

laying the
foundations

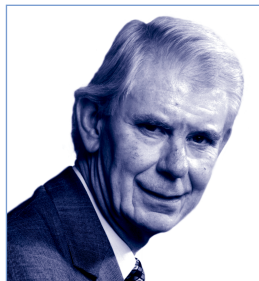


Financial
Ombudsman
Service

first annual report

26 February 1999 to 31 March 2000

setting out the blueprint



chairman's statement

by **Andreas Whittam Smith**

This annual report is unlike the usual reports published by ombudsman schemes. And it is different from the reports which we will be publishing in future years. The major difference is that the report contains only a few statistics, and no analysis of the complaints we have handled or the lessons to be drawn from them. Nor are there any case studies – the accounts of people's grievances, and the circumstances surrounding them, which generally make such salutary reading.

The reason for this is that we are not yet handling complaints in our own right. This report covers the first year in existence of the Financial Ombudsman Service, a year spent planning ahead and preparing to 'go live' – something that will happen once we receive our powers under the Financial Services and Markets Act. We have nevertheless behaved corporately as if the terms of the Act were already in force.

This is why we are calling this annual report *Laying the foundations*. In the year covered by this report, we have progressed from the blueprint stage – working closely with the Financial Services Authority (the FSA) on the regulatory proposals underpinning the new complaints-handling framework – to the implementation stage, which has involved putting in place the infrastructure which will be needed to support the new single ombudsman service.

Whilst there are close links between us and the FSA, we are to operate independently. On the one hand, the FSA appoints our board and makes most of the rules under which we operate. And we must seek approval from the FSA for our budget.

On the other hand, both the board and the ombudsmen are required to be appointed on terms that secure their independence and to publish annual reports on our work. We have agreed a memorandum of understanding with the FSA covering how these matters should work in practice.

The Parliamentary Committee that studied the draft legislation recommended that we should report annually on the adequacy of our budget. In April 2000 the FSA approved our budget for 2000-2001 in the sum of £22.7 million. Our budget discussions with the FSA centred, among other things, on the forecasts it was prudent to make about the level of growth in complaints.

We indicated that if they rose more sharply than estimated, we should need more resources.

On the evidence of the first two months of the year, that could be the case. Subject to that, we are satisfied that the budget approved this year will be adequate for our purposes.

Our work on the new ombudsman structure has taken place around the existing complaints-handling and ombudsman schemes, which carried on 'business as usual' throughout the year. →

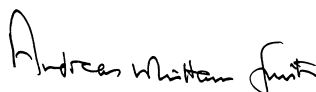
← Building work inevitably causes some disturbance. I am most grateful to the staff, council and boards of the schemes for their co-operation, tolerance and fortitude during this process.

The fact that the Financial Ombudsman Service is being constructed on virtually the same ground as the current ombudsman schemes – with a structure that builds on established strengths and retains the best features – is deliberate. The ombudsman network, which has evolved over the last twenty years as a free, informal alternative to the courts, has become the accepted framework for resolving financial complaints fairly, speedily and independently.

In fact, it must be seen as a tribute to the ombudsman system that this is the model put forward by the Government as a key part of the proposed unified structure for complaints-handling under the Financial Services and Markets Act. Building on their successes and achievements, the new service will bring together the existing complaints-handling organisations on a single statutory footing and take forward the ombudsman concept into the new century.

The idea behind the merger of a number of smaller related bodies into a single one-stop organisation has already led to the formation of the FSA. The rationale behind the establishment of the Financial Ombudsman Service is similar – to reduce confusion and possible duplication, especially so far as consumers are concerned, while responding to the blurring of traditional distinctions between the industry sectors, as firms are restructured and products are packaged together.

This annual report focuses on the work that has been done during our first year of 'behind the scenes' preparations, to turn the concept of a unified Financial Ombudsman Service into an imminent reality. This would not have happened without the hard work and dedication of many people – at the existing ombudsman schemes, at the FSA, across the financial services industry and the consumer world, and at the embryonic Financial Ombudsman Service itself. I am grateful to everyone who has been involved in this exciting and worthwhile venture so far. And I look forward to the many challenges ahead, when we 'go live' and start handling complaints in our own right.



Andreas Whittam Smith
chairman

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from blueprint to building site



chief ombudsman's report

by **Walter Merricks**

This year has been one of design and construction, as we gradually put in place the elements needed for operating the new single ombudsman service. During this period, we have only been a 'shadow' organisation, while we wait to receive our full statutory powers under the Financial Services and Markets Act (at a date commonly known as 'N2'). Nevertheless, it is important that we establish longer term objectives.

We aim to:

- provide consumers with a free one-stop service for dealing with disputes about financial services
- resolve disputes quickly and with minimum formality
- offer user-friendly information as well as adjudication; and promote avoidance of disputes as well as their resolution
- take decisions which are consistent, fair and reasonable
- be cost-effective and efficient; be seen as good value
- be accessible to disadvantaged and vulnerable people
- be forward-looking, adaptable and flexible, making effective use of new technology
- be trusted and respected by consumers, the industry and other interested parties

quick with minimum
formality

← **a one-stop service**

Seamless, comprehensive coverage should clearly be our aim. But this objective is combined with caution as to the speed with which we may arrive at this destination. At 'N2' the coverage of our service under the proposed 'compulsory jurisdiction' will largely resemble that of the existing schemes combined under one roof. This in itself will provide a very large measure of unification, and the vast majority of consumers with complaints related to financial services will find that we are able to deal with their problems.

