual	31 March 2003 Budget
customer contact/enquiries	84	82	87
best practice/management information system unit	6	6	9
investment casework	179	171	161
insurance casework	61	59	61
banking and loans casework	65	61	61
legal casework	10	10	10
company secretarial/library	5	5	5
finance/IT/HR/facilities	41	42	45
technical advice/communications	15	15	16
management	4	3	3
Total	470	454	458

- 8.6** The reason for the anticipated increase in support staff during 2002/03 is due to the change in the way we are funded. The Financial Ombudsman Service is now responsible for invoicing firms directly for the levy and case fees and for collecting these amounts from them. (In the past two years the schemes making up the new ombudsman service paid service charges to the Financial Ombudsman Service.) There is therefore a need for additional strength in finance, IT and credit control. In addition, we propose to begin charging firms for the new complaints leaflets, which were provided free for N2.

alternative scenarios

- 8.7** In the two alternative scenarios the impact would be as follows:

a) higher complaint levels In this situation, total costs before interest would be £0.6m higher than the base budget – £28.1m instead of £27.5m. Staff numbers would be 21 higher than the base budget – 479 instead of 458.

b) falling complaint levels In this situation, costs would be £0.6m lower than the base budget – £26.9m instead of £27.5m. Staff numbers would be 24 fewer than the base budget – 434 instead of 458.

voluntary jurisdiction

- 8.8** We are required to show the allocation of costs between the Compulsory and Voluntary Jurisdictions. In the year to March 2003, the costs of the Voluntary Jurisdiction are expected to be immaterial at less than 1% of the total expenditure.

cashflows

- 8.9** The FSA guaranteed an overdraft facility of £25m. But after we reviewed this figure in the light of our experience, this limit was reduced to £18m. However, the facility was extended by one year because N2 was delayed. Part of the borrowing is attributable to the costs of establishing the Financial Ombudsman Service, some £4.9 million. We intend to eliminate this overdraft over the next eight years, by collecting our establishment costs levy and reducing our capital expenditure in relation to our depreciation charge. The expected cash flows are as follows:

	2001/02	2002/03
	£m	£m
Total costs before depreciation	(25.5)	(25.6)
Capital expenditure	(2.6)	(1.5)
Establishment costs	(0.4)	
Lease premium	(0.6)	
Cash outflow	(29.1)	(27.1)
Income from schemes	30.5	
Levies/case fees	1.2	27.3
Establishment costs		1.5
Net cash inflow	2.6	1.7
Opening bank balance	(14.3)	(11.7)
Closing bank balance	(11.7)	(10.0)

- 8.10** The budget for capital expenditure for 2002/03 includes £1.0m for computer development and £0.5m for computer infrastructure. We propose to continue developing our case-handling system by adding document image management and an intranet/extranet capability. We will also need to enhance our infrastructure so that it will be suitable for our longer-term development programme.

conclusion

- 8.11** Given that inflation is expected to rise by around 2.0% our budget remains stable in real terms, rising in absolute terms from £27.6m to £28.2m – no more than 2.2%. The unit cost also falls in real terms, remaining constant in absolute terms at £688,

chapter nine
tariff and case
fee information

‘this is the first year that the
Financial Ombudsman
Service will be collecting the
levy directly from firms’

introduction

9.1 This is the first year that the Financial Ombudsman Service will be collecting the levy directly from firms. As agreed during the consultation on the fee raising rules, 50% of the costs will be raised by a levy on firms and 50% by case fees. The total budget is therefore divided into two amounts of £14.1m.

general levy

9.2 The tariff rates in appendix A are for information only. They are presently part of a FSA consultation document (CP119) and any comments should be sent to the FSA by 21 February 2002.

9.3 Financial services firms are grouped in a total of 15 different industry blocks, based on provisional data provided by the FSA. The levy has been apportioned across these blocks, according to the number of case-handling staff assigned to deal with cases that fall in each relevant block. During the consultation period we intend continually to refine our fee data which may give rise to a change, perhaps materially, in the tariff rates.

9.4 As mentioned in the policy document, *Dispute Resolution: the Complaints Sourcebook*, we intend to send out estimated invoices in March/April 2002, based on the above tariff, which we will revise in the autumn to take account of the tariff data received from the FSA.

9.5 In addition to the annual budget of £28.2m, we intend to recover one third of our £4.9m establishment costs. Establishment costs will be collected from firms over a three-year period until 2004/05 (£1.63m per annum) and will be charged in proportion to the general levy. These rates are also subject to consultation in CP119 as above.

case fee

9.6 The case fee will be the total to be raised divided by the number of expected case closures. Our current estimate is £360 (see appendix B), made up of £344 (50% of the unit cost) plus £10 for interest and £6 to cover contingencies such as bad debts.

