the Financial Ombudsman Service

corporate plan & 2006/07 budget

about this document

The Financial Ombudsman Service year runs from 1 April to 31 March. Each June we publish our annual review, recording what has happened over the past year. But in this document – our *corporate plan & budget* – we look ahead. We consult on our workload forecasts and proposed budget for 2006/07. We also look further ahead, sharing with our stakeholders our agenda for the next three years. Where appropriate, we will consult specifically about any significant changes that entails.

responses

We invite your views. We would particularly welcome comments on our workload forecasts and proposed 2006/07 budget by Friday 17 February 2006. Please send any comments to:

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1 introduction to corporate plan

The work of the Financial Ombudsman Service has grown at an unprecedented rate since we were established by law as a unified service for resolving disputes between consumers and financial firms.

In 1999/2000, just before our predecessor complaints-handling schemes were brought together to form the Financial Ombudsman Service, these schemes handled around 25,000 cases in total – at an average cost per case of around £750.

In 2004/05, only five years on, the Financial Ombudsman Service handled over 110,000 cases – at an average cost per case of under £500.

To cope with the increasing workload our staff has grown from about 350 to about 1,000, which makes us by far the largest ombudsman scheme worldwide.

We have coped well with this massive growth. This is thanks to the solid foundations that we and the Financial Services Authority (FSA) established at the outset – in consultation with our stakeholders – as well as to our continuing flexibility of approach, which has enabled us to adapt to changing circumstances.

Our overriding priority has been coping with this rapid growth without compromising the quality of our work. But there is now a realistic expectation that our workload will begin to plateau.

Future increases in some areas (including a wider jurisdiction in consumer credit) are likely to be balanced by future reductions in mortgage endowment complaints – currently our largest area of work.

This should allow us to continue improving our standard of service to consumers and firms. It should also enable us to review (and, where appropriate, redesign) the approaches and processes we use in our key roles of:

- resolving complaints – in a way that is impartial, fair, accessible, timely, informal, efficient and free to consumers – and awarding fair redress where appropriate;
- encouraging the resolution of complaints before they reach us, by providing clear information about our approach; *and*
- encouraging the elimination of the sources of financial complaints, by providing clear information about the lessons to be learned from our work.

Our key roles involve us in a number of important relationships, in addition to our relationship with those who use our services. These include:

- (as part of the statutory arrangements designed to underpin confidence in financial services) – with *HM Treasury* and the *Financial Services Authority*;
- (as a future part of the statutory arrangements designed to underpin confidence in consumer credit) – with the *Department of Trade and Industry (DTI)* and the *Office of Fair Trading (OFT)*;
- (as an alternative to the courts for resolving disputes) – with the *Department*

of Constitutional Affairs and the *wider arrangements for the administration of justice*; *and*
- (as a founder member of the financial redress network [FIN-NET] designed to increase confidence in the European single market in financial services) – with *the European Commission*.

We are also a key member of the *British and Irish Ombudsman Association*, which validates and represents public and private sector ombudsman schemes in the UK and Ireland.

In fulfilling our roles, we must take account of many constraints and challenges. Chapter 2 of this document – *a demand-led service* – explains the factors that can cause our workload to rise and fall, in ways that can be difficult to predict. Chapter 3 – *dealing with the demand* – refers to associated staffing, process, systems, resources, regulatory and political issues.

Chapter 4 – *foundations for the future* – provides an overview of our three-year agenda to build foundations for the future. Key items include:

- resolving the current flood of mortgage endowment cases;
- enhancing the efficiency and effectiveness of our casework process;
- demonstrating enhanced clarity and quality in decision-making;
- increasing openness in relation to our work;
- reviewing how our costs are apportioned among financial firms;
- improving two-way dialogue with our stakeholders; *and*
- enhancing our stakeholders' confidence in the essential role we fulfil.

In line with our commitment to openness, in 2004 we commissioned an independent external review of the Financial Ombudsman Service. This concluded that "*the Financial Ombudsman Service is a thoughtful, well-managed organisation that is doing a good job under difficult circumstances*".

We propose to commission further independent external reviews every three years, with the next due in 2007.

2 a demand-led service

A key challenge is the fact that we are a demand-led service dealing with a workload that can rise or fall rapidly for many reasons – and in ways that can be difficult to predict – all outside our control. Managing our workload is not just a question of overall numbers. Surges in the number of cases about particular (and sometimes new) products also place demands on specialist expertise.

A range of factors affect the number and type of new enquiries and cases we receive and many of these factors are interdependent. The time-lag before they affect the inflow of enquiries and cases varies from one factor to another.

Some of these factors can also affect the handling of cases. For example, some firms that are under financial pressure may be more likely than others to fight their cases through all the internal 'appeal' stages of our process, as may some individual consumers.

jurisdiction
The number of financial firms and activities we cover has increased, and is likely to go on increasing.

As government has extended the range of FSA-regulated activities, the FSA has extended our compulsory jurisdiction correspondingly. The number of FSA-regulated firms we cover has grown from around 8,000 when we were first set up to around 26,000 now.

Further extensions to FSA-regulation are in prospect for firms managing or administering personal pensions and for firms offering home-reversion plans.

