FSCS Financial Services Compensation Scheme

Plan and Budget: 2018/19

Financial Services Compensation Scheme

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Chair's Foreword

Lawrence Churchill
Chairman

This will be the final FSCS *Plan and Budget* I introduce. My second and final term as Chair comes to an end in March after six challenging, but hugely enjoyable, years.

This is, therefore, a good moment to reflect on the distance FSCS has travelled over those years as it completes, in the year ahead, the five-year strategy we began in 2014.

What has changed over these years?

First and foremost, I should say that FSCS is now a more resilient and better controlled organisation than it was when I arrived.

Then, as now, FSCS's business model relied on outsourcing the great majority of non-deposit claims. This was, and is, an intelligent strategy for dealing with an unpredictable and volatile workload. It enables FSCS to transfer the volume risk to bigger organisations better equipped to manage it.

But outsourcing when I arrived was a paper-driven exercise, with claims passing physically between FSCS and its outsource partners. Those outsource partners maintained separate records of the claims they were handling.

This was cumbersome and inefficient, with risks to data security and to reliable management information.

Now, thanks to the investments we have made in our claims handling, FSCS and its partners operate on a common platform. All claims move electronically. All data is held securely by FSCS. This enables FSCS and its partners to respond efficiently to changes in the volume and complexity of claims.

And, of course, there have also been big benefits to the speed and quality of service we offer our customers. Mark Neale talks more about this in his overview on page 6.

In 2018/19, FSCS will complete the re-tendering of its claims handling and enter a new arrangement with a single partner, which will generate new investment in our process and cost efficiencies, as well as enabling us further to improve our service to customers.

Alongside this investment in our physical resilience, I should also highlight FSCS's effective integration into resolution planning by the authorities and the accompanying gain in clarity about the scale of failure to which FSCS might be asked to respond. This is part of the work that has been done to ensure that financial services

£100m

returned to industry as a result of recoveries following Keydata failure

businesses can fail safely, without undermining financial stability or transferring the costs of failure to taxpayers.

When I arrived as Chair, we lacked, for example, certainty about the size of bank or building society FSCS might be asked to payout in the event of failure. As I leave, there is a clear resolution plan for every deposit-taker set by the Bank of England and FSCS knows exactly which firms would be resolved through insolvency and payout. We are fully confident that we would be able to compensate the great majority of depositors in those firms within seven days. We have done so for savers in 34 credit unions, which failed during my time as Chair.

What is more, public awareness of FSCS protection is now at record levels – around three-quarters of adults know about our protection or know of FSCS specifically. In 2012, awareness of FSCS protection was significantly lower.

The challenge for FSCS will now be to achieve wider public awareness of its protection of other products – a pressing concern as the public exercises increasingly important financial choices, particularly about retirement. Clarity about FSCS's protection is critical here and I am delighted that the Financial Conduct Authority (FCA) took an important step in this direction in October, when it proposed increasing FSCS's protection for investments and investment advice to £85,000.

If FSCS is now better equipped to deal with future challenges, it has also done a good job of clearing away the legacy of past ones.

At the time of my appointment as Chair, FSCS still owed HM Treasury £18bn as a result of the money we borrowed in 2008 to meet the costs of compensating depositors in the banks that failed then. We were levying the industry £370m in interest charges annually. To match this borrowing, FSCS had a corresponding stake in the estates of the failed firms.

Thanks to FSCS's work to achieve recoveries, we have now repaid HM Treasury all but £4.7bn of that borrowing. The interest payment in 2018/19 will be down to less than £100m. What is more, I fully expect the remaining borrowing to be repaid within a month or two of my departure, as HM Treasury completes the sale of another tranche of the Bradford & Bingley mortgage book.

FSCS's work on recoveries is too little known, but makes a real financial contribution to the industry. In my time as Chair, FSCS also returned a net £100m to the industry as a result of its recoveries following the Keydata failure.

Finally, and perhaps appropriately in the context in which I am writing, I should say FSCS is significantly more transparent in its budgeting and financial reporting.

As you will see from this *Plan and Budget*, we now present our management expenses on an activity basis so that our levy payers can see exactly what outcomes their levies are paying for. And we now publish annually, alongside our Annual Report and Accounts, a separate document setting out the cash flows over the year – the compensation costs, levies and recoveries - for each industry sector, so that firms can see exactly how each of the class balances has been determined.