9.7 We have also provided details of our proposed tariff rates for the Voluntary Jurisdiction (appendix C). Where there is a direct comparison, such as in the banking and loans block or general insurance, we will use the same rate as for the Compulsory Jurisdiction. In other cases we will use an appropriate factor. The Voluntary Jurisdiction blocks are at present limited to: firms that were members of a predecessor scheme on 30 November 2001, but which are not regulated by the FSA for events from 1 December 2001 onwards (the activities covered are the same as those covered by the predecessor schemes); mortgage lenders that are

not currently regulated by the FSA for complaints about events before or after 1 December 2001 (but limited to lending money secured by a charge on land, plus any ancillary advice and services); and certain non-UK financial services companies based in the EEA but trading in the UK.

conclusion

- 9.8** The methodology for charging our levy and case fees has been the subject of thorough consultation. However, we are committed to consulting each year on the method of determining the tariff, the tariff rates and our case fee.

chapter ten
new standard term
for funding the
voluntary jurisdiction

introduction

10.1 The joint FSA/Financial Ombudsman Service Policy Statement on CP74 and CP99 included the 'final' text of the funding rules in DISP 5. However, the rules could not be made at that time; they were subject to consultation on the specific figures to be included in the fee-instrument in DISP 5 Annex 1R. This sets the tariff-rates for general levy purposes and the case fees that firms must pay.

The consultation on those figures is being conducted through the FSA's Consultation Paper CP119 which is being issued simultaneously with this paper. The funding of the Voluntary Jurisdiction will be achieved by applying relevant funding rules in DISP 5 to the firms that join the Voluntary Jurisdiction. However, the Standard Term which will apply those rules can only be made at the same time as the funding rules in DISP 5.

10.2 Appendix E provides the proposed text of the new Standard Term.

commentary on the proposed Standard Term

10.3 The rules and guidance identified by each sub-paragraph of the proposed Standard Term, as set out below, are applied to Voluntary Jurisdiction participants (as part of their agreement to be subject to the Voluntary Jurisdiction) as if they were authorised firms – but subject to the minor variation where stated:

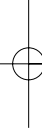
- **DISP 4.2.12R(1)** This sub-paragraph applies DISP 5.4.6R, so that Voluntary Jurisdiction participants will be obliged to pay the general levy.
- **DISP 4.2.12R(2)** This sub-paragraph applies DISP 5.4.8R, so that the calculation of the general levy against Voluntary Jurisdiction participants is made in exactly the same way as for the Compulsory Jurisdiction.
- **DISP 4.2.12R(3)** This sub-paragraph applies DISP 5.5.1R, so that a Voluntary Jurisdiction participant must provide the Financial Ombudsman Service with a statement showing the total amount of relevant business that it conducted in the previous year to 31 December, in relation to the tariff-base for each of the industry blocks into which the participant falls.
- **DISP 4.2.12R(4), (5) and (6)** These three sub-paragraphs apply DISP 5.6.1R, DISP 5.6.6R, DISP 5.7.5R and DISP 5.7.6R, so that Voluntary Jurisdiction participants will be obliged to pay standard and special case fees, and the supplementary levy for establishment costs of the Financial Ombudsman Service.
- **DISP 4.2.12R(7)** This sub-paragraph applies the rules relating to payment of fees in DISP 5.8.1R to DISP 5.8.6R and DISP 5.8.8R and DISP 5.8.9R, so that the general levy and supplementary levy are paid annually or quarterly by direct debit; standard and special case fees for chargeable cases are

payable within 30 days of the date of invoice; and interest at 10% per annum will be payable on outstanding invoices. If it appears to the FSA or to the Financial Ombudsman Service that there are exceptional circumstances, any fee payable may be remitted in full or part or refunded.

- **DISP 4.2.12R(8)** This sub-paragraph applies DISP 5.9.1R and DISP 5.9.2R, which are rules making provision for apportioning the general levy and the supplementary levy when a Voluntary Jurisdiction participant joins the Voluntary Jurisdiction part way through a financial year.
- **DISP 4.2.12R(9)** This sub-paragraph applies the whole of DISP 5 Ann1R, which is the annex to the funding rules specifying the amounts payable.

conclusion

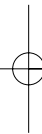
- 10.4** In relation to the cost of membership of the Voluntary Jurisdiction, Voluntary Jurisdiction participants will pay on the same basis as authorised firms in the Compulsory Jurisdiction.



appendix A

general levy table

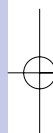
This table is included for information only and is part of the FSA's consultation paper 119 (CP119) which can be found on the FSA website.