National Savings & Investments has recently joined our voluntary jurisdiction. And the Consumer Credit Bill – if enacted by Parliament – will give us a new compulsory jurisdiction covering more than 100,000 active consumer credit firms, to be introduced in stages. (We already cover many consumer credit issues for FSA-regulated firms.)

economic factors
Stock market performance affects investment returns. Generally, consumers do not complain about having been mis-sold a product if it does well.

More general upturns and downturns in the economic cycle affect the behaviour of consumers and firms in ways relevant to our work – as indicated below.

consumers
An economic upturn may encourage consumers to borrow more, both secured (mortgages) and unsecured (credit cards and personal loans). An economic downturn may affect consumers' safety margins and their propensity to complain.

Campaigns directed at consumers by consumer bodies – or by those with a financial interest, such as claims intermediaries – may affect complaint numbers. And press coverage of a financial 'scandal' appears to increase consumers' propensity to complain, too, about other – unrelated – financial products.

financial firms
Because most firms resolve the majority of the complaints they receive, only a proportion come on to the ombudsman service. This means that a small change in a firm's approach can have a large effect on us. For example:

- if a firm satisfactorily resolves 95 in 100 complaints, 5 in 100 of these complaints may be brought to the ombudsman service;
- if a firm satisfactorily resolves only 90 in 100 complaints (about 5% fewer), 10 in 100 of these complaints may be brought to the ombudsman service (100% more).

An economic downturn may lead some firms to cut costs (in ways that can affect service and so stimulate complaints). It may also affect the propensity of some firms to settle consumer complaints.

A variety of economic factors may encourage firms to amalgamate, reorganise or go out of business. The disruption associated with some amalgamations and reorganisations can stimulate complaints.

The number of complaints a firm generates can change if a 'good' firm takes over a 'bad' one – or vice versa. How the firm handles these complaints can also change. And a firm's attitude to the fair treatment of its customers and their complaints may be affected by regulatory action or changes in management.

tax and benefits policy
Changes in tax and benefits policy by successive governments can affect the attitudes of industry and consumers to the appropriateness of certain financial transactions. For example:

- Changes in the benefits system for mortgage-payers indirectly affected attitudes to payment-protection insurance.
- Changes in the benefits and tax systems affected attitudes to private pension provision, and to contracting-out of the state second pension.
- Concerns about future pensions and the current level of consumer savings may encourage a wider range of customers to start investing.

regulatory
The impact of regulation varies in different areas. Some FSA-regulated activities are subject to prudential regulation only, while others are also subject to conduct-of-business regulation. The powers of the OFT differ from those of the FSA.

The FSA's *treating customers fairly* initiative aims to improve the way in which FSA-regulated firms deal with customers and handle complaints, if things go wrong. This may also raise consumers' expectations.

Regulatory initiatives on consumer education may affect consumers' willingness to buy, capacity to understand or propensity to complain – as may rule changes, such as the FSA requirement for firms to give consumers special warnings about time limits for mortgage endowment complaints.

3 dealing with the demand

Other key challenges and constraints arise in relation to:

- staffing;
- quality and process;
- systems and resources; *and*
- regulatory and political issues.

staffing

We have to match staffing to an inflow of work that can change rapidly, in relation both to overall numbers and to the product-specific expertise required to deal with it. If the mix of work changes, then experienced existing staff will need re-training in (possibly complex) product-specific areas.

If our total workload increases unexpectedly, there is inevitably a delay before we can complete the recruitment of additional adjudicators. Generally, so far, there has been no shortage of suitable recruits but that may not continue – and there is a skills shortage in some specialised areas.

Once we have recruited additional adjudicators, it takes time before they have sufficient training and experience to resolve cases without close supervision.

The ombudsman service has tripled in size in five years. A quarter of our adjudicators have been with us for less than one year, and only a quarter for more than two years. This places particular strain on our middle managers and more experienced adjudicators, who must coach newcomers and also deal with the more complex cases.

Until now, staff turnover has been low, but that may not continue. The accumulated pressures of a rapidly-increasing workload may have an effect. And there may be less scope in future for career progression within the organisation, when compared with the period of rapid growth over the last five years.

quality and process

The matching of staff numbers and expertise to our changing inflow of work creates a challenge in maintaining and enhancing quality. We see 'quality' as including an outcome that is correct, consistent, clear, timely, authoritative and persuasive.

Currently, individual decisions made by an ombudsman are not usually published for public scrutiny. This makes it less easy for us to demonstrate publicly the quality standards we have achieved. So it is all the more important that we communicate openly the approach we take in reaching our decisions.

Timeliness can be adversely affected by a number of external factors. For example:

- The majority of firms are unused to having complaints referred to the ombudsman service and are unfamiliar with our process.
- Some professional indemnity insurers and their lawyers treat the ombudsman process as if it were a form of litigation.

- Some claims intermediaries try to impose their processes on us.

Our work can also be slowed by the increasing number of hard-fought and complex cases where the stakes are high for the firm. Threats of judicial review are not rare. And the High Court has confirmed that we are right to use a more detailed and measured approach to the most significant and complex cases.