I shall not be in the Chair to see the delivery of the *Plan and Budget* published today, but I wish my successor and FSCS well in taking this work forward. I am quite sure that FSCS will continue to protect consumers even more effectively in future and, in doing so, continue as an important guarantor of financial stability.

I am also sure that FSCS's people will continue to give their whole-hearted commitment to this task and bring to bear their outstanding professionalism on the challenges ahead. Working with FSCS's people has always been a pleasure and perhaps the outstanding memory of my six years as Chair.

Chief Executive's Overview

Mark Neale
Chief Executive

£3.5m
rise in total management expenses budget to just under £73m

The *Plan and Budget* for 2018/19 we publish today bridges FSCS's current strategy, which concludes next year, and our strategy for the early 2020s which we expect to publish later in 2018.

As Lawrence Churchill describes in his foreword, our current strategy has involved investment in our handling of non-deposit claims. This complements the investment we made at the beginning of the decade in the capacity to deliver seven day payout of deposits in failing banks, building societies and credit unions.

We are now seeing the benefits from these more recent investments in a claims handling platform which we share with our outsource partners and in an online portal through which our customers have been able to make claims since December 2016.

In fact, we have realised greater benefits sooner than expected.

By the end of 2017 we were receiving over 80 per cent of claims online. We set ourselves the target of achieving 60 per cent by March 2019. The advent of the online service has coincided with significant improvements in customer satisfaction, now at 83 per cent - well above the 70 per cent threshold we expected to achieve by the end of next financial year. And FSCS is turning around high and increasing levels of claims within our service level targets (see Appendix).

The electronic transmission and handling of claims has also contributed to marked reductions in costs. We estimate that, like-for-like, our claims handling costs by the end of 2017/18 will be £2m lower than they would otherwise have been.

That saving is, however, disguised in the budget we publish today by a continuing rise in the volume and complexity of claims which we expect next year, generating offsetting additional costs.

£1m

fall in our investment budget to £8m

As usual, our *Plan and Budget* sets our latest forecast of potential claims volumes and associated compensation costs for 2018/19. You will note, however, that, in order to align our levy and financial years[1], our forecasts for next year cover the nine months from 1 July 2018 to 31 March 2019. Where relevant, we have pro-rated the annual levy limits commensurately so that firms will be levied no more than 75 per cent of the annual limit over these nine months. This follows the approach proposed by the FCA's Consultation Paper 18/1 for the transition of FSCS to a common financial year for raising the levy and applying the limits.

Against this background, our *Plan and Budget* for 2018/19 rounds off our existing five-year strategy.

We are, in particular, taking steps to enhance FSCS financial and organisational resilience. To this end, we are increasing to £1.45bn the size of the revolving credit facility with a consortium of banks which would enable us to fund a seven-day payout of a failing bank or building society. Under the current formula, this adds £1.7m to next year's budget. And, in the light of the lessons learned from the failure in 2016 of Enterprise Insurance Company plc, we are migrating the handling of insurance data onto our core system at a cost of £0.5m.

We also make provision in this year's budget for the renewal of our office IT, for the strengthening of our risk and control function and for Brexit preparation.

Taken together, these resilience and other costs account for the rise of £3.5m in the total management budget to just under £73m.

We are also paving the way for the 2020s.

Our investment budget falls by £1m to £8m, but we are taking important steps to enable better customer service and more efficient operation in the years to come.

Most importantly, our plan for 2018/19 provides for the introduction, at a cost of £1.5m, of a new single partner to handle the majority of our claims, following a year-long and rigorous procurement exercise, which is due to complete soon. This partner will take over in the summer and replace the current panel of three providers.

We expect this new partnership, which we hope will last five years or more, to yield significant benefits. As a sole supplier, our partner will have a strong incentive to invest in our claims-handling process to achieve further efficiency savings and customer service improvements.

We shall also invest a further £2m next year in the development of our digital service where, despite the success of our online portal, we lag well behind not just the industry, but also customers' reasonable expectations. We are particularly conscious of the need to exploit digital technology to eliminate the delays in processing claims as we gather supporting evidence, and to provide our customers with better information about progress, as well as clear explanations of decisions.

We are, in short, in good shape to face the challenges ahead. We very much welcome feedback on our plans for 2018/19.

