

# Approved budget and consultation feedback 2011/2012

30 March 2011

## Overview

Each year in January and February the financial ombudsman service consults its stakeholders on its plans and budget for the coming financial year.

The consultation paper we published in January 2011 explained our proposed plans for the 2011/2012 financial year - against the background of what had happened in the first nine months of the financial year 2010/2011.

We invited comments from stakeholders on these plans. We have also had discussions with key trade associations, industry practitioners and consumer groups.

## Our approved budget for 2011/2012

Taking into account the feedback we have received from those who responded to our consultation paper, we have set - with the approval of the financial services authority (FSA) - an operational budget for 2011/2012 of £102.9 million.

This budget - which assumes our workload will fall within a specified range of new and resolved cases - means that for the second year running we will be able to freeze both the case fee and the total levy.

However, we have also needed to take careful account of the uncertainties we face, particularly in relation to complaints about payment protection insurance (PPI). To help manage the financial risks in this area, we have - with the agreement of the FSA - set an additional amount of £25 million, to boost our financial reserves in relation to our "compulsory jurisdiction" (for FSA-regulated firms).

This will be funded by an addition to the levy for the "compulsory jurisdiction". [The FSA has consulted separately](#) on the allocation of this levy. We will account clearly and openly for the way we use these financial reserves.

## Our approved budget for 2011/2012

Income	<i>£ million</i>
General levy	17.7
Other levy	2.8
Case fees	82.7
Other income	0.2

Provision for bad/doubtful debts	-0.5
<b>Total</b>	<b>102.9</b>

Expenditure	£ million
Staff and staff-related costs	84.2
Professional fees	2.0
It costs	2.0
Premises and facilities	6.7
Other costs	3.0
Depreciation	2.1
Investment	2.9
<b>Total operating costs</b>	<b>102.9</b>
Financing costs	0
<b>Surplus/deficit</b>	<b>0.0</b>

Estimated number of resolved cases	180,000
Unit cost (£)	571

Of the 180,000 cases we expect to resolve during the year - which is the *central* number within the range we set out - we assume that 72,000 will relate to PPI.

The case fee for 2011/2012 will remain £500. Financial businesses will be charged this case fee only for the *fourth* (and any subsequent) case during the year.

## Summary of responses to our consultation paper

We summarise below the feedback we received from stakeholders on each of the themes we set out in our consultation paper. We also explain below how we have decided to proceed in the light of this feedback.

### *Levy and case fee*

We proposed to freeze the total levy and case fee in 2011/2012 - apart from any increase in our reserves. And we asked stakeholders how they believed our funding should be balanced in future between the case fee and the levy.

We said that if the numbers of cases we were assuming were correct, we would expect to be able to set a budget for 2011/2012 totalling between £90 million and £116 million.

Everyone who responded from the financial services industry supported the proposed freeze in the levy and case fee (other than for any increase in our reserves). Some trade associations additionally called for changes in the way case fees are charged.

Two trade associations called for free cases to be applied at the level of *appointed representatives* of a network authorised as a firm by the FSA - rather than at the level of *the network firm* itself. Another trade association called for a wider definition of those cases that are categorised as "frivolous or vexatious". And another called for *lower* case fees for cases ruled "out of jurisdiction".

Three trade associations suggested a wider review of the way in which the ombudsman service is funded. One consumer organisation and two trade associations called for *higher* case fees for financial businesses that generate a large number of complaints about the same issue.

We have frozen the levy and case fee for 2011/2012 - apart from any increase in our reserves. And we have set a budget for 2011/2012 of £102.9 million - *excluding* any amount to increase our reserves. We are able to do this because we remain on track to deliver our planned 10% reduction in our cost base.

We recognise that the way in which the total cost of the ombudsman service is allocated across the financial services industry is always likely to involve lively debate - with different funding arrangements potentially advantaging or disadvantaging different sectors or groups of financial businesses.

The new Financial Conduct Authority (FCA) will assume the role currently undertaken by the FSA in relation to approving our budget and setting the levy for the "compulsory jurisdiction". We will discuss with the FCA - once it is up and running - the possibility of a review of the way in which we are funded.

### *Our financial reserves*

We asked stakeholders what they believed our position on financial reserves should be - and how this should be funded. We forecast a range of scenarios in relation to our reserves - from a zero increase through to a £30 million increase - which we assumed would be an addition to the levy for the "compulsory jurisdiction".

Nearly half of the organisations who responded to our consultation paper did not object to an addition to the "compulsory jurisdiction" levy - as a way of increasing the level of our reserves. A further four financial businesses were not against an increase in reserves, as long as it was primarily those financial businesses that caused the need for the increase that paid for it.

Four businesses and four trade associations were uncomfortable with an increase in reserves and suggested a variety of alternatives - such as having a lower level of reserves, using an overdraft facility, increasing the proportion of funding through the "compulsory jurisdiction" levy, increasing the case fee, or spreading the cost over several years.