Not only are financial products attracting a broader range of consumers, but the needs of consumers are changing. For example, some products are aimed at consumers who have not invested before. Some consumer credit borrowers are disadvantaged. And some of the consumers who are new to financial products may feel intimidated by our existing procedures – informal though they are.

systems and resources

Our current computer systems have coped well with the organisation's expansion and adaptation. But, like all systems, they have a limited life.

Our funding is variable. The majority of it comes from case fees. The expansion of our workload has produced increasing income, which has funded our additional workload as well as leading to economies of scale. But changes in the mix of work can increase unit costs, despite efficiency savings.

Our funding is also comparatively inflexible. It uses the same principles for firms of all types and sizes.

- Most small firms refer no cases to us. And there is no case fee for the first two cases per year. So only 5% of firms (predominantly the larger ones) paid any case fees in 2004/05. Despite this, some small firms resent the risk of case fees.
- At the other end of the scale, the current level of case fee has not dissuaded a few of the large firms from skimping their in-house complaint-handling and ‘dumping’ cases on the ombudsman service.

We have been able to expand within our existing building, on terms that give us reasonable flexibility to reduce in size again. But there is little room left for expansion. So any significant increase in staff numbers would necessitate a considerable amount of 'home-working', or a complete or partial move to new premises.

regulatory and political

We need to continue working closely with the FSA, so far as is consistent with our independent roles, where these roles overlap. A practical example of this is the process we have developed to deal with 'wider-implications' issues and to publish the results.

We will need to develop similar interaction with the OFT in relation to consumer credit. The different nature of many of the firms, and of some of the issues, in the new consumer credit jurisdiction will affect this – as will the fact that the powers of the OFT differ from those of the FSA.

The statutory framework within which we, the FSA and the OFT operate was set by Parliament and might change. This could have direct or indirect effects on the nature of our role and the amount of our workload.

4 foundations for the future

We aim to:

- provide fair, consistent, authoritative and persuasive outcomes to complaints, and be recognised as an expert organisation in resolving consumer disputes;
- be demonstrably accessible and impartial, and give consumers and firms a good standard of customer service;
- have well-trained and highly-motivated staff;
- be efficient, effective and flexible, and make good use of technology;
- coordinate our work with associated regulatory and dispute-resolution bodies, so far as is consistent with our independent roles;
- be open about our work and governance, and ensure stakeholders understand our role and have confidence in our work; *and*
- provide a comprehensive service covering, as far as practicable, activities that consumers identify as 'financial'.

To fulfil these aims, allowing for the challenges and constraints described in chapter 2 – *a demand-led service* – and chapter 3 – *dealing with the demand* – we have adopted an ambitious agenda for the next three years and beyond. The main development tasks currently underway or planned are as follows.

incoming work
We carry out significant external liaison and training activities. These are designed to reduce incoming cases by encouraging firms and consumers to resolve complaints themselves, and also to help eliminate the sources of financial complaints. We will be reviewing ways to make our work in this area even more effective.

Despite the uncertainties explained in chapter 2 – *a demand-led service* – our forecasts have been remarkably accurate. We will continue to improve the model we use to estimate:

- the nature and extent of incoming work;
- the stage of our process at which incoming work is likely to be resolved; *and*
- the staff numbers we need to deal with this work.

We will also keep in close contact with HM Treasury, the FSA, the Department of Trade and Industry and the OFT to help ensure that extensions to our jurisdiction are phased in accordance with our ability to absorb the work efficiently.

mortgage endowment cases
Mortgage endowment cases have formed almost two-thirds of our incoming work in the current year – 2005/06. While that continues, we will continue to treat these cases differently from other types of case, in two ways.

First, the cases that reach the ombudsman service are part of a wider regulatory picture, with which the FSA is actively engaged. So we will continue to provide relevant firms and the FSA with a wider range of data about mortgage endowment cases.

We are also seeking, in conjunction with the FSA, to increase the industry's engagement in the project-management of issues affecting mortgage endowment cases, including greater transparency in numbers and responsibilities. At the same time we will continue making our own contingency plans for changes in the number of mortgage endowment cases.

Second, we will continue for a time to operate within the more generous timeliness standards we use when resolving and closing mortgage endowment cases. But we will then move towards the standards we use for other types of case.

We will continue to provide speedier arrangements for priority cases. But in most mortgage endowment cases, the loss will materialise at a future date. Consumers know there is a huge surge of mortgage endowment cases and our satisfaction surveys show that – as long as we keep consumers informed – they accept that dealing with these cases will take a little longer.

staff recruitment and retention

We will keep our policies for recruiting and retaining staff under review – in the light of projected work, likely staff turnover and competition from other potential employers. We will also improve our mechanisms for manpower and 'succession' planning.

By continuing to attract applicants with appropriate skills and to offer our staff appropriate opportunities, rewards and motivation, we will help our organisation to develop. Ensuring that our salaries and benefits remain competitive will require realistic budgetary provision.

Internal transfers, secondments and training, supported by further expansion in our intranet-based knowledge system, will help increase the number of our staff who have the technical skills to deal with complaints about a range of different products.