[1] Our *Outlook*, published January 2018, provides full information about the basis on which the FSCS Board decided to bring about the alignment of levy and financial years provided for in the rule change made by FCA in October 2017.

Strategic Direction: taking forward our Five-Year Vision

83%
customer satisfaction (against the 70% imperative target)

Four years ago, when we published our five-year strategy we set out to strengthen FSCS's capability in seven key respects: the seven imperatives.

The stated imperatives were:

- Serving our customers by modernising our service
- Diversifying how we deliver compensation to provide maximum convenience and continuity for consumers
- Improving value for money (VFM) to drive value and strengthen accountability
- Deepening contingency planning to be ready to respond effectively to crises
- Achieving excellence as a creditor
- Raising awareness of the protection FSCS provides
- Engaging our people to be even more agile and professional

Since 2014, we have made substantial progress and in some areas exceeded our ambitions. This time next year, we will be moving to a new strategy, in order to adapt to the evolving and increasing demands of the public and stakeholders. Many of the themes will still be relevant – but the ambition and goals of FSCS will be restated. We shall engage with stakeholders over the next few months on the development of our strategy.

We shall launch the new strategy in Autumn 2018, but are already preparing. We shall move to a single outsource partner, bringing greater investment and further enhancements to our customer experience and building on the progress made to date. We shall further enhance our digital experience for customers by more closely aligning all our online platforms, including the claims service and website. We shall also boost our operational and financial resilience.

Ahead of the launch, it is appropriate in this Plan and Budget, as the last prepared under the five-year vision launched in 2014, to review the performance against the seven imperatives. Our customer service is much enhanced, thanks to our investments in technology and process. We improved our value for money and the transparency of our reporting. There has been significant innovation in how we deliver our service – most recently, for example, we enabled continued cover for some Enterprise and Gable policyholders. Awareness of protection is now at record levels, the legacy of the 2008 banking failures is now mostly resolved, we are in a position of greater preparedness for future failures thanks to planning and testing work and we have become a more professional and resilient organisation.

Providing an excellent customer experience is a key aim in our overall mission to deliver a trusted compensation service. The launch of our customer portal in December 2016 laid the foundation for our digital service. In June 2017, we built on this success with the introduction of an online claims service for claims management companies, submitting claims on behalf of their customers. Customer satisfaction has risen steadily – now at 83 per cent (from 76 per cent last year and against the 70 per cent imperative target) – with a target of 85 per cent for the end of the year. We reduced processing times considerably, by an average of 170 days, with 96 per cent of all claims processed within our targets. 97 per cent of direct customers (those who contact the FSCS themselves, rather than through a claims management company) are using the portal to submit their claim rather than filling out a paper application. Following the extension of our online claims service for representative companies, by November 2017, 128 representative firms had registered to use our online claim service, with approximately 95 per cent of representative claims being processed through this channel.

We are pleased with our customer experience achievements so far, but will continue our efforts to make it easier for our customers to make a claim, communicate with us and receive their compensation. We have been trialling a webchat service to give online support to our customers. The pilot has been very successful, with customer satisfaction for those trialling the channel at 90 per cent on average. We have also improved our online claims service so that our customers receive regular messages on the progress of their claim, keeping them as up to date as possible.

Last year we said that we were keen to examine the options for accelerated payouts, primarily in the event of a bank, building society or credit union failure, in order to provide faster liquidity to customers than our current method of payment by cheque or cash from a local post office. We anticipated some external spend to support a feasibility analysis of the options, but during this year, we have explored the opportunity to capitalise on our work in establishing a claims portal as a possible vehicle for electronic payments, and discussed with industry how the fast developing market solutions might assist. We wish to continue that work into 2018/19 and will engage closely with the Authorities on any possible solutions.

In pursuing the customer imperative, we continue to focus on achieving efficiencies throughout our core business as our operating model evolves and we improve our use of technology. We also commissioned an independent external benchmarking exercise of our cost base. The results show that FSCS is broadly in line with its comparators.

The biggest driver of costs is the volume and mix of claims we deal with, so our focus continues to be improving value for money in the claims-handling process. The investments we have made will have reduced like-for-like claims handling costs by £2m annually by April 2018, compared to pre-investment costs. As we consolidate our outsourced claims-handling processes and move to a single outsource partner, this will pave the way for a stronger partnership relationship in this key area, from which we expect greater efficiencies will come.