But anomalies will still remain. So far as financial intermediaries are concerned, complaints about investment broking will fall within our remit, but (with a few exceptions) complaints about insurance or mortgage broking will not. Nor, unless they involve disputes with banks or building societies, will complaints about unsecured personal loans and credit cards fall within the remit of the new Financial Ombudsman Service. We will wish these to come within our 'voluntary jurisdiction' in the longer term. But we have been deliberately careful to avoid promises about the timing.

The consolidation of our compulsory jurisdiction, together with the rise in the number of complaints which currently shows no sign of relenting, represents a substantial challenge for us. We plan to expand our remit – the voluntary jurisdiction – once we are confident that we can cope with the scope of the compulsory jurisdiction. In the

meantime, we will be discussing with trade associations and consumer organisations how and when the voluntary jurisdiction could be expanded.

resolve disputes quickly and with minimum formality

The legislation itself – the new Financial Services and Markets Act – provides that this should be our aim. We inherited responsibility for existing complaints-handling schemes, some of which had accumulated delays in processing and resolving complaints. The transfer of staff, their transition to a new location, the disruption caused by new systems and the time taken to train newly recruited employees will take their toll on productivity. We will need to work hard to provide service standards of which we can properly be proud.

There has been much debate about the impact that the European Convention on Human Rights may have on our service, and of course this remains to be seen. However two things are clear: first, that our procedures should be fair to all parties and should respect their rights; and secondly, that we should minimise the formality that the procedures will necessarily involve. We will therefore be designing a unified complaint process that will attempt to combine these features. →

❖ **offer user-friendly information**

Given the range of financial services and products that will be covered by the Financial Ombudsman Service – from motor insurance to stockbroking – we will need to operate on a divisional basis with a uniform system for processing complaints. But we must be flexible, courteous and responsive, with each case treated on its merits rather than being stereo-typed. Although a large organisation compared to our predecessor schemes, we aim to continue the virtues of smallness which we have inherited from them. We should deal with consumers as far as possible using their preferred medium of communication – by phone, letter or email as appropriate – only formalising matters when it is necessary to avoid confusion or for a final recorded decision. We will be revising all our enquiry procedures, complaint forms, information material and standard communications.

Based on experience to date, we can expect to receive a large number of enquiries from people whose complaints we cannot immediately investigate, either because they will not be within our remit or because the complaint has not yet completed the complaints procedure of the firm itself. In these circumstances, we will offer information and assistance. Our aim will be to maximise the opportunities for resolving disputes at the earliest possible stage, rather than leaving problems to escalate. Likewise, we should offer access to advice and help on our process and

policies for complaints-handling staff within firms and for professional consumer advisers. By assisting firms and potential complainants in this way, we can help to defuse budding disputes, set consumer expectations appropriately and raise industry standards in what should be a virtuous circle.

consistent, fair and reasonable decisions

Consistency is a virtue prized by the industry but of less interest to consumers. But we should do our best to ensure that the financial services industry is aware of consistent policies setting out how we would approach commonly encountered situations. This will enable firms to resolve complaints with an understanding of what would happen if the dispute were referred to us. We have the opportunity to introduce consistency of policy in areas where the schemes have hitherto adopted different approaches. For example, we will be able to harmonise the approach to handling complaints about banks and building societies where some matters have previously been dealt with differently by the separate Banking Ombudsman and Building Societies Ombudsman schemes. And we will prepare and publish common guidelines in relation to awards for distress and inconvenience. ❖

← We will not be obliged to follow precedent, since cases all have to be considered on their merits. But we should aim where possible to act predictably and consistently. Our right to make decisions that go beyond the law, and that bind firms but not consumers, should make us act with care and responsibility.

accessible for disadvantaged and vulnerable people

We will prepare guidelines on what is known as 'informability' – the principle that people should receive information in the medium they can most easily assimilate. These guidelines will cover how we should provide access to people who do not use English as their first language (including Welsh language users and people from ethnic communities), people with reading/learning difficulties and people with hearing or visual impairment, as well as those with mobility disabilities.

We will need to take account in the service we offer of changing social trends and working patterns. Some firms in the industry are already offering round-the-clock service, though this is exceptional. But very many service providers now offer phone access from 8am until 8pm in the evening. We will test whether the demand would justify us providing a service at this level.

cost-effective and efficient; be seen as good value

The decision by the government to set up a single ombudsman scheme was driven by policy rather than budgetary considerations. In the long term, harmonised ombudsman arrangements should prove beneficial both for consumers, in terms of accessibility, and for the financial services industry, in terms of cost efficiency. But in the short term, the exercise has entailed substantial extra costs and the immediate need to invest in additional management and new technology. The industry will want to see this reflected in due course in lower unit costs. We must begin the drive for productivity improvements as soon as we have a stable platform.

In the meantime, we have established an Industry Funding Group, consisting of representatives of the main financial services trade associations. We have consulted the group both about our overall budgetary outlook and about how contributions to our funding should be allocated across the financial services industry. We have also established industry liaison groups in the banking and insurance sectors, and a forum for investment practitioners to meet representatives from the Financial Ombudsman Service on a regular basis will be arranged shortly.

As far as standards of service are concerned, we should aim to provide a service to our stakeholders – consumers, the financial services industry, regulators, the media *etc* – of at least the same standard that the industry would itself expect to provide to its customers. Firms would be concerned if we offered an obviously worse level →

showing
our
accountability
by our
actions

of service to their customers than they themselves provide. If this were the case, consumers would feel doubly aggrieved – first by the matter giving rise to their complaint and then by the poor service we offered. If we are to criticise firms for delays or poor service, our own standards should not be open to a similar reproach.