We will introduce more robust, representative and business-focused arrangements for consulting and communicating with our staff. We will also ensure we are seen to value the work of all our employees.

quality

We have appointed a quality director to champion quality issues. We will refine the criteria we use to define 'quality'. We will also review:

- the way we produce, disseminate and record technical and process information; *and*
- the relationship between this information and our staff-training materials.

We will enhance our internal quality-management system to:

- assure the integrity of our quality-checking;
- demonstrate that casework is carried out in accordance with our documented processes and standards;
- analyse where things can be improved; *and*
- feed back information to help improve our process.

We will reduce the amount of time between our taking on a consumer complaint and allocating it to an adjudicator for investigation. We will also continue to improve our communication with consumers, while cases are awaiting allocation.

Our systems for identifying cases that remain unresolved for significantly longer than average will be improved, and we will continue with our targeted programme for reducing the number of such cases.

enquiry and casework process
We will consider how the kind of external changes that may occur over the next three years and beyond could affect us – including possible changes in:

- user expectations;
- the profile of firms;
- the social profile of consumers;
- general working and communication methods; *and*
- the role of third parties such as claims-management companies.

Continuous improvement and innovation in our process and productivity will be a key focus for us and will include a review of:

- how far our process is efficient, flexible, clear, documented and accessible for firms and consumers (including disadvantaged and disabled consumers);
- how well our process manages – and fulfils – the expectations of consumers and firms;
- how we can build on the adaptability we have already demonstrated in dealing with mortgage endowment cases;
- how we can address the possibility of a shifting balance between enquiries and cases (including more early-resolution of cases and the development of self-help processes); *and*
- how we can develop different ways of handling cases, depending on their complexity or on the types of firms and consumers involved.

information
We will consider with stakeholders whether it would be appropriate to increase the amount of information about cases and outcomes that we currently make publicly available. This would help to enhance the predictability of our approach.

We will improve the scope, appropriateness, clarity and reliability of our management information. This will include the systems for monitoring quality issues and identifying firms whose conduct should be referred to the regulator.

systems and resources
We have set up a team to plan for 'next-generation' information and telephony systems that:

- can support flexible casework processes and communication channels; *and*
- are secure, resilient, scalable and easy to modify.

The team will also review the effectiveness of our current disaster-recovery and business-continuity plans.

We will discuss with our stakeholders ways in which we can increase the flexibility of our finances. We will also review the structure of our annual levy and case fee. In particular, we will consider ways to:

- further mitigate small firms' concerns about case fees;
- improve the way in which costs are allocated among the large firms which provide most of our income; *and*
- allow for the firms that will be brought in by the proposed consumer credit jurisdiction.

We will prepare contingency plans enabling us to continue operating effectively if we were to outgrow our existing premises.

stakeholders
We will maintain close liaison with the FSA, OFT and Financial Services Compensation Scheme – so far as is consistent with our independent roles – in order to demonstrate a 'joined-up' system for users and improve our responsiveness to each other's concerns.

And by continuing to share our experience with firms, industry bodies and consumer groups, we aim not only to encourage the fair resolution by firms of consumer complaints but also to help avoid the need for our direct involvement in these complaints.

We will continue to collate information about the root causes of complaints and to share this with firms, industry bodies, consumer bodies and regulators, to help prevent complaints occurring. And we will review the ways in which we liaise with firms, industry bodies and consumer bodies, to ensure effective two-way communication at the right level.

To promote a clear and realistic understanding of our work, we will maintain constructive relations with all our stakeholders – including the media, who play a vital role in helping us deliver key messages to the general public. We will also continue to share experience with those – nationally and internationally – who are involved in dispute-resolution, and to work with those who wish to apply the Financial Ombudsman Service model to their own sphere of work.

5 overview of budget

The first section of this document – *the corporate plan* – describes the context for our planning and budgeting over the next three years or so. The following section – *2006/07 budget* – details:

- how, in the current year (2005/06), we are meeting the forecasts we made in our *plan & budget* for the year (chapter 6 – *2005/06 forecast*);
- complaint trends and our expected workload for 2006/07, together with a forward look at an estimate for 2007/08 (chapter 7 – *complaint trends*); *and*
- our proposed financial budget for 2006/07, for consultation (chapter 8 – *2006/07 budget and case fees*).

2005/06
The number of new complaints referred to us – and our performance in handling cases – are both broadly as we forecast in our 2005/06 *plan & budget*, on which we consulted in January 2005.

2006/07 and 2007/08
In 2006/07 and 2007/08 we expect to see a gradual decline in the number of new mortgage endowment complaints referred to us, compared to the number we resolve. The number of mortgage endowment cases we resolve is forecast to peak in 2006/07, falling back only slightly in 2007/08. We expect the exceptionally high level of work-in-progress resulting from the growth of mortgage endowment complaints in 2003/04 and 2004/05 to have eroded significantly by March 2008. Other incoming complaints are forecast not to exceed the number resolved.

We expect the financial resources needed to handle our caseload in 2006/07 to increase. This reflects the full impact of the expansion that has been necessary over the past two years and of essential investment in our infrastructure. We anticipate that the number of cases to be resolved in 2007/08, after the peak in 2006/07, will then decline only to about the current level (2005/06).