In our contingency planning, we work closely with the Authorities and wider industry to identify and respond to emerging risks. FSCS has performed a number of tests and exercises over the year. An example of this was a large-scale simulation exercise, designed to demonstrate and test our response to the failure of a bank. This exercise involved the end-to-end payout process, including resolution notification, 7-day payout and the treatment of those more complex claims, as well as our communication and funding protocols. We learnt useful lessons and overall this validated our planning assumptions and showed our plans for such a failure are fit for purpose.

We have also performed testing with other European Union schemes to simulate our response to a cross-border failure. Next year, we shall continue with our plan to carry out further testing, as required by the Deposit Guarantee Schemes Directive, including a cross-border failure and a funding exercise with the Authorities.

We do not only plan for deposit-taker failures, but routinely ensure that our contingency plans are maintained and exercised across the full range of FSCS protection. In 2017/18, we performed a test of our ability to recover from a major failure of our IT systems, with the added complexity of a reduced recovery time window. This provides assurance that in the event of a significant IT disruption, we are able to recover services in a timely and effective manner. In 2018/19, we shall further our work in relation to incident and crisis management, focusing on our response to cyber-related events.

Pursuing recoveries is one of FSCS's statutory functions. We recognise that recoveries reduce the burden on levy payers and accordingly seek to maximise them, whether through dividends from insolvency estates or other third party sources. We are now close to completing the claims against the legacy bank failures of 2008. This year, we have reduced our debt to HMT in respect of Bradford & Bingley (B&B) by £11bn to £4.7bn as a result of sales of mortgage assets by B&B, with this recovery substantially reducing the amount of interest incurred on the loan from 25 April 2017 onward. We expect to repay the remaining amount in 2018/19 following a further sale of the B&B mortgage assets.

Over the years, other sectors have received substantial recoveries such as from Keydata. This year, we have secured significant recoveries in relation to PPI litigation, with legal proceedings still ongoing. And into next year, we shall increase our focus on pursuing cross-jurisdictional recoveries where the underlying investment (in SIPP mis-selling and other similar cases) has failed. For example, in the context of the failed property developments relating to Harlequin in the Caribbean, where FSCS has paid compensation worth around £100m to 2,500 consumers following SIPP-related mis-selling by IFAs. FSCS has been pursuing recoveries in the insolvencies of Harlequin entities in both St Vincent and the Grenadines and St Lucia.

Alongside the customer experience, communicating the protection we provide for millions of people is central to our vision and mission to build and maintain trust in the financial services industry. Our research shows clearly that hearing about FSCS reassures people. This translates into trust in the industry, too, and aids financial stability.

Our continuing awareness campaign has sustained a high level of awareness among all UK adults (77 per cent). Our campaign is deposit-focused, but we pursue multi-channelled communications across all the products we protect - FSCS has featured in more than 4,800 media articles and 8,000 social media mentions during the year; our PR and social media reached 83 per cent of UK adults with our messages an average of 79 times. We are keen for the industry to take further responsibility for awareness, and get the right messages to their customers at the right time. This year, we signed a voluntary agreement with deposit takers to use our "Protected" badge in communications and advertising. Next year, we aim to develop an industry-wide agreement on promoting our protection for life and pensions, and have set up a working group with the industry for that purpose.

Both to complete our ongoing imperatives and to deliver our future strategy, we recognise the need to continue the transformation of our systems, processes and cultural change. During 2017, we piloted a new approach to performance management ("Performance Achievement"), built around the key pillars of personal development, measures and metrics and priorities, and a new approach to talent management. Next year, we will implement our workplace transformation, rolling out new infrastructure and technology to enhance collaborative and flexible working.

We are also pleased to report that we were recognised in the Employee Benefits Awards 2017 for Best Employee Value Proposition and FSCS was shortlisted in the Business in the Community Responsible Business Awards for our work on supporting older workers.

Management Expenses

The FSCS Board approved a management expenses budget of £72.7m.

This budget represents an increase of £3.5m compared to the 2017/18 budget. The PRA and the FCA are consulting on the overall FSCS management expenses levy limit of £77.7m, allowing for an unlevied contingency reserve of £5m. The consultation is open from Thursday 18 January to Friday 16 February 2018.

In figure 1 we show these costs on an activity basis as developed in 2017/18 and which will be our primary reporting view going forward.

