Financial Services Compensation Scheme

Budget Update
January 2023

Chief Executive's **Statement**

Caroline Rainbird
Chief Executive

As we welcome in a new year, I am pleased to introduce our latest *Budget Update*. This provides information regarding our proposed management expenses which are consulted on each year by the FCA and PRA via the Management Expenses Levy Limit (MELL).

Our 2023/24 total levy forecast (including both proposed management expenses and compensation costs) was presented in our *November 2022 Outlook*. I trust this early view of the following year's levy proved helpful for the industry.

The proposed 2023/24 management expenses budget

To meet our running costs, and ensure we are helping our customers get back on track as quickly as possible, we are proposing a management expenses budget of £99.8m - a 5% increase against our budget announced this time last year.

This proposed budget includes a year-on-year reduction in volume-related costs, as we expect claims volumes to remain broadly at the level they are now, which is lower than forecast this time last year. However, this reduction is offset by an increase in our controllable costs due to inflation and the resulting price rises. Through very careful control of our spending, we have kept the increase in our controllable costs to below inflation - at less than 6%.

In addition, our recoveries work plays an important role in reducing the levy we need to raise from the industry. Between April and December 2022, we recovered £4.1m. Of this, £2.5m has been paid to customers who had losses greater than our compensation limits and the balance at the end of the year will be used to offset levies in the relevant funding classes.

2022/23 management expenses latest forecast

Our forecasted running costs for 2022/23 now stand at £89.2m which represents a £6.3m reduction against our budget announced in January 2022.

This is the result of FSCS processing fewer claims than expected, primarily in the Life Distribution and Investment Intermediation and Investment Provision classes. Overall, we expect to make 13,600 fewer claims decisions this year compared to our initial forecast.

Any surpluses remaining at the end of the financial year in March will be used to offset the 2023/24 levy and will be factored into our next *Outlook* update in the spring.

Investing for the future

Last year, I explained that although we have the right teams and systems in place to efficiently process claims and make recoveries today, the sheer complexity of claims now coming to FSCS means that we are likely to see increases in costs over the coming years. To that end, this year's proposed budget includes a £3.9m increase in our investment costs which covers essential enhancements to our technology and processes.

2023/24 will be the first year of a three-year plan to invest in our people and systems. We must enhance our claims handling capabilities and ensure we are able to continue to provide an efficient service in the future – one that is both accessible and swift for consumers who are left out of pocket when a firm fails, and cost-effective for the industry that funds us. This includes critical work to keep pace with customer expectations and learn from other schemes globally, as well as engaging with the Bank of England's review of alternative processes for supporting depositors in the event of bank insolvency.

Handling claims in areas such as pension transfers and SIPP operator failure is growing ever-more complex, and we expect this trend to continue. We must keep our technology up to date, both to handle this increased complexity but also to ensure our customer's information continues to be safe and secure. Part of this investment covers the completion of our Cloud migration project, which is now in its final stages.

There is also a significant amount of regulatory change expected in the coming years, with landmark legislation coming through post Brexit, to help the UK identify opportunities to improve its rules and benefit from its position as a non-EU member. We will also be working closely with the FCA and others on the next stages of the Compensation Framework Review, which the FCA recently published an update on.

To ensure we can respond to changes as they arise, as well as look ahead and plan for the future, we are also investing in both recruiting new expertise and developing our own people. Our aim is to develop our own in-house capabilities in vital areas such as data, insight and policy. In doing so, we can build on the work we have started this year, sharing research and views on important topics such as the compensation framework and consumer trust and confidence. This will not only help FSCS make change efficiently, but also allow us to continue to make valuable contributions to work in the wider financial services ecosystem – including through the Wider Implications Framework.

As I have said many times before, it is only through collaboration and collective effort that we will solve the problems facing consumers and our industry, bringing greater stability whilst also creating the right environment to innovate and stimulate growth.

Our proposed budget is now being jointly consulted on by the FCA and PRA until 9 February 2023.