2008/09 and beyond
Looking further forward – to 2008/09 and beyond – becomes increasingly speculative, for the reasons outlined in chapter 2 – *a demand-led service*. Mortgage endowment complaints should have declined. Part at least of the proposed new consumer credit jurisdiction should have taken effect. The regulation of claims intermediaries should have begun. Underlying levels of banking, insurance and investment complaints referred to us are unlikely to change dramatically. But experience tells us that unexpected surges in the number of complaints about particular products can occur.

During 2006/07 we will continue to model the assumptions that affect the level of our work in the longer term, and to plan accordingly.

6 2005/06 forecast

This chapter deals with the current year – 2005/06. By the end of March 2006 we expect the overall position to be very close to the figures we forecast in our budget for the year.

new complaints

Our 2005/06 budget assumed we would receive 115,000 new cases – a 4% increase on the previous year. This reflected a small increase in complaints about mortgage endowments and other products, as well as the extension of our remit to cover mortgage and general insurance intermediaries.

Our current forecast is that we will receive 70,000 mortgage endowment cases and 45,000 other cases, in line with the budget. Mortgage endowment complaint numbers appear to be stabilising for the time being. Investment complaints have reduced (partly reflecting improved stock markets and also a tailing off of ‘splits’ complaints). This reduction has been offset by a general increase in banking and insurance cases.

cases resolved

Our 2005/06 budget assumed we would resolve and close 116,000 cases. Our current forecast is that we will resolve and close 116,000 cases, in line with our budget. This represents a 28% increase on the previous year, reflecting the investment we have made in increasing our productive capacity – in particular by recruiting additional adjudicators.

productivity

Our 2005/06 budget assumed that productivity would fall marginally, as many cases became more complex and were vigorously contested by the parties. Our current forecast is in line with the budget.

timeliness

In framing our budget for 2005/06 we decided that – because of the nature and scale of the issues involved – we would set different standards of service for mortgage endowment cases than for other cases. This is reflected in the forecast in the table below.

As explained in the next chapter – *complaint trends* – we expect to reduce the number of outstanding cases. But timeliness is currently measured when cases are closed. So closing some older cases, particularly in complex areas such as ‘splits’ and Equitable Life, will sometimes make our overall timeliness look worse.

unit cost

Our 2005/06 budget assumed that our unit cost (total costs, less financing, divided by the number of cases resolved) would fall to £456. Our current forecast is in line with the budget.

	actual 12 months 2004/05	actual 9 months 2005/06	forecast 12 months 2005/06	budget 12 months 2005/06
opening work-in-progress*				
mortgage endowment complaints	26,056	46,924	46,924	44,056
other complaints	20,645	19,832	19,832	17,645
total	**46,701**	**66,756**	**66,756**	**61,701**
new complaints				
mortgage endowment complaints	69,737	50,108	70,000	70,000
other complaints	41,226	32,122	45,000	45,000
total	**110,963**	**82,230**	**115,000**	**115,000**
cases resolved				
mortgage endowment complaints	48,869	51,457	69,000	69,000
other complaints	42,039	34,490	47,000	47,000
total	**90,908**	**85,947**	**116,000**	**116,000**
closing work-in-progress**				
mortgage endowment complaints	46,924	45,575	47,924	45,056
other complaints	19,832	17,464	17,832	15,645
total	**66,756**	**63,039**	**65,756**	**60,701**
work in hand (weeks)				
mortgage endowment complaints	31.2	34.1	36.6	34.0
other complaints	24.3	18.9	17.3	17.3
total	**30.7**	**28.1**	**27.8**	**27.0**
productivity				
mortgage endowment complaints	6.1	5.4	5.3	5.3
other complaints	3.4	3.4	3.4	3.4
total	**4.4**	**4.3**	**4.3**	**4.3**
closed within 6 months				
mortgage endowment complaints	55%	50%	40%	20%
other complaints	72%	73%	70%	80%
total	**64%**	**59%**	**50%**	**45%**
unit cost	£496	n/a	£457	£456

* '*opening work-in-progress*' means the number of cases open at the beginning of the year

** '*closing work-in-progress*' means the number of cases open at the end of the year

7 complaint trends

enquiries
Enquiries to our 'front-line' customer contact division, by phone and in writing, have increased significantly during the year. We have maintained our service standards by making use of resource planning software and by recruiting additional staff.

	actual 2004/05	budget 2005/06	forecast 2005/06	budget 2006/07
phone calls to our enquiry line	330,000	340,000	365,000	370,000
written enquiries	285,000	275,000	317,000	320,000
total	**615,000**	**615,000**	**682,000**	**690,000**

Our customer contact division plays an important role in the early resolution of complaints. At present it is resolving an average of more than 200 complaints per week at this earliest stage. These would otherwise have gone on to be 'full-blown' cases and to incur a case fee. Many of these are mortgage endowment complaints and we aim to increase still further the number of mortgage endowment complaints we resolve at this early stage.

new cases
For the reasons outlined in chapter 2 – *a demand-led service* – forecasting complaint numbers is an inexact science. The total number of new cases is comparatively stable at present and we expect this to continue through 2006/07. We would welcome any comments on our working assumptions.