The key drivers for the 2018/19 budget stem from our continuing focus on improving customer service, resilience, control and efficiency.

- **Outsourced claims handling – flat compared to 2017/18, but includes**:

  Efficiency savings of £2m from the benefits of past investments and from the move to a single outsource partner offset by an increase of £2m because of increased complexity (PPI and pensions) and higher volumes (PPI).

- **IT, facilities and central services – increase of £2.7m primarily**:

  Due to provisions made for activities related to Brexit, the renewal of office IT, strengthening of the risk function and the implementation of outcomes from the FCA's review of FSCS funding.

- **Bank charges - increase of £1.7m**:

  We will raise our revolving credit facility limit (from £1.1bn budgeted in 2017/18 to £1.45bn), increasing our capacity to finance major failures, in particular of any banks or building societies – where we aim to pay the majority of depositors in seven days. In addition, we will continue to prepare for actual and potential failures, maintaining current payout obligations.

- **Depositor protection – decrease of £0.4m**:

  We are looking to align more closely our customer experience and communications to increase trust in FSCS. Alongside deposit awareness, we will seek to build knowledge of FSCS protection of pensions, insurance and investments.

Figure 1: Management expenses budget – by activity

	2017/18 Budget (£m)	2018/19 Budget (£m)
Claims handling infrastructure and support	**50.2**	**51.0**
Outsourced claims handling	16.2	16.2
Internal claims handling support	7.4	7.5
IT, facilities and central services	20.1	22.8
Investment: systems maintenance and improvement	6.5	4.5
Bank charges	**5.9**	**7.6**
Depositor protection, investment, recoveries and pension deficit	**13.1**	**14.1**
Depositor protection	4.7	4.3
Recoveries	4.0	3.9
Investment: digital and outsourcing	2.5	3.5
Pension deficit funding	1.9	2.4
Total management expenses	**69.2**	**72.7**

£72.7m

proposed management expenses budget for 2018/19

£5m
Reserve for 2018/19, slightly lower than the level last year

Figure 2: Split of management expenses for 2018/19

	FSCS Total costs (£m)	PRA fee block allocation (£m)	FCA fee block allocation (£m)
Base costs total (Split 50:50)	**25.7**	**12.8**	**12.8**
Specific costs			
Deposits (SA01)	14.0	14.0	-
General Insurance Provision (SB01)	6.9	6.9	-
General Insurance Intermediation (SB02)	7.8	-	7.8
Life and Pensions Provision (SC01)	-	-	-
Life and Pensions Intermediation (SC02)	9.2	-	9.2
Investment Provision (SD01)	-	-	-
Investment Intermediation (SD02)	7.9	-	7.9
Home Finance Intermediation (SE02)	1.2	-	1.2
Specific costs total	**47.0**	**20.9**	**26.1**
Management expenses total	**72.7**	**33.7**	**39.0**

Figure 3: MELL Annex

	2017/18 Budget (£m)	2018/19 Budget (£m)
Staff Costs	17.8	17.8
Contractor Costs	0.8	0.8
Facilities	2.9	3.1
IT	3.8	3.9
Communications	4.0	3.7
Legal and Professional	4.1	4.0
External Providers	0.9	1.6
Depreciation	0.2	0.4
Other	0.5	1.1
Outsourced Claims	14.4	15.0
Outsourced Printing	0.9	0.7
Resilience - Insurance	0.0	0.5
Investment - Digital	1.1	2.0
Investment - Outsourcing	1.4	1.5
Investment - Sustain/Improve	6.5	4.5
Bank charges	5.9	7.6
Recoveries litigation	2.1	2.1
Pension	1.9	2.4
Total	**69.2**	**72.7**

- **Investment – the total spend is decreasing by £1m to £8m**:
  - Maintain/Improve – we shall spend £4.5m on enhancements to our core applications, infrastructure and equipment;
  - Digital – £2m will be committed to our plans to harness digital technology to improve customer service and further reduce costs;
  - Outsourcing – £1.5m represents the one-off costs of switching to, and on-boarding of, our single partner.
- **Pension deficit funding – increase of £0.5m**:

  The next revaluation will be as at 1 April 2018 and following recommendations made by the Trustees, we have budgeted for an increase to the annual contributions by £0.5m as current indications show we are behind on the Recovery Plan.
- **Allocation to funding classes**

Like last year, we have split the 2018/19 management expenses budget between firms regulated by the PRA and FCA (see Figure 2).

