

**26<sup>th</sup> January 2005**

## **FSCS' Plan and Budget aims to strike a balance between the needs of consumers and levy payers**

The Financial Services Compensation Scheme (FSCS/the Scheme) has today (Wednesday) published its Plan and Budget for 2005/06, including present estimates of levies to be fixed in March.

### **Loretta Minghella, FSCS' new Chief Executive says:**

“This is the first time we have published our Plan and Budget. In doing so, we are responding to calls from the industry and consumer representatives for more information about our work.

Our Plan rests on our best forecasts of the number, nature and value of claims we will receive in 2005/06. Information about possible claims changes daily, and, by the time it comes to fixing the levies in March, our forecasts may well have changed. Levies may therefore be higher or lower than those predicted here.

Nevertheless, publishing forecasts at this early stage meets calls from the industry for early notice of likely costs, to enable firms to make prudent provision for the levies they may have to pay. It also provides reassurance to consumers that we will be sufficiently funded to deal effectively with the claims we expect them to send our way.

The overall costs of compensation are expected to be lower next year, but for some parts of the industry, the costs will be significantly higher than before.

We recognise that, whilst consumers do need a prompt, but considered, response to their claims, we also have to ensure our levy payers do not pay any more than they need to for the mistakes or misdeeds of others. Our Plan and Budget provides a clear and sensible strategy for striking a balance between the needs of those who use our service and those who pay for it.”

The Plan provides the basis for the Scheme's proposed Management Expenses Levy Limit of £27.03m, which is currently being consulted on by the Financial Services Authority (FSA). Under the rules for FSCS the management expenses are subject to an annual limit, known as the Management Expenses Levy Limit, which is set each year after consultation.

The Plan provides background information about the work of FSCS and includes details of:

- i. FSCS' latest forecasts for the financial year 2004/05 for claims, compensation payments and management expenditure;

- ii. the estimated numbers of claims the Scheme expects to handle in 2005/06 and how it intends to manage these, including the resourcing strategy;
- iii. current predictions of the levies FSCS estimates it may need to raise in 2005/06, including compensation payments and management costs. The current estimate for the total levy for 2005/06 is £202.9m. (See below for more details).

**The key points of the Plan and Budget are:**

**Current estimates for 2005/06 levies**

FSCS currently estimates that the prospective levy for 2005/06 will be £202.9m, compared to the levy of £218.2m<sup>1</sup> called for in 2004/05. The Scheme expects to pay somewhere in the region of £255m in compensation during 2005/06. Although the total levy on the financial services industry as a whole for compensation and management costs is likely to be lower than last year, investment brokers and advisers will see another significant increase in levies and fund managers should expect to see a significant increase in levies for the first time.

**Levy proposals by contribution groups**

<i>Contribution group</i>	<i>Ref</i>	<i>2004/05 Actual levy £m</i>	<i>2005/06 Prospective levy £m</i>	<i>Increase / (decrease) £m</i>
<b>Accepting deposits</b>				
Deposit takers	A1	0.0	0.0	0.0
<b>Insurance</b>				
General insurance	A3	135.0	95.0	(40.0)
Life insurance	A4	0.0	0.0	0.0
<b>Investments</b>				
Fund managers	A7	0.1	27.0	26.9
Managers of AUTs, ACDs and depositories	A9	0.5	0.7	0.2
Dealing as principal	A10	0.3	0.0	(0.3)
Brokers holding client money	A12	7.2	16.0	8.8
Brokers not holding client money	A13	25.4	30.0	4.6
Corporate advisers	A14	0.1	0.1	0.0
<b>Pensions review</b>	(A16)	64.1	32.0	(32.1)
<b>Mortgage brokers</b>	A18	0.0	0.4	0.4
<b>Insurance intermediaries</b>	A19	0.0	1.7	1.7
<b>Totals</b>		<b>232.7<sup>1</sup></b>	<b>202.9</b>	<b>(29.8)</b>

<sup>1</sup>Levy called for was £218.2m. Further cash amounts have been received as firm tariff amounts were updated.

## Claims forecasts for 2005/06

FSCS is forecasting a 53% rise in new claims, from 13,400 to 20,500 during the year.