We have set an additional amount of £25 million to boost our financial reserves in relation to the "compulsory jurisdiction". This is to be funded by an addition to the levy for the "compulsory jurisdiction". [The FSA has consulted separately](#) on the allocation of this levy. We believe that increasing our reserves is prudent and necessary in order to manage our financial risks in 2011/2012.

PPI is the latest example of volatility in the volume and type of complaints referred to us - as a result of systemic failures in the financial services industry. So far as this type of volatility causes our income from case fees to be delayed, it may be appropriate to bridge the gap in our income with a bank overdraft. However, an increase in our financial reserves is needed, to cover the real prospect of:

- o an absolute and irrecoverable reduction in *income* (without a corresponding reduction in costs); *or*
- o an absolute and irrecoverable increase in *costs* (without a corresponding decrease in costs).

It is important to ensure that these additional reserves are used to deal with *volatility* and are *not* used to address "business as usual" issues or any shortfalls in efficiency. So a decision on whether to use any of the reserves will be one for the board of the ombudsman service to take formally - in a way that ensures the transparent governance of the additional reserves. Naturally, we expect to see some volatility in our workload as a matter of course. In our consultation paper we set out *the range* in the number of new and resolved cases that we might expect to deal with - in relation to each of the main types of case.

Type of case	Number of new cases		Number of resolved cases	
	<i>Ranging from</i>	<i>To</i>	<i>Ranging from</i>	<i>To</i>
Banking	51,000	69,000	52,500	70,500
Insurance (excluding PPI)	17,600	23,800	18,600	24,800
Investment	13,400	18,200	13,700	18,500
Consumer credit	7,200	9,800	7,200	10,200
Payment protection insurance (PPI)	48,000	72,000	60,000	84,000
<b>Total</b>	<b>137,000</b>	<b>192,800</b>	<b>152,000</b>	<b>208,000</b>

We would not expect to use the additional reserves to meet fluctuations in our workload that fall within these ranges.

However, a call on reserves might be required in any of the following circumstances:

- volumes of new cases fall outside these ranges;
- the types of cases involved change significantly;
- the workflow of cases is disrupted by regulatory or legal action;
- businesses and consumers referring complaints to us show low levels of cooperation with us (we would expect to be able to identify these patterns of behaviour where they relate to significant volumes of cases); or
- there are other significant external events outside our control.
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In these circumstances, our executive team would set out for the consideration of the board: the nature of the events that had led (or appeared likely to lead) to any significant financial variance from our normal budget position; and the revised operational approach and forecast financial position.

We produce management accounts on a monthly basis and we propose to re-forecast our budget on a quarterly basis. We will highlight any variances in the actual and forecast results which arise from the circumstances described above. Where necessary, we will present a formal request to the board to draw-down any reserves.

The board will review the financial results, forecasts and variance analysis at its regular meetings - and will satisfy itself as to the validity and value of any draw-down request. It would then be for the board to decide whether this gave rise to a justified call on reserves. Our external auditors will include a statement on this governance mechanism within their assurance report as part of their sign-off of the directors' reports and financial statements.

### *Our aims*

In our consultation paper we asked for feedback on our overall aims and plans for the coming year (2011/2012) - particularly in terms of priorities for developing our service.

Our aims are to:

- deliver a trusted, fair and easy-to-use service - for everyone;
- put knowledge and expertise at the heart of everything we do;
- be flexible, reliable and effective;
- run a "lean" and efficient organisation; and
- share our experience and insight - helping to prevent future problems.

Everyone who responded to our consultation welcomed the overall plans and aims we set out in the consultation paper.

Almost half supported our emphasis on the importance of transparency. Some called for more discussion about what kind of new information we might publish. Other priorities highlighted by people responding to the consultation included: improving the knowledge of adjudicators and the consistency of their work; improving efficiency and timeliness; "e-enablement"; and demonstrating value-for-money.

We have published a separate document called our plans for a changing world which sets what we will be doing and spending, to deliver our overall aims and plans. The document explains, for example, how we will be engaging with stakeholders on how we might publish more information, in line with the commitment to transparency in the Government's recent paper, a new approach to financial regulation: building a stronger system.

We recognise the other priorities that stakeholders have highlighted, and we are committed to making real progress on each of them. Clearly, some factors that will inevitably have an impact on us remain outside our control - for example, the extent to which businesses, claims-management companies and consumers do (or do not) cooperate with our investigations. However, we are committed to ensuring that we work as efficiently as possible.

Our next three-yearly external review will be carried out during 2011/2012 by the National Audit Office (NAO) who will report on our efficiency.

### *Complaint volumes*

In our consultation paper we set out the numbers of new cases we expected to receive, and we asked stakeholders whether the ranges we set seemed reasonable.