All costs have been identified as either "specific" or "base" costs. Specific costs are allocated to the relevant industry sectors and base costs spread between all firms.

The costs continue to be allocated as follows:

- Costs that are wholly attributable to a type of business are allocated to that specific sector.
- Overhead costs are split between specific, on the basis of the proportion of frontline staff full time equivalents (FTE), and base costs, on the proportion of support staff FTE.
  - Base costs have reduced as a result of the reclassification of the commercial loan facility costs to the deposits class, as the specific requirement to have a £1.45bn facility limit is driven by our responsibilities to deal with deposit failures, although we would review the actual costs in the event the facility is triggered. Previously, this facility was charged as if generally available and as such, as a base cost.
  - We have reviewed and updated our methodology for allocating specific costs to individual classes to a fairer system, based on claims activity. This has resulted in a more appropriate allocation of specific costs and is the main reason for the individual class changes.
- Total base costs are split 50:50 between the PRA and FCA (who will then apply their overall class allocation matrix to spread between their fee classes).
- **Contingency Reserve for Major Failure**

The proposed Management Expenses Levy Limit (MELL) includes a contingency reserve, within which FSCS can incur management costs beyond the budget without further consultation by the Authorities, in response to unforeseen failures. This reserve is not levied on the industry unless in response to an unforeseen major failure or failures, or urgent need. The reserve for 2018/19 is being consulted on as part of the MELL - it is slightly lower than the level last year at £5m (2017/18 £5.3m) as we have re-validated the assumptions on which the calculation is based.

The reserve level does not reflect the specific or known costs of any particular future failures. It is indicative of the short-term costs of, for example, dealing with large, unexpected failures within tight timeframes.

We do not expect to raise more than our budgeted expenses, unless there is a specific event or events that require us to do so. In line with our usual practice, we will liaise with the relevant parties, such as the PRA, FCA and trade bodies, before raising a levy against this reserve.

Compensation costs and levies

Key components of the 2018/19 levy

Our indicative forecasts for compensation costs and levies in the year ahead reflect a number of assumptions. The most important are the volume and cost of claims we expect to receive during the year.

We discuss how we arrive at these assumptions below. During 2018/19, FSCS will move to align the accounting years used for most levy sectors with the financial year. This results in 2018/19 being a nine-month period for most levy sectors and the impact of this on our forecasts is explained more fully below.

We also have to take into account the expected surplus or deficit for each funding class at the end of the funding period on 30 June 2018, the forecasts for recoveries which offset compensation costs and the management expenses attributable to each class. The surpluses or deficits with which we end one year and begin the next are themselves influenced by decisions taken about supplementary levies in the preceding year.

In 2017/18 we decided, consistent with our policy, to raise a supplementary levy on one industry sector – life and pensions advisers, which fell to be paid by the retail pool. We shall also make a refund to the general insurance provision sector. This refund and the supplementary levy are reflected in our year-end forecasts.

The indicative 2018/19 levy is £336m. This compares to the £316m final levy raised in 2017/18 – although £24m of supplementary levies is also to be raised and a £20m refund made. The amounts are detailed in figure 4. In addition, we forecast that the cost of the interest on the outstanding bank legacy loan will be £98m, although we currently expect to levy £61m of this sum and meet the remainder of the cost from recoveries. As usual, we will review and confirm the final levies for each class in April.

Our calculations

Under our rules we may levy for the higher of the expected costs calculated under a 36-month approach or the traditional 12-month basis. We calculate the expected compensation costs using both methods. Because 2018/19 is a year of transition to align the levy year with the financial year for most classes, we have pro-rated both bases of calculation to estimate costs over a nine-month period where relevant.

In most classes, we have applied the nine-month forecast, except for investment intermediation, where the levels of claims we continue to receive support a higher trend. As shown below, we have therefore applied the 36-month average (pro-rated to a nine-month period) for the investment intermediation class.

Figure 5 sets out the alternative nine-month and 36-month figures. The amounts (in figure 5) are then adjusted for opening balances, management expenses and projected recoveries by funding class. The result of this is the funding requirement for the levy. The highlighted numbers are the indicative compensation amounts to be levied for in 2018/19.