This approach to establishing our service standards should put us on a sound footing and justify expenditure levels to meet these standards.

forward-looking, adaptable and flexible, making effective use of new technology

We should anticipate developments in the industry – its products and services – and the extent to which these will impact on consumers and us. By making a substantial investment in IT, we should be able to reduce our dependence on paper files and allow flexibility in case-handling across the scheme. Web-based systems should allow us to develop home-working and will also be the key to the development of effective knowledge management within the organisation.

trusted and respected by consumers, the industry and other interested parties

Our reputation is our most vital asset. We only have to look at recent examples of public service organisations whose reputations have been impaired by failure to meet accepted standards of service. We should undertake stakeholder opinion research and combine this with survey work measuring consumer satisfaction.

We can gain respect and trust only if we operate and communicate in an open and transparent fashion, showing our accountability by our actions and not just by formal statements. We look forward to a close involvement and interest in our affairs on the part of consumer organisations, journalists from the specialist and general media, parliamentarians, trade associations and individual firms.

In January 2000 we held our first conference for industry and consumer representatives. This was well attended with over 250 delegates.

The following month we held a seminar in Edinburgh for consumer representatives from all over Scotland.

structure

My first task following my appointment in June 1999 was to determine the structure for the new single ombudsman service. I decided that there should be three ombudsman divisions →

a new structure built around the existing schemes

← – each headed by a principal ombudsman – to take charge of the insurance, investment and banking and loans areas. This allowed the new structure to fit not too uncomfortably around the existing complaints-handling and ombudsman schemes during the interim period leading up to ‘N2’, while establishing a relatively small ‘top team’ to steer the project forward.

David Thomas, the banking ombudsman, took up responsibility for the banking and loans division and, with his previous close involvement in the Ombudsman Steering Group, was able to make a significant contribution from the early stages. I am grateful to him for his unstinting help over a wide range of issues. Tony Boorman, formerly deputy director-general at OFGEM, the energy regulator, joined in March 2000 to head the insurance division. It was a loss for us when Tony Holland, who had been designated as principal ombudsman to head the investment division, was appointed chairman of the Northern Ireland Parades Commission. I welcome as his replacement Jane Whittles, the former director of compliance at OFTEL and previously the deputy director of the Inland Revenue’s Special Compliance Office.

On my recommendation, the board of the Financial Ombudsman Service appointed individuals from the existing schemes to the ombudsman panel contemplated in the Financial Services and Markets Act – these appointments of ombudsmen being mirrored by the schemes themselves. Although the Financial Ombudsman Service’s panel of ombudsmen will not formally ‘go live’ until ‘N2’, the panel is now ready and in place.

the legal framework

We shall be operating under the terms of the Financial Services and Markets Act, when this legislation comes into force. Naturally we have taken a close interest in the ombudsman provisions of this piece of legislation. One provision in particular had caused us concern – a provision relating to the power of the ombudsman to make money awards – because it seemed to be ambiguously expressed. We were grateful, therefore, that while the Bill was in the House of Lords, a cross party grouping of peers promoted a clarifying amendment, prompting the Government to come forward with its own amendment.

The Act itself contains no transitional provisions, and we shall take a close interest in the orders which the Treasury is empowered to make to provide transitional arrangements. It is important that complaints already in train, as well as those which might have been made under the previous schemes, can be brought within our service, whether or not the events complained about took place before the Act came into force.

This date – ‘N2’ – is as yet unknown. But it is now expected some time next year. While the delay is welcome in some respects, giving us more time to plan, too long a period in which we have to operate through the existing complaints-handling and ombudsman schemes as a ‘service provider’ would not be desirable. →

moving towards
resolving and handling
own in our
complaints
right

◀ **relations with the FSA**

Some of our predecessor schemes have enjoyed close relations with a regulator while others have been totally independent. We will clearly have close contact with the Financial Services Authority (the FSA) for a number of reasons. First, the FSA's rules relating to complaints-handling by firms will be of the greatest importance to us. These rules will be completely new to those in the general insurance and banking sectors. The complaints-handling rules have the potential to provide consistency in the standard of service consumers receive, and I warmly welcome them.

The FSA is also required to make the rules that govern our compulsory jurisdiction and our funding, and to approve our budget. Clare Boyle, head of complaints oversight and policy at the FSA, has been the driver and architect of much of the FSA's work in this area. She was the principal author of the joint consultation paper (CP33), issued by the FSA and us in November 1999, and its companion feedback statement (CP49). Her vast experience in the field of financial services regulation, and her energy and commitment to the objectives of the new service, have served us exceptionally well.

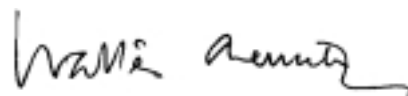
To clarify our ongoing relationships with the FSA, we have entered into a memorandum of understanding, covering how we expect to deal with sensitive subjects such as the transfer of information, budget approval and rule making. We will also need memoranda to govern our relationships with others, such as the Pensions

Ombudsman, the Office of Fair Trading, the professional bodies and other dispute-resolution organisations – all of which we expect to be working closely with, as the Financial Ombudsman Service moves into its second year.

our staff

Staff at the complaints-handling and ombudsman schemes had to endure more than two years of uncertainty – following the initial announcement in December 1997 that there was to be a single scheme – before their future could be clarified. They might have been justified in feeling resentful and uncooperative towards this new organisation. Instead, they continued to work energetically through this period, and the vast majority accepted our offer of employment with the new Financial Ombudsman Service. In addition, we have been able to recruit many new, talented and enthusiastic individuals to join us.