Caroline Rainbird
Chief Executive

FSCS Budget **Update**

January 2023

In this publication we present our management expenses which includes our day-to-day running costs, as well as the costs associated with processing claims.

Please note: the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) will also be consulting on our 2023/24 management expenses as part of the yearly Management Expenses Levy Limit (MELL) consultation.

The proposed budget for 2023/24 is £99.8m

This represents a £4.3m (5%) increase on the budget that was confirmed by the PRA and FCA in March 2022. This includes a:

- **£3.9m** increase in investment to deliver essential strategic initiatives and the ongoing enhancement of FSCS processes and customer services;
- **£3.2m** increase in controllable costs due to rising prices – i.e. rent and costs associated with critical business support functions such as IT and HR. This is a 5.9% increase, which is below inflation at 8.6% (published by the Office of National Statistics, September 2022); and
- **£2.8m** reduction in volume related costs, i.e. all costs associated with investigating and assessing claims, due to the expectation that fewer claims will be processed than the 2022/23 budget.

We also propose an unlevied reserve of £10m for 2023/24

The FCA and PRA are consulting on an overall MELL of **£109.8m**. This takes into account a **budget of £99.8m** and an unlevied reserve of **£10m**. This contingency (£10m) ensures we have the funds to process a significant increase in claims for any unexpected large firm failures, should they arise. This is £5m less than the contingency fund proposed in 2022/23.

Please note, the unlevied reserve is only invoiced to firms if deemed necessary.

Table 1 - 2023/24 budget proposal vs 2022/23 budget

Category	2023/24				2022/23				Variance			
	Budget (£m)	Controllable costs (£m)	Volume and complexity driven (£m)	Investments (£m)	Budget (£m)	Controllable costs (£m)	Volume and complexity driven (£m)	Investments (£m)	Total variance (£m)	Controllable costs (£m)	Volume and complexity driven (£m)	Investments (£m)
Staff costs	32.2	25.2	6.7	0.3	27.2	21.0	6.2	-	(5.0)	(4.1)	(0.5)	(0.3)
Non-project contractor costs	13.2	0.7	10.1	2.4	7.4	0.5	5.7	1.2	(5.8)	(0.2)	(4.4)	(1.2)
Facilities	2.4	2.4	-	-	2.2	2.2	-	-	(0.2)	(0.2)	-	-
IT	6.5	5.9	0.6	-	6.0	5.5	0.5	-	(0.4)	(0.4)	(0.0)	-
Communications	4.4	4.2	0.3	-	3.8	3.8	-	-	(0.6)	(0.4)	(0.3)	-
Legal and professional	16.7	8.9	2.7	5.2	14.4	8.9	2.7	2.8	(2.4)	(0.0)	(0.0)	(2.4)
External providers	0.6	0.5	0.0	-	0.6	0.5	0.0	-	(0.0)	-	(0.0)	-
Depreciation	1.4	1.4	-	-	1.4	1.4	-	-	0.1	0.1	-	-
Other / contingency	0.5	0.5	-	-	0.5	0.5	-	-	(0.0)	(0.0)	-	-
Outsourced claims handling	13.6	-	13.6	-	21.4	-	21.4	-	7.8	-	7.8	-
Outsourced printing and scanning services	0.5	0.4	0.1	-	0.6	0.4	0.3	-	0.2	-	0.2	-
Bank charges	8.0	8.0	-	-	8.0	8.0	-	-	-	-	-	-
Pension deficit funding	0.8	0.8	-	-	1.9	1.9	-	-	1.1	1.1	-	-
Interest income	(0.9)	(0.9)	-	-	-	-	-	-	0.9	0.9	-	-
Management expenses	**99.8**	**57.9**	**34.0**	**7.9**	**95.5**	**54.7**	**36.8**	**4.0**	**(4.3)**	**(3.2)**	**2.8**	**(3.9)**
Unlevied reserve	10.0	-	10.0		15.0	-	15.0		5.0	-	5.0	-
MELL	**109.8**	**57.9**	**44.0**	**7.9**	**110.5**	**54.7**	**51.8**	**4.0**	**0.7**	**(3.2)**	**7.8**	