Type of claim	Claims in hand Forecast at 1 April 2005	Estimate of new claims	Estimate of claims completed	Claims in hand Forecast at 31 March 2006
Investments:				
Endowments	5,100	7,000	8,400	3,700
Precipice bonds	1,900	3,600	4,600	900
Others, inc. splits	700	8,800	4,200	5,300
<b>Total investments</b>	<b>7,700</b>	<b>19,400</b>	<b>17,200</b>	<b>9,900</b>
Pensions review	4,100	100	4,200	0
Credit unions	40	0	40	0
M&GI firms <sup>2</sup>	0	1,000	700	300
<b>Total claims</b>	<b>11,840</b>	<b>20,500</b>	<b>22,140</b>	<b>10,200</b>
Insurance payments <sup>3</sup>	-----	12,000	12,000	-----

<sup>2</sup> Mortgage and general insurance firms

<sup>3</sup> Figures relate to payments only. Insurance claims are usually handled by the appointed run-off agent and presented to FSCS for checking and payment.

FSCS includes in these estimates:

- **known** claims - for defaults already declared, or about to be declared;
- **probable** claims - although the actual volume and timing of claims may not be clear at the time of preparing the budget, it is prudent for the Scheme to make provision for areas that it believes are likely to give rise to claims in the financial year.

### Reserve contingency

Prospective claims – those that are not yet sufficiently likely to warrant providing for in the central budget – are not included, but FSCS proposes including a reserve contingency of £5.6m within the Management Expenses Levy Limit for the costs of handling these claims if they arise. This gives FSCS the flexibility to handle additional claims if they materialise, although the Scheme will not levy for these costs if they don't.

FSCS does not include in its budget or contingency arrangements possible areas of work that, at the time of preparation, are too remote. It follows that, in the event of material developments during the year, the Scheme might need to review the adequacy of its budgetary provision. If an increase in the Management Expenses Levy Limit were needed, further consultation by the FSA would be necessary.

### FOR FURTHER INFORMATION CONTACT:

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## Notes for editors

The full Plan and Budget is available at: [www.fscs.org.uk/publications](http://www.fscs.org.uk/publications)

A summary of the Plan is contained in the Scheme's industry newsletter, *OUTLOOK*, which is being sent to all authorised firms this week. Copies are available at [www.fscs.org.uk/publications](http://www.fscs.org.uk/publications)

### Updated forecasts for 2004/05

FSCS forecasts that management expenses for 2004/05 will be £14.6m, against a revised budget of £16.9m (announced in July 2004) and an original budget of £11.8m. Compensation payments are expected to be in the region of £223.6m.

During 2004/05 the Scheme has focused on managing increased claims volumes, the inclusion of mortgage and general insurance firms, and meeting financial and budgetary savings targets. It has continued to review its work processes to maximise efficiencies, improve service to claimants and reduce running costs where possible.

To meet increased workloads the Scheme expects to increase staff to around 180 by the end of 2004/05, an increase of 48% compared to March 2004. Dedicated teams have been established for mortgage endowment and precipice bond claims. The Scheme does not expect claims against mortgage firms to be significant. Some claims relating to general insurance mediation are expected, and a separate team has been established to handle these.

### Claims forecasts for 2004/05

Type of claim	Claims in hand at 1 April 2004	Estimate of new claims	Estimate of claims completed	Claims in hand Forecast at 31 March 2005
Investments:				
Endowments	2,600	6,000	3,500	5,100
Precipice bonds	300	3,000	1,400	1,900
Others, inc. splits	300	900	500	700
<b>Total investments</b>	<b>3,200</b>	<b>9,900</b>	<b>5,400</b>	<b>7,700</b>
Pensions review	5,000	3,100	4,000	4,100
Credit unions	60	400	420	40
M&GI firms <sup>4</sup>	0	0	0	0
<b>Total claims</b>	<b>8,260</b>	<b>13,400</b>	<b>9,820</b>	<b>11,840</b>
Insurance payments <sup>5</sup>	-----	25,400	25,400	-----

<sup>4</sup> Mortgage and general insurance firms

<sup>5</sup> Figures relate to payments only. Insurance claims are usually handled by the appointed run-off agent and presented to FSCS for checking and payment.