I am grateful to all of them for their cheerfulness, loyalty and support.



Walter Merricks
chief ombudsman

overview of the ombudsman services provided during the formation of the new single scheme

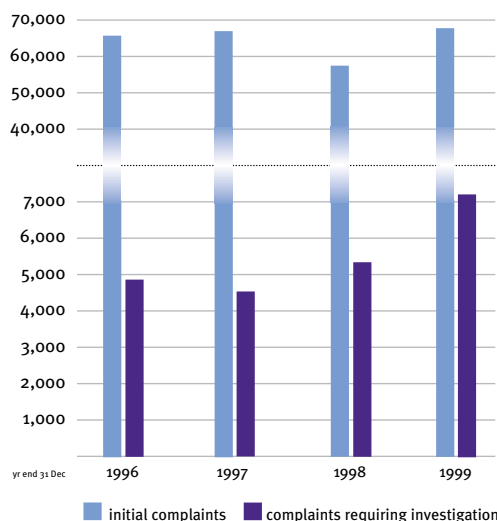
In March 2000, the Financial Ombudsman Service signed 'service level' agreements with the boards of the existing complaints-handling and ombudsman schemes. Under these agreements, the Financial Ombudsman Service undertook to provide the appropriate complaints-handling service on behalf of each of the existing boards from 1 April 2000 until the Financial Services and Markets Act comes into place – at which time the Financial Ombudsman Service will assume full responsibility. We have structured the new service around four principal areas – insurance, investment, banking and enquiries.

insurance-related complaints

The insurance division will be responsible for the work formerly carried out by the Insurance Ombudsman Bureau (IOB). The vast majority of insurance-related complaints relate to the refusal of an insurer to pay either the whole or a part of a claim under a policy. Nearly two thirds of complaints relate to household and motor policies, but complaints are also made about all types of personal insurance – travel, accident, medical expenses, loan protection, legal expenses, pets and animals, caravans, yachts *etc.* Disputes can relate to a variety of issues – policy terms, exclusions or conditions, incorrect information disclosure, no claims discounts or poor service.

The IOB published its annual report in March 2000. In 1999 it received over 7,000 cases requiring investigation, an increase of 35% on the 5,261 received in the previous year.

complaints to the Insurance Ombudsman Bureau*



investment-related complaints

The investment division will be the largest of the three case-handling divisions at the Financial Ombudsman Service. The Personal Investment Authority (PIA) Ombudsman Bureau will form the biggest constituent part of this division. →

**These figures are drawn from the recent annual reports published by the different ombudsman schemes. As separate organisations, using different rules, terms of reference and procedures, the figures are not directly comparable. For example, the year-ends are different as are the exact definitions of 'initial complaints' and 'complaints requiring investigation'. The figures are shown here only as a general guide to trends across the different schemes.*

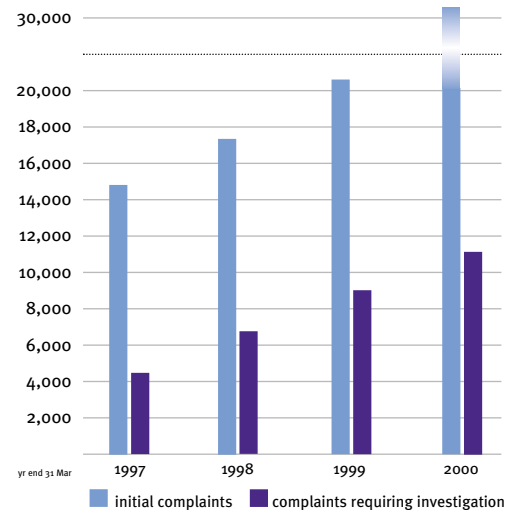
integration
of the
into the
new
single
separate
schemes
structure

Most of the complaints dealt with by the investment division relate to advice given to consumers to buy investments. These cases generally involve having to decide whether the details of the investment were properly explained and whether the investment in question was suitable, given the consumer's personal and financial circumstances.

Personal pension plans are the investment products complained about most frequently, followed by low-cost endowments linked to mortgages, a rapidly growing area of complaint. Other significant categories of complaint relate to the range of long term insurance policies and other investment bonds, annuities and unit trusts. In the year ending March 2000, the PIA Ombudsman Bureau received 11,346 complaints requiring investigation, an increase of 25% on the 9,034 received in the previous year.

The investment division will also be responsible for the work carried out by the Office of the Investment Ombudsman, which deals with complaints against firms regulated by IMRO. These types of complaint relate to investment management – usually alleged poor administration or failure to carry out instructions. PEPs are the products most frequently complained about to the Investment Ombudsman. The Office of the Investment Ombudsman is a small complaints-handling scheme, receiving 433 complaints in the year ending March 2000*.

complaints to the PIA Ombudsman Bureau*



The Securities and Futures Authority (SFA) Complaints Bureau also forms part of the investment division of the Financial Ombudsman Service. The SFA Complaints Bureau deals with complaints about firms regulated by the SFA – mainly involving share dealing or the administration of new issues. In the year ending March 2000 the SFA Complaints Bureau received 854 complaints*. Although this was fewer than the 972 complaints received in the previous year, that year's figures were distorted by over 260 complaints relating to a single new issue by one firm.

banking-related complaints

The banking and loans division of the Financial Ombudsman Service resolves consumers' disputes with banks and building societies, inheriting the work of the separate Banking Ombudsman and Building Societies Ombudsman schemes. Complaints fall broadly into two