	actual 2004/05	forecast 2005/06	budget 2006/07	estimate 2007/08
types of complaint				
endowments linked to mortgages	69,737	70,000	60,000	40,000
pensions	4,696	5,000	4,000	4,000
single premium investment bonds	6,281	5,000	3,500	3,000
other investments	8,274	7,500	7,000	7,500
banking and loans	7,490	9,500	10,500	10,500
mortgages	3,001	4,000	4,000	4,000
insurance	11,484	14,000	13,500	13,500
contingency	-	-	2,500	5,000
total	**110,963**	**115,000**	**105,000**	**87,500**

As explained in last year's budget consultation, because of the nature and scale of the complaints we receive about mortgage endowments, we treat them as a separate category and set different service standards for them.

mortgage endowment cases
We have assumed that the number of cases about mortgage endowments will reduce slightly in 2006/07, mainly because of an increase in the proportion of

complaints that are obviously time-barred. However there is still the possibility of a surge of cases from consumers whose cases are about to be time-barred.

Following regulatory action by the FSA, we have seen a reduction in the number of mortgage endowment cases brought to us involving larger firms. However, an increase in the number of cases involving smaller firms has resulted in the overall number of mortgage endowment cases reaching us remaining largely the same. This has an effect on productivity, as there can be economies of scale in dealing with batches of complaints from larger firms.

Currently, the number of cases about mortgage endowments that we resolve and close in a week matches the number of cases we receive. On the basis of our current assumptions about new mortgage endowment cases in 2006/07, we expect during that year to resolve and close more cases than we receive. This should lead to a steady reduction of work-in-progress.

other cases

We have assumed that cases about other products and services are likely to continue at about the current level. Within the total, the proportion of investment cases has reduced – although the complexity of some of the products involved has increased and the proportion of banking and insurance cases has grown.

The number of cases we resolve and close each week already routinely exceeds the number of cases we receive. We expect the overall reduction in work-in-progress to continue.

workload plans

	actual 2004/05	**forecast 2005/06**	**budget 2006/07**	**estimate 2007/08**
opening work-in-progress				
mortgage endowment complaints	26,056	46,924	47,924	31,924
other complaints	20,645	19,832	17,832	13,832
total	**46,701**	**66,756**	**65,756**	**45,756**
new complaints				
mortgage endowment complaints	69,737	70,000	60,000	40,000
other complaints	41,226	45,000	45,000	47,500
total	**110,963**	**115,000**	**105,000**	**87,500**
cases resolved				
mortgage endowment complaints	48,869	69,000	76,000	58,500
other complaints	42,039	47,000	49,000	48,000
total	**90,908**	**116,000**	**125,000**	**106,500**
closing work-in-progress				
mortgage endowment complaints	46,924	47,924	31,924	13,424

other complaints	19,832	17,832	13,832	13,332
total	**66,756**	**65,756**	**45,756**	**26,756**
work in hand (weeks)				
mortgage endowment complaints	31.2	36.6	22.5	12.7
other complaints	24.3	17.3	14.2	14.2
total	**30.7**	**27.8**	**19.2**	**13.4**
productivity				
mortgage endowment complaints	6.1	5.3	5.2	5.0
other complaints	3.4	3.4	3.5	3.7
total	**4.4**	**4.3**	**4.4**	**4.3**
closed within 3 months				
mortgage endowment complaints	20%	15%	20%	
other complaints	42%	35%	45%	
total	**32%**	**25%**	**30%**	**45%**
closed within 6 months				
mortgage endowment complaints	55%	40%	45%	
other complaints	72%	70%	80%	
total	**64%**	**50%**	**60%**	**75%**
closed within 9 months				
mortgage endowment complaints	75%	65%	70%	
other complaints	82%	85%	85%	
total	**80%**	**75%**	**80%**	**90%**
closed within 12 months				
mortgage endowment complaints	92%	80%	90%	
other complaints	88%	90%	90%	
total	**90%**	**85%**	**90%**	**95%**

8 2006/07 budget and case fees

income and expenditure
For 2006/07 we are proposing a balanced budget, with income and expenditure of £59.2 million. In addition, we expect to incur £1.5 million capital expenditure on:

- replacing our telephone system (which we have outgrown);
- continued development of our computerised casework system; *and*
- upgrading our IT infrastructure and carrying out building improvements.

	actual 2004/05 £m	**budget 2005/06 £m**	**forecast 2005/06 £m**	**budget 2006/07 £m**
income				
levy	12.4	12.8	11.2	15.8
return of surplus	-	(1.7)	-	-
case fees	31.2	40.0	40.5	43.2
other income	0.4	0.0	0.0	0.2
total	**44.0**	**51.1**	**51.7**	**59.2**
staff and staff-related costs	34.7	41.1	41.5	46.1
professional fees	0.6	0.8	0.8	0.7
IT costs	1.7	1.7	1.8	2.2
premises and facilities	4.8	5.7	5.8	6.1
other costs	1.1	0.6	0.5	0.5
depreciation	2.7	2.9	2.9	3.3
operating costs	**45.6**	**52.8**	**53.3**	**58.9**
financing costs	0.2	0.3	0.3	0.3
total costs	**45.8**	**53.1**	**53.6**	**59.2**
surplus(deficit)	**(1.8)**	**(2.0)**	**(1.9)**	**0.0**
cases resolved	90,908	116,000	116,000	125,000
unit cost	**£496**	**£456**	**£457**	**£472**

We expect expenditure to be 10% higher than in 2005/06, mainly because of increased staff and IT costs.