industry block	general levy			supplementary levy		
	tariff rate(£)	min levy	block total	tariff rate	min levy	block total £ contribution by block
1	£0.01573 (Per relevant account)	£250	£3,060,100	£0.0018 (Per relevant account)	£29	£354,000 21.72%
2	£0.1593000 (Per £1000 relevant annual gross premium income)	£250	£2,515,769	£0.0184 (Per £1000 relevant annual gross premium income)	£29	£291,000 17.87%
3	N/A	N/A	£201,100	N/A	£23,000	£23,000 1.43%
4	£0.0980000 (Per £1000 relevant adjusted annual gross premium income)	£100	£5,011,049	£0.013000 (Per £1000 relevant adjusted annual gross premium income)	£12	£580,000 35.59%
5	£0.00132000 (Per £1000 relevant funds under management)	£100	£951,915	£0.000015 (Per £1000 relevant funds under management)	£12	£111,000 6.76%
6	£0 (Per £ relevant annual gross income)	£100	£32,600	N/A (Per £ relevant annual gross income)	£12	£3,767 0.23%
7	£100 (Per relevant trader)	£100	£163,000	£12 (Per relevant trader)	£12	£19,000 1.16%
8	£362 (Per relevant approved person)	£362	£668,487	£42 (Per Relevant Approved Person)	£42	£77,210 4.75%
9	£203 (Per relevant approved person)	£203	£1,290,688	£23 (Per relevant approved person)	£23	£150,000 9.17%
10	£100 (Per relevant approved person)	£100	£30,400	£12 (Per relevant approved person)	£12	£3,511 0.22%
11	£0 (Per £ relevant annual commission or fee income)	£100	£20,400	N/A (Per £ relevant annual commission or fee income)	£12	£2,357 0.14%
12	£105	£105	£88,956	£12 (Per relevant approved person)	£12	£10,274 0.63%
13	£0 (Per £ relevant annual gross premium income)	£50	£1,250	N/A (Per £ relevant annual gross premium income)	£6	£144 0.01%
14	£0 (Per £ gross assets)	£50	£31,900	N/A (Per £ gross assets)	£6	£3,686 0.23%
15	£0 (Per £ relevant annual gross premium income)	£50	£12,300	N/A (Per £ relevant annual gross premium income)	£6	£1,421 0.09%
Total - all blocks			£14,079,914			£1,630,370 100.00%

appendix B

case fees



Case fee (Compulsory Jurisdiction)

Standard case fee	£360
Special case fee	£720

See chapter 5.6 (case fees) of the FSA Handbook, Module DISP, for the definitions of standard case fees and special case fees.

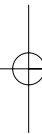
appendix C

voluntary jurisdiction tariff



Financial Ombudsman Service Industry Block and Business Activity	Tariff base	Tariff rate	Minimum levy	Establishment rate	Minimum levy	Case fee
1V Mortgage lenders and administrators	Number of relevant accounts	£0.01573	£250	£0.0018	£29	£360
2V Firms undertaking insurance activities subject only to prudential regulation	Relevant annual gross commission income	£0.1593 per £1,000	£250	£0.0184 per £1,000	£29	£360
3V Intermediaries	Relevant annual gross commission or fee income	Nil	£200	Nil	£23	£360
4V Firms falling into neither of the above categories	Relevant annual gross premium income	Nil		Nil		£720

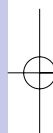
appendix D
forecast 2001/02
and budget 2002/03
expenditure



	Actual 6 months to 31/10/01 £m	Budget 2001/02 £m	Forecast 2001/02 £m	Budget 2002/03 £m
Staff and staff-related costs	9.5	19.6	19.4	19.9
Professional fees	0.3	0.5	0.5	0.5
IT running costs	0.3	0.6	0.6	0.5
Premises and facilities	1.6	3.3	3.5	3.5
Other costs	0.2	0.4	0.4	0.5
Depreciation	1.0	2.1	2.1	2.6
Operating costs	12.9	26.5	26.5	27.5
Financing costs	0.4	1.1	1.1	0.7
Total costs	13.3	27.6	27.6	28.2
Case closures		38,500	38,500	40,000
Unit cost*		£688	£688	£688
<i>*Unit cost is calculated before financing charges</i>				

appendix E

funding



4.2.12R The following rules in DISP 5 apply (subject to DISP 4.2.13R) to VJ participants as part of their agreement to be subject to the Voluntary Jurisdiction as if they were authorised firms, but subject to the variations stated in each case.

(1) DISP 5.4.6R (general levy) subject to substituting the words 'Voluntary Jurisdiction' for 'Compulsory Jurisdiction';

(2) DISP 5.4.8R (calculation of general levy);

(3) DISP 5.5.1R (information) subject to substituting the words 'FOS Ltd' for 'FSA';

(4) DISP 5.6.1R (standard case fee);

(5) DISP 5.6.6R (special case fee);

(6) DISP 5.7.5R and DISP 5.7.6R (supplementary levy for establishment costs);

(7) DISP 5.8.1R to DISP 5.8.6R and DISP 5.8.8R and DISP 5.8.9R (payment);

(8) DISP 5.9.1R and DISP 5.9.2R (joining the Financial Ombudsman Service);

(9) DISP 5 Ann 1R (fees payable).

how to contact the
Financial Ombudsman Service



write to us

Financial Ombudsman Service
South Quay Plaza
183 Marsh Wall
London E14 9SR



phone us

0845 080 1800



email us

complaint.info@financial-ombudsman.org.uk



look at our website

www.financial-ombudsman.org.uk

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