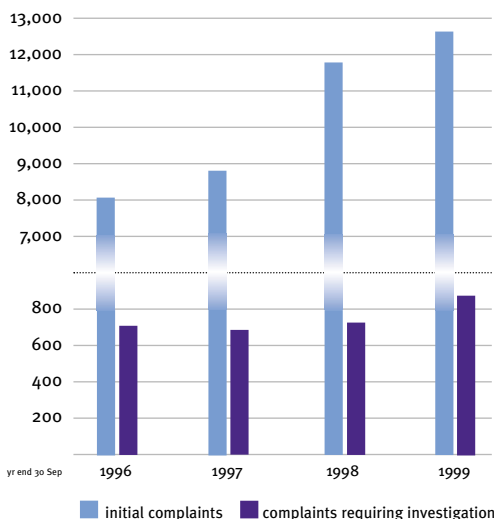
← categories – complaints about investment accounts, payment accounts, current accounts and card services; and complaints about mortgages, overdrafts and other loans. Many of the complaints in this area arise from disputed circumstances, errors by the institution, or alleged unfairness in administration.

As the number of building societies reduces, so have the number of complaints relating to building societies. In the year ending March 2000, the Building Societies Ombudsman scheme received 856 cases for investigation, a reduction of 29% on the 1,222 cases in the previous year*. However, complaints relating to banks – including the de-mutualised building societies – have increased. In the year ending September 1999, the Banking Ombudsman received 846 complaints requiring formal investigation – an annual increase of 14% – and 12,713 initial complaints, 7% more than in the previous year.

planning a ‘single point of entry’ for enquiries

The enquiries division provides general advice and guidance for consumers on what to do if they are not happy with a financial product or service. The division also gets involved at the initial stages of the ombudsman process, acting as a gateway to the complaints-handling and dispute-resolution services currently provided by the existing schemes and – in due course – directly by the Financial Ombudsman Service.

complaints to the Banking Ombudsman scheme*



*see footnote on page 12

At present the division’s resources are structured to support the specific requirements of the existing individual schemes. However, the process of integrating and aligning these resources, to deliver the uniform ‘single point of entry’ capability required when the Financial Services and Markets Act comes into force, are now well advanced.

Against this background of integration and alignment, the enquiries division is recording a significant increase in consumer demand for its services. There have been month-on-month increases in the number of calls since the turn of the year, with the division currently handling an average of 1,200 phone calls daily (equivalent to 300,000 calls a year). This level of demand represents a 40% increase compared with the same period last year. The division is also recording a similar increase in written correspondence with an average of 600 items daily.

building in progress



chief operating officer's review

by **Ian Marshall**

During the six months to 31 March 2000, a large number of people – some from the existing complaints-handling and ombudsman schemes and some recruited externally from commercial backgrounds – worked hard to bring the new organisation to its present form. The work can be divided into a number of distinct activities:

- getting the management team on board
- preparing the infrastructure for the new organisation
- encouraging staff from the existing schemes to join the new organisation and to re-locate to offices at South Quay in East London
- negotiating 'service level' agreements with the boards of the existing schemes
- agreeing the budget

getting the management team on board

The board appointed Walter Merricks and me in the early summer of 1999. Over the next four months, the three principal ombudsmen and the senior staff responsible for the support functions of the new organisation were also appointed. Wherever possible, people were recruited from the existing schemes. But specialist senior managers were brought in externally to head support functions responsible for technology, human resources, communications and service quality. The existing schemes were still of a size where they did not need this type of specialist skill. Bringing the schemes together therefore anticipated the addition of these specialist functions.

preparing the infrastructure for the new organisation

The board had taken an early decision to follow the example of the Financial Services Authority (the FSA) and bring the separate schemes together in one location. After a thorough search, the board selected our current base located on four floors of a refurbished building in South Quay, East London. South Quay does not yet have the facilities of Canary Wharf in London's Docklands and our offices were therefore obtained at a competitive rent. →

← The lease on the office space was signed in November 1999. This gave us five months to 'fit out' the floors, ready for staff from the separate schemes to co-locate here during April and May 2000. The fit-out was based on an open-plan design with no individual offices, using mid-range specifications. Nevertheless, this still gave rise to significant expenditure.

A key element of the fit-out was the installation of a modern IT infrastructure. The computer networks in place at the existing schemes were of various types and ages, and we decided at an early stage that the most sensible route was to install a single resilient network for the new organisation. From a technology viewpoint, the Financial Ombudsman Service is similar to any operation involving a high level of transactions with consumers, and performance and reliability will be essential.

Although staff from the different schemes have shared a common IT infrastructure since co-locating to South Quay, they currently still use their old complaints-handling software systems. The next stage is therefore to rationalise the business process in preparation for 'N2' – when the Financial Ombudsman Service will start handling complaints in its own right, using harmonised rules and procedures – and subsequently to introduce a single complaints-handling system. This work should be completed by April 2001.

attracting existing staff to South Quay

We needed to encourage as many staff as possible from the existing schemes to accept employment with the new Financial Ombudsman Service and to re-locate to South Quay in East London. Negotiations on terms and conditions started in November 1999, and job offers were sent to all staff in the first week of February 2000. Of the 340 job offers that we made, 25 people did not accept employment with the Financial Ombudsman Service for a variety of reasons.