Staff costs reflect:

- the full-year cost of new staff recruited during 2005/06 to deal with the increasing volume of cases and strengthen our management team;
- the cost of the staff recruited in recent years (to deal with our increasing

workload) now progressing to 'benchmark' salary rates;
- the salary cost of retaining experienced staff in a competitive environment; *and*
- additional pension-matching contributions.

We expect IT costs and depreciation to increase as a result of the revenue effect of the capital expenditure described above.

unit cost
The low unit cost of £457 that we expect in 2005/06 is assisted by factors which will not recur in 2006/07. In particular, implementing the FSA's mortgage endowment strategy has had two effects. First, it has facilitated the resolution of some cases from larger firms during 2005/06. Second – as explained earlier – it has begun to reduce the proportion of mortgage endowment cases from larger firms.

As the consequent economies of scale reduce in 2006/07, our projected unit cost increases slightly to £472. This unit cost is similar to the 2004/05 figure and lower than the 2003/04 figure. It continues to compare favourably with the 2000/01 average of about £750 for the schemes we replaced.

The increasing number of complaints resolved by our customer contact division demonstrates an improved service to consumers and firms. But because complaints that are resolved at this stage do not count as cases when we calculate the unit cost – they have the effect of raising the apparent unit cost.

staff
For 2006/07 we have assumed a headcount of 1,018. The small increase is mainly for staff to enhance our quality and business-improvement activities.

	actual 2004/05	**budget 2005/06**	**forecast 2005/06**	**budget 2006/07**
casework divisions and ombudsmen	709	751	779	781
customer contact division	102	96	105	105
external liaison and publications	23	22	22	22
knowledge, information and policy	15	20	21	21
service quality	13	14	19	21
support services	63	66	66	68
total	**925**	**969**	**1012**	**1018**

source of income
Parliament decided that the ombudsman service should be free to consumers and funded by the industry, like the former industry-led schemes. After consultation it was decided that our income should be derived in two ways. All firms pay an annual levy, and those firms involved in cases we resolve also pay a case fee. In 2004/05 we introduced arrangements whereby the first two cases brought against a firm each year are free.

review before 2007/08
The existing funding arrangements apply to firms of all types and sizes. But it has

become apparent that the current model impacts very differently on the largest firms – which provide the majority of our cases and income – and on smaller firms.

During this current consultation, and during 2006/07, we will discuss with stakeholders the structure and balance of the case fee and annual levy, in order to explore whether there are practicable and better ways of sharing costs for the future, and the level for reserves.

As mentioned in chapter 4 – *foundations for the future* – we will discuss ways to:

- further mitigate small firms' concerns about case fees;
- improve allocation of costs among large firms, which provide most of our income; *and*
- allow for firms brought in by the proposed consumer credit jurisdiction.

case fees for 2006/07
Currently, firms pay no case fee for the first two cases brought against them in any one year. After that, they pay a standard case fee of £360, or a 'special' case fee of £475. The ‘special’ case fee applies in a small minority of cases – mainly where the complaint has been made by a small business.

We propose to continue these arrangements for 2006/07. We expect to close 125,000 cases and (after allowing for the two ‘free’ cases per firm) to charge case fees totalling £43.2 million. This would provide 73% of gross income – compared to 78% in 2005/06 and 71% in 2004/05.

annual levy for 2006/07
The remainder of our expenditure (£15.8 million) would be raised through the 2006/07 annual levy. This would represent an increase of £4.6 million on the 2005/06 levy, although £1.7 million of the difference reflects a specific reduction in the 2005/06 levy in order to return to firms a surplus that had accrued from previous years.

Taking into account:

- the forecast £1.9 million deficit for 2005/06;
- the inclusion for the first time (to comply with accounting standard FRS17) of the deficit on the final-salary pension scheme (that applies to certain staff inherited from some former schemes); *and*
- agreed reserves;

there is not expected to be any surplus to deduct from the levy for 2006/07.

balance between case fee and annual levy
Our current proposals involve holding the standard case fee at the amount fixed five years ago. It has been suggested that some respondents might prefer an increase in the case fee to an increase in the levy. In preliminary discussions with industry representatives, we found no support for increasing the case fee – especially in view of the plan to review the structure of our funding during 2006/07. But we welcome comments on this point.

If the total levy were to remain at the 2005/06 level, the standard case fee would have to increase from £360 to about £400. This would result in case fees providing

81% of our gross income – with the increased case fee applying to cases resolved during 2006/07, whether they were received during that year or earlier.

impact of levy on firms
The FSA will consult separately on the levy payable by firms in the compulsory jurisdiction. It consulted on the method of allocating the total levy among firms in its consultation paper CP74. Broadly the method involves two stages:

- The total levy is divided among the fee blocks (based on activities), according to the number of case-handling staff we expect to need for cases from that sector.
- The levy for each fee block is divided among the firms in that block according to a tariff rate (relevant to that sector), which is intended to reflect the scale of the firm's business.