Table 2 - 2023/24 management expenses split by PRA and FCA classes

	2023/24			2022/23			Variance		
	FSCS total costs (£m)	Fee block allocation		FSCS total costs (£m)	Fee block allocation		FSCS total costs (%)	Fee block allocation	
		PRA (£m)	FCA (£m)		PRA (£m)	FCA (£m)		PRA (%)	FCA (%)
Base costs total (split 50:50)	**38.3**	**19.2**	**19.2**	**29.9**	**15.0**	**15.0**	**28%**	**28%**	**28%**
Specific costs									
Deposits	14.1	14.1		14.1	14.1		0%	0%	
General Insurance Provision	7.6	7.6		7.2	7.2		6%	6%	
Life and Pension Provision	-	-		-	-		-	-	
General Insurance Distribution	1.7		1.7	5.9		5.9	(71%)		(71%)
Life Distribution and Investment Intermediation (LDII)	30.3		30.3	27.7		27.7	9%		9%
Investment Provision	7.0		7.0	9.7		9.7	(27%)		(27%)
Home Finance Intermediation	0.8		0.8	1.0		1.0	(18%)		(18%)
Debt Management	-		-	-		-	-		-
Specific costs total	**61.5**	**21.7**	**39.8**	**65.6**	**21.2**	**44.3**	**(6%)**	**2%**	**(10%)**
Management expenses total	**99.8**	**40.8**	**59.0**	**95.5**	**36.2**	**59.3**	**5%**	**13%**	**0%**

The latest forecast for 2022/23 is £89.2m

We expect to end this financial year £6.3m below budget compared with the 2022/23 budget announced in January 2022 (£95.5m).

As outlined in November's *Outlook*, we now expect to pay out compensation on fewer claims, most of which relate to the Life Distribution and Investment Intermediation and Investment Provision classes.

Further, we will not be using the unlevied reserve (£15m) and any budget surpluses (currently £6.3m) will be used to help offset the levy for the relevant classes in 2023/24.

Table 3 - 2022/23 latest forecast vs 2022/23 budget

Category	2022/23 latest forecast			2022/23 budget			Variance		
	Budget (£m)	Controllable costs (£m)	Volume and complexity driven (£m)	Budget (£m)	Controllable costs (£m)	Volume and complexity driven (£m)	Total variance (£m)	Controllable costs (£m)	Volume and complexity driven (£m)
Staff costs	27.0	21.6	5.4	27.2	21.0	6.2	0.3	(0.5)	0.8
Non-project contractor costs	10.4	1.2	9.2	6.2	0.5	5.7	(4.2)	(0.6)	(3.5)
Facilities	2.2	2.2	0.0	2.2	2.2	-	0.1	0.1	(0.0)
IT	6.6	6.1	0.5	6.0	5.5	0.5	(0.5)	(0.6)	0.0
Communications	3.8	3.8	-	3.8	3.8	-	0.1	0.1	-
Legal and professional	12.1	9.3	2.9	11.6	8.9	2.7	(0.6)	(0.4)	(0.2)
External providers	0.4	0.4	0.0	0.6	0.5	0.0	0.2	0.2	0.0
Depreciation	1.1	1.1	-	1.4	1.4	-	0.4	0.4	-
Other / contingency	0.5	0.5	0.0	0.5	0.5	-	(0.0)	(0.0)	(0.0)
Outsourced claims handling	12.4	-	12.4	21.4	-	21.4	8.9	-	8.9
Outsourced printing and scanning services	0.3	0.3	0.1	0.6	0.4	0.3	0.3	0.1	0.2
Strategic change portfolio	4.3	4.3	-	4.0	4.0	-	(0.3)	(0.3)	-
Bank charges	6.9	6.9	-	8.0	8.0	-	1.1	1.1	-
Pension deficit funding	1.3	1.3	-	1.9	1.9	-	0.6	0.6	-
Management expenses	**89.2**	**58.7**	**30.5**	**95.5**	**58.7**	**36.8**	**6.3**	**(0.0)**	**6.3**

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