Staff who were previously employed by the separate complaints-handling and ombudsman schemes became employees of the new ombudsman service on 1 April 2000. During April and May 2000 they moved to the Financial Ombudsman Service's offices at South Quay from six different locations across London.

negotiating 'service level' agreements with the existing schemes

In addition to negotiating terms and conditions of employment with the staff of the separate complaints-handling and ombudsman schemes, we also needed to agree a way forward with the schemes' boards and councils. These boards and councils retain responsibility for handling complaints – under the rules and terms of reference of each of their schemes – until 'N2'. The boards and councils all agreed that the staff working at their schemes should come together into the new organisation as soon as possible. →

agreeing a reasonable basis for estimating increases in workload

As a result, the new Financial Ombudsman Service signed 'service level' agreements with each of the boards in March 2000. Under these agreements, the new single ombudsman scheme undertakes to provide sufficient resources to meet agreed service levels in the period leading to 'N2'.

agreeing a budget for 2000-2001

Expenditure incurred by the Financial Ombudsman Service in the period to 31 March 2000 comes under the heading of 'establishment expenditure' – preparatory set-up costs resulting from the decision to bring together the existing schemes and create a single ombudsman service. The total figure to 31 March 2000 of £2.9 million is transferred to the establishment cost recovery fund and will be recovered from the industry in the three years following 'N2'.

Expenditure for the year to 31 March 2001 will fall into two categories. The smaller part forms the residue of 'establishment' expenditure. The bulk of expenditure forms the operating budget for 2000-2001, which will be recovered from the financial services industry through the existing schemes' funding mechanisms.

The operating budget for 2000-2001 is £22.7 million – significantly higher than the aggregate of the existing schemes' budgets for 1999-2000. This is partly due to the projected increase in the volumes of enquiries and complaints in 2000-2001. There is some concern about this estimated increase in workload.

We have therefore initiated a joint study with the FSA, to identify and analyse the factors underlying the growth in workload and to agree a reasonable basis for estimating increases in workload in the future.

In developing the budget for 2000-2001, it was clear from an early stage that there would not be the customary 'merger savings' from bringing the separate schemes together. In addition to the costs of co-locating staff from separate offices, the new scheme has needed to add specific skills and resources which none of the existing schemes either had or needed. This will be an additional cost to the new service in its early years.

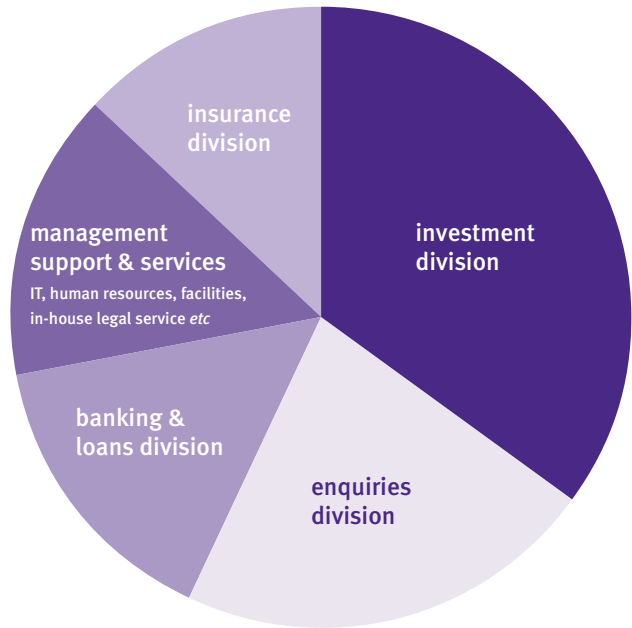
consulting
about the
costs of the
new
service

← **setting standards**

How will this extra cost show itself in a return on the investment? The board of the Financial Ombudsman Service is satisfied that it was the correct decision to set up the new service with a robust infrastructure and management, and that this will turn out to be the cost effective route. While we are still at an early stage in the life of the Financial Ombudsman Service, we are aiming in our initial budget planning to reduce in real terms the unit operating cost of the new service to the cost levels of the existing schemes by 2002-2003 – and to have cost levels in real terms less than those of the existing schemes after 2003.

These unit cost targets need to be properly defined and accompanied by service level targets. We intend to publish these in January 2001 in our 2001-2002 budget consultation documents.

how staff fit into the new Financial Ombudsman Service structure



organisation chart

chief ombudsman Walter Merricks					the board chairman – Andreas Whittam Smith				
enquiries division		banking & loans division		insurance division		investment division		management support & services	
dealing with phone and written enquiries and handling the early stages of complaints resolution		investigating, adjudicating and resolving banking-related complaints		investigating, adjudicating and resolving insurance-related complaints		investigating, adjudicating and resolving investment-related complaints		chief operating officer Ian Marshall	
head of enquiries & service quality Steve White		principal ombudsman David Thomas		principal ombudsman Tony Boorman		principal ombudsman Tony Holland (to Autumn 2000) Jane Whittles (from June 2000)		company secretary Barbara Cheney	
		ombudsmen Chris Eadie Jane Hingston Michael Reddy Josephine Thompson Roger Yeomans		ombudsmen Reidy Flynn Peter Hart (to June 2000) Stephen Lilley Michael Lovegrove		ombudsmen Ron Bennett Richard Prior Philip Roberts Chris Tilson Ken Webb (associate)		head of communications David Cresswell	
								human resources director Sue Ferran	
								IT director Trevor Kirkham	
								management accountant Harsha Pandya	
								head of facilities & administration Ian Pattison (to June 2000)	
								financial controller Chris Smith	

statutory accounts and statements

Financial Ombudsman Service Limited

(formerly Financial Services Ombudsman Scheme Limited)