Although the total levy has increased, the effect of this on firms in different fee blocks is mixed. This is because the levy depends on the number of cases expected from firms in that fee block. In any event, we estimate that about 85% of firms will pay the minimum fee for their fee block.

Subject to consultation, typical consequences are likely to be:

firm	2004/05 levy	2005/06 gross levy*	2005/06 net levy**	2006/07 estimate
bank or building society with 2 million relevant accounts	£13,800	£9,053	£7,550	£11,630
general insurer with £100 million of relevant gross premium income	£8,100	£5,200	£4,400	£5,820
life office with £200 million of relevant adjusted gross premium income	£18,600	£22,000	£18,800	£27,000
an investment adviser that holds client money and has 50 relevant approved persons	£3,250	£5,250	£4,500	£7,500
three-partner firm of independent financial advisers that does not hold client money	£90	£90	£75	£105
mortgage or insurance intermediary firm	n/a	£50	£50	£50

*Gross levy is *before* the return of the £1.7 million surplus

**Net levy is *after* the return of the £1.7 million surplus

A: compulsory jurisdiction – provisional levy

This is expected to form part of a separate consultation by the FSA in January 2006

industry block	description	tariff basis	proposed gross tariff rate	2005/06 tariff rate	proposed minimum levy per firm £	proposed gross total	2005/06 gross total	proposed contributions by block %	contribution by block % 2005/06
1	deposit acceptors, mortgage lenders and administrators (excluding firms in block 14)	per relevant account	0.0059	0.0042	100	£1,579,296	£1,115,111	10.0%	8.7%
2	firms that undertake insurance activities subject to prudential regulation only (excluding firms in blocks 13 & 15)	per £1000 of relevant annual gross premium income	0.055	0.052	100	£1,403,530	£1,231,183	8.9%	9.6%
3	Society of Lloyd's		n/a	n/a	n/a	£28,000	£28,138	0.2%	0.2%
4	firms that undertake insurance activities subject to both prudential and conduct of business regulation (long-term life insurers) (excluding firms in block 15)	per £1000 of relevant adjusted annual gross premium income	0.135	0.12	100	£5,596,540	£4,620,518	35.5%	36.1%
5	fund managers (including those holding client money/assets and not holding client money/assets)	per £1000 relevant funds under management	0. 0007	0. 001	100	£495,325	£542,139	3.1%	4.2%
6	operators, trustees & depositaries of collective investment schemes	flat fee	0	0	75	£36,225	£30,300	0.2%	0.2%
7	dealers as principal	flat fee	0	0	50	£25,500	£12,400	0.1%	0.1%
8	advisory arrangers, dealers or brokers holding and controlling client money and/or assets	per relevant approved person	150	115	150	£3,982,800	£3,008,985	25.3%	23.5%
9	advisory arrangers, dealers or brokers not holding and controlling client money and/or assets	per relevant approved person	35	30	50	£1,267,300	£1,117,760	8.0%	8.7%
10	corporate finance advisers	flat fee	0	0	50	£50,500	£28,450	0.3%	0.2%
13	cash plan health providers	flat fee	0	0	50	£850	£850	0.0%	0.0%
14	credit unions	flat fee	0	0	50	£28,100	£27,400	0.2%	0.2%
15	friendly societies whose tax-exempt business represents 95% or more of their total relevant business	flat fee	0	0	50	£7,200	£3,800	0.0%	0.0%
16	mortgage lenders, advisers and arrangers	flat fee	0	0	50	£365,600	£350,000	2.3%	3.2%
17	general insurance mediation	flat fee	0	0	50	£937,300	£650,000	5.9%	5.1%
	total – all blocks					£15,804,066	£12,767,034		

2006/07 budget

B: compulsory jurisdiction – case fees

compulsory jurisdiction – case fee table

case fee		
standard case fee	£360	(for the third chargeable case and any subsequent chargeable case in this financial year – 2006/07)
special case fee	£475	(for the third chargeable case and any subsequent chargeable case in this financial year – 2006/07)

The definitions of *standard case fee* and *special case fee* are in FEES 5.5, replacing DISP 5.6 (case fees), in the *FSA Handbook*.

The definition of *chargeable case* is in the Glossary to the *FSA Handbook*.

C: voluntary jurisdiction – levy and case fees

voluntary jurisdiction – general levy tariff and case fee table

industry block and business activity		tariff basis	tariff rate	minimum levy	*case Fee
1V	deposit acceptors, mortgage lenders and administrators, including debit/credit/charge card issuers	number of relevant accounts	0.0042	£100	£360
2V	firms undertaking insurance activities subject only to prudential regulation	per £1,000 of relevant annual gross premium income	0.052	£100	£360
3V	firms undertaking insurance activities subject to prudential and conduct of business regulation	per £1,000 of relevant adjusted annual gross premium income	0.12	£100	£360
6V	intermediaries	not applicable	not applicable	£50	£360
8V	National Savings & Investments	not applicable	not applicable	£10,000	£360

*** note on case fees:** As in the compulsory jurisdiction, firms will be charged for the third and subsequent chargeable case in this financial year