We proposed working on the assumption that the "base" number of new cases we would receive in 2011/2012 (other than PPI cases) was likely to be the same as our forecast for 2010/2011 - 105,000 cases plus or minus 15%.

Almost everyone from the financial services industry who responded to our consultation said that the ranges we had set for new cases were reasonable assumptions on which to work. They also said that there was an element of uncertainty in this area.

People responding to the consultation pointed out that some potential developments could lead to an increase in our caseload - for example, the impact of regulatory action, the proposed abolition by the FSA of the "two-stage" complaints-handling process, and the activities of claims-management companies.

Other developments, however, could have the opposite effect - for example, regulatory initiatives on complaints-handling, the publication of complaints data and improvements in the economy.

Two organisations who responded suggested that a key to managing this uncertainty was for financial businesses and the ombudsman service to have continued close dialogue throughout the year, in order to identify changing trends as early as possible.

In the light of this feedback, we have used the ranges for case volumes that we consulted on for our budget for 2011/2012. However, we agree that, as in previous years, there will remain an element of uncertainty. This is why we will continue close dialogue throughout the year with financial businesses - on the trends that we and they are seeing.

As complaints are raised first with the financial business concerned - before unresolved disputes are then referred to the ombudsman service - businesses should see trends in complaints before we do. So we encourage businesses to tell us when they see complaints volumes potentially deviating from the trends we have assumed.

#### *Volumes of payment protection insurance (PPI) complaints*

We asked stakeholders whether they believed that volumes of complaints about PPI sales would rise or fall - and to what level. We proposed to plan on the assumption that we would receive around 60,000 PPI cases (plus or minus 20%) in 2011/2012.

Businesses responding to our consultation agreed that a fall in PPI complaints was unlikely - and that complaint volumes would remain high, or rise further. The key uncertainty, however, was what would happen to complaint numbers, and to the behaviour of the parties involved, once the outcome of the current legal challenge (the British Bankers Association's judicial review of PPI-related matters) was known.

Responses to our consultation recognised that our workload in this area had the potential either to rise or fall significantly, depending on the outcome.

In the light of this feedback, we have assumed in setting our budget for 2011/2012 that we will receive around 60,000 PPI cases. However, we agree that there is a real risk that actual volumes could be significantly higher or lower than this - depending on the outcome of the judicial review and on the actions of the banks and other businesses supporting this legal challenge.

There is also uncertainty about how consumers, claims-management companies and businesses will deal with complaints even if the legal issues are resolved. The section on this page about our financial reserves sets out how we plan to deal with the risks of volatility such as this.

### *Other issues raised by stakeholders*

Some stakeholders raised wider issues with us that were not formally part of this consultation on our plans and budget.

All eight trade associations who responded expressed concerns about the activities of claims-management companies. These trade associations said that these companies had a distorting and/or detrimental impact on consumers.

Some of these trade associations called for claims-management companies to have to contribute to the funding of the ombudsman service - for example, by having to pay case fees. One trade association suggested that consumers should pay a refundable deposit. And two consumer organisations stated that the ombudsman service should remain free for consumers.

Claims-management companies are active in complaints about PPI - and also in complaints involving some charging and debt issues. In our experience, the standards adopted by these commercial businesses vary significantly. We will continue to work with the FSA, the OFT and the Ministry of Justice (which is responsible for regulating the claims-management sector) to encourage good practice by claims-management companies and the effective handling of complaints by financial businesses.

The possibility of charging complaints-management companies would have a range of implications - and would require primary legislation. We will discuss with the new Financial Conduct Authority (FCA) - once it is up and running - the possibility of a review of the way in which we are funded. We remain committed to a service which is free to customers.

Three consumer organisations, three trade associations and a financial business welcomed the steps taken by the ombudsman service to work together to share knowledge. Some emphasised the importance of this being done in a way that continued to be seen as impartial.

We intend to continue to work closely with businesses and consumer organisations, to share knowledge and ensure that our service is easy to use. Examples of this include our new arrangements for liaising with industry practitioners and arrangements we have made with Citizens Advice to put clients of theirs with financial complaints directly through to our own consumer helpline, where appropriate. We talk more about our plans in our document, our plans for a changing world.



### *List of respondents*

The following organisations responded to our consultation paper. A further six organisations, who are not listed, also provided responses but requested that these be kept confidential.

- Association of British Insurers
- Association of Independent Financial Advisers
- Association of Mortgage Intermediaries
- AXA UK
- British Bankers Association
- Building Societies Association
- Citibank International
- Citizens Advice
- Council of Mortgage Lenders
- Consumer Council of Northern Ireland
- Consumer Finance Education Body
- Financial Services Consumer Panel
- Finance and Leasing Association
- Ministry of Justice
- Nationwide Building Society
- The UK Cards Association
- Which?