(a company limited by guarantee)

officers and company secretary

Walter Merricks, Chief Ombudsman

Ian Marshall, Chief Operating Officer

Barbara Cheney, Company Secretary

report and financial statements

31 March 2000

officers and professional advisers page 20

directors' report page 21

statement of directors' responsibilities page 23

auditor's report page 24

income and expenditure account page 25

balance sheet page 26

notes to the accounts page 27

registered office

To 25 April 2000:

25 North Colonnade

Canary Wharf

London E14 5HS

From 26 April 2000:

South Quay Plaza

183 Marsh Wall

London E14 9SR

officer and professional advisers

directors

The directors of the company at 31 March 2000 and during the period were:

Andreas Whittam Smith (chairman)

Brian Landers (deputy chairman)

Michael Barnes CBE

Robert Crawford

Ruth Evans

Maggie Lee

Dr Oonagh McDonald CBE

Sylvie Pierce

John Rawlings

Richard Thomas

Helena Wiesner

Charles Wilson

bankers

Lloyds TSB Bank plc

City Office

PO Box 17328

11 – 15 Monument Street

London EC3V 9JA

auditors

Deloitte & Touche

Stonecutter Court

1 Stonecutter Street

London EC4A 4TR

All directors were appointed on incorporation of the company

directors' report

The directors present their report and the audited financial statements for the period from 26 February 1999 to 31 March 2000.

incorporation, activities and business review

The company was incorporated on 26 February 1999 as the Financial Services Ombudsman Scheme Limited. On 6 December 1999 the company changed its name to Financial Ombudsman Service Limited.

The Financial Ombudsman Service has been created as part of the government's new legislation for the financial services market. The company has been incorporated with a view to consolidating into a single statutory body the complaints-handling and ombudsman services currently provided by a number of statutory and voluntary schemes. The schemes are the Office of the Banking Ombudsman, the Office of the Building Societies Ombudsman, the Insurance Ombudsman Bureau, the Personal Investment Authority Ombudsman Bureau, the Personal Insurance Arbitration Service, the Securities and Futures Authority Complaints Bureau, the Office of the Investment Ombudsman and the FSA Direct Regulation Complaints Unit .

The Financial Ombudsman Service derives its authority from the Financial Services and Markets Act which received Royal Assent on 14 June 2000. The principal activity of the company will be the provision of an informal dispute resolution service for consumers of financial products. The Financial Ombudsman Service will formally receive its powers through the enactment of secondary legislation following the Financial Services and Markets Act. In the period from 1 April 2000 to the date on which the Financial Ombudsman Service receives formal power to act, the company will provide management support, staffing and administration for the schemes listed above.

financial results and key activities for the period

The company presents its results for the period from inception to 31 March 2000. During this period the company incurred preparatory set up costs and incurred a net deficit of £2,923,151.

The company's key activities during the period were preparations for the integration of the eight schemes to a single location and arranging the employment of the eight schemes' staff by the Financial Ombudsman Service as of 1 April 2000. Shared infrastructure facilities enabling the provision of a single service have been created. The company signed service level agreements with each of the boards of the above schemes, effective from 1 April 2000, with a view to providing management support, staffing and administration for the existing schemes until the secondary legislation following the Financial Services and Markets Act is enacted.

future developments

The timing of the secondary legislation following the Financial Services and Markets Act will be key to the company's activities in the next financial year, as the secondary legislation will define the date from which the Financial Ombudsman Service has the authority to begin providing an ombudsman service in its own right.

directors and their interests

The directors are set out on page 20. No director has any interests in the transactions of the company.

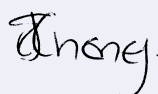
year 2000

The directors continue to be alert to the potential risks and uncertainties surrounding the year 2000 issues. As at the date of this report, the directors are not aware of any significant factors which have arisen, or that may arise, which will affect the activities of the business; however, the situation is still being monitored. Any future costs associated with this issue cannot be quantified but are not expected to be significant.

auditors

Deloitte & Touche were appointed by the directors as auditors and a resolution to reappoint them will be proposed at the forthcoming annual general meeting.

Approved by the board of directors and signed on behalf of the board.



Barbara Cheney
secretary

statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company as at the end of the financial year and of the income and expenditure of the company for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Financial Ombudsman Service Limited
(formerly Financial Services Ombudsman
Scheme Limited)

auditor's report to the members

We have audited the financial statements on
pages 25 to 28 which have been prepared under
the accounting policies set out on page 27.

**respective responsibilities of directors
and auditors**

As described on page 23 the company's directors
are responsible for the preparation of financial
statements which are required to be prepared in
accordance with applicable United Kingdom law
and accounting standards. It is our responsibility
to form an independent opinion, based on our
audit, on those statements and to report our
opinion to you.

basis of opinion

We conducted our audit in accordance with United
Kingdom Auditing Standards issued by the
Auditing Practices Board. An audit includes
examination, on a test basis, of evidence relevant
to the amounts and disclosures in the financial
statements. It also includes an assessment of the
significant estimates and judgements made by the
directors in the preparation of the financial
statements, and of whether the accounting
policies are appropriate to the company's
circumstances, consistently applied and
adequately disclosed.

We planned and performed our audit so as to
obtain all the information and explanations which
we considered necessary in order to provide us
with sufficient evidence to give reasonable
assurance that the financial statements are free
from material mis-statement, whether caused by
fraud or other irregularity or error. In forming our
opinion we also evaluated the overall adequacy of
the presentation of information in the financial
statements.

opinion

In our opinion the financial statements give a true
and fair view of the state of the company's affairs
at 31 March 2000 and of its deficit for the period
then ended and have been properly prepared in
accordance with the Companies Act 1985.

Deloitte & Touche

Chartered Accountants and Registered Auditors
Stonecutter Court
1 Stonecutter Street
London EC4A 4TR

income and expenditure account period ended 31 March 2000

	Note	31 March 2000 £
Expenditure		
Interest payable and similar charges	3	(42,891)
Administrative expenses		(2,880,260)
<hr/>		
Operating loss		(2,923,151)
<hr/>		
Deficit of income over expenditure before taxation	4	(2,923,151)
<hr/>		
Deficit of income over expenditure after taxation transferred from establishment costs recovery fund	10	(2,923,151)
<hr/>		

All amounts relate to continuing activities.

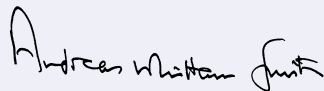
There were no other recognised gains or losses other than the reported deficit for the period.

The notes on pages 27 to 28 form part of these financial statements.

balance sheet at 31 March 2000

	Note	31 March 2000	
		£	£
Fixed assets			
Tangible assets	6	3,787,422	
Current assets			
Debtors	7	264,039	
Cash at bank and in hand		293,750	
		557,789	
Creditors: amounts falling due within one year	8	(1,268,362)	
Net current liabilities		(710,573)	
Total assets less current liabilities		3,076,849	
Creditors: amounts falling due after more than one year			
Bank loan	9	(6,000,000)	
Total net liabilities		(2,923,151)	
Funds			
Establishment cost recovery fund	10	(2,923,151)	

These financial statements were approved by the board of directors on 28 July 2000 and signed on behalf of the board.



Andreas Whittam Smith
chairman

notes to the accounts year ended 31 March 2000

1 status of the company

Financial Ombudsman Service Limited is a company limited by guarantee and registered in England (03725015). The liability of each of the members is limited to the amount of £1 guaranteed in the memorandum of association.

2 accounting policies

The financial statements are prepared in accordance with applicable accounting standards. The particular accounting policies adopted are described below.

accounting convention

The financial statements are prepared under the historical cost convention and in accordance with the applicable accounting standards of the United Kingdom.

income

The Financial Ombudsman Service does not have any income for the period under review and was funded by the Financial Services Authority until 31 March 2000. After 1 April 2000, until the enactment of the secondary legislation following the Financial Services and Markets Act, the company's main income will be in the form of a service charge levied on the existing schemes.

tangible fixed assets

Tangible fixed assets are capitalised at cost. Depreciation is provided at rates calculated to write-off the cost, less estimated residual value, of each asset evenly over its expected useful life as follows:

leasehold premises	Over 10 years
computer software	Over 5 years
computer hardware	Over 3 years
other office equipment	Over 3 years

Assets are depreciated from the start of the financial year following the year in which they are brought into use and bear a full annual charge in the year of disposal.

The carrying values of tangible fixed assets are renewed for impairment in periods if events or changes in circumstances indicate that the carrying value may not be recoverable.

operating lease commitments

Operating lease costs will be charged to the income and expenditure account to reflect usage of the assets leased.

pension costs

The company makes payments on behalf of employees to a money purchase scheme. These payments are charged to the income and expenditure account in the period to which they relate.

cash flow statement

The company is a small company as defined by sections 246 and 247 Company Act 1985. It has therefore taken advantage of the exemption conferred by FRS1 Cash Flow Statements (revised 1996) not to prepare a cash flow statement.

3 interest payable and similar charges

	31 March 2000
	£
Bank loan and overdraft	42,891

4 deficit of income over expenditure

This is stated after charging:

	31 March 2000
	£
Auditors' remuneration:	
Audit fee	12,925
Other services	21,150
Amounts paid under operating leases	–
Pension costs	36,907

5 directors' remuneration

Directors' remuneration payable during the period amounted to £155,597.

6 tangible fixed assets

	Leasehold improvements	Computer equipment and software	Total
	£	£	£
Cost			
Additions	2,950,747	836,675	3,787,422
At 31 March 2000	2,950,747	836,675	3,787,422
Depreciation	–	–	–
Charge for period	–	–	–
At 31 March 2000	–	–	–
Net book value			
At 31 March 2000	2,950,747	836,675	3,787,422

No depreciation has been charged in the period under review as assets are depreciated in the financial year following the year in which they have been brought into use.

7 debtors

	31 March 2000
	£
Prepayments	257,219
Sundry debtors	2,500
Financial Services Authority	4,320
	264,039

8 creditors: amounts falling due within one year

	31 March 2000
	£
Accruals	1,268,362

9 bank loan

	31 March 2000
	£
Bank loan	6,000,000

The company has a revolving loan facility of £25m of which £6m was drawn down at 31 March 2000.

The loan is repayable in instalments by 31 March 2011. The interest rate payable is 0.15% per annum above London interbank offered rates. A commitment fee of 0.07% is charged on the outstanding sum on the revolving loan facility not yet drawn down. The FSA has guaranteed the loan facility.

10 establishment costs recovery fund

	31 March 2000
	£
Deficit for the period and at 31 March 2000	(2,923,151)

The company will be able to recover the expenditure transferred to the establishment costs recovery fund over a period of three years after the enactment of the secondary legislation following the Financial Services and Markets Act.

11 operating lease commitments

The company entered into a fifteen year lease in November 1999 with a rent review every five years. Under the lease the company was entitled to a one year rent free period. Rent has been charged from the date at which the premises became available for occupation. As a result no charge has been made to the income and expenditure account for the period ended 31 March 2000.

At 31 March 2000 the company was committed to making the following payments during the next year in respect of operating leases:

	Land and Buildings 2000
	£
Leases which expire: after five years	529,927