Any surplus/deficit at the year-end will then form the opening balance of the calculation for 2019/20.

Figure 4: 2017/18 final levy compared with 2018/19 indicative levies by funding class

Funding classes	2017/18 Final levy (£m)	2017/18 Supplementary levies/(refunds) (£m)	2017/18 Total levies (£m)	2018/19 Indicative levy (£m)	Variance[1] (£m)
Deposits (SA01)[2]	9	-	9	16	7
General Insurance Provision (SB01)	52	(20)	32	88	56
General Insurance Intermediation (SB02)	18	-	18	23	5
Life and Pensions Provision (SC01)	-	-	-	-	-
Life and Pensions Intermediation (SC02)[3]	100		100	87	(13)
Funded by Retail Pool		24	24		(24)
Investment Provision (SD01)	10	-	10	34	24
Investment Intermediation (SD02)	88	-	88	46	(42)
Home Finance Intermediation (SE02)	14	-	14	17	3
Debt Management (SK01)	-	-	-	-	-
Base costs	**25**	**-**	**25**	**25**	**-**
Total	**316**	**4**	**320**	**336**	**16**

[1] Note that 2018/19 is a nine-month period, whereas 2017/18 covers a full 12-month year.

[2] This does not include the levy for interest costs in respect of the outstanding bank legacy loan, which we forecast to be £98m, offset by recoveries of £37m.

[3] Capped at £100m in 2017/18 and £75m in 2018/19 (reflecting a nine-month levy period), with the balance above these amounts to be paid by the retail pool.

Figure 5: Forecast compensation costs by funding class 2018/19

Funding class	3-yr average (apportioned to 9-mths excluding deposits) (£m)	9-mth forecast (excluding deposits) (£m)	Notes
Deposits (SA01)	n/a	4.20	Rules don't allow for 3-yr average or part-year apportionment
General Insurance Provision (SB01)	93.24	89.67	History of class surpluses on 9-mth forecast basis unless new failure
General Insurance Intermediation (SB02)	10.42	14.35	Rising costs but 9-mth forecast greater than 3-yr average
Life and Pensions Provision (SC01)	-	-	No costs expected
Life and Pensions Intermediation (SC02)	83.80	76.81	Falling trend from peak 2 years ago
Investment Provision (SD01)	5.71	31.50	SIPP operator costs included in 9-mth forecast, no history
Investment Intermediation (SD02)	57.96	39.07	Uncertainty around one default so use 3-yr average
Home Finance Intermediation (SE02)	10.22	11.07	Costs are for Fuel Investments – distinct population of claims
Debt Management	-	-	No costs expected
Total	**261.35**	**266.67**	

Used in Levy

Claims assumptions

So that we can forecast the claims FSCS expects to receive, we make use of data from a variety of sources, such as the FCA, PRA, Financial Ombudsman Service and the industry as a whole. We also examine claims data and analyse trends, where there is sufficient information to quantify the numbers.

The assumptions we make and the trends we follow are reviewed regularly, as they may well change across the year, when for instance a large failure or other unforeseen event occurs. This helps us to determine the resources and expenses required to pay the claims we expect to receive.

We expect a 9 per cent increase in claims overall in 2018/19, excluding General Insurance Provision. Trends' analysis suggests that SIPP and PPI claims, as we explain below, are set to grow further, while investment advice and home finance claims fall. We expect a significant change in the mix of claims. This reflects activity by Claims Management Companies, which are driving an increase in PPI-related claims as the FCA complaint deadline for these claims approaches in 2019.

SIPP and other Life and Pension-related claims are also showing signs of increasing and we expect this to continue next year. Pension claims are the most complex and expensive for us to process.

This volatility in claims levels and mix will be factored into our assumptions as the real numbers become clearer. The forecasts are shown in figure 6 (see table page 21).

Debt management

From 1 April 2018 a ninth funding class will be created covering the business of debt management firms with a levy limit of £20m. At this time we are not envisaging receiving any claims in relation to this new class.

Deposits (SA01)

Based on our recent experience of credit union failures, we allow for a small number of these each year. Our assumptions do not allow for the failure of any other deposit takers, although we have in place the appropriate plans to deal with larger deposit taker failures if necessary.

2018/19

We expect to see a decline in overall claims volumes

Figure 6: Claims assumptions 2017/18 and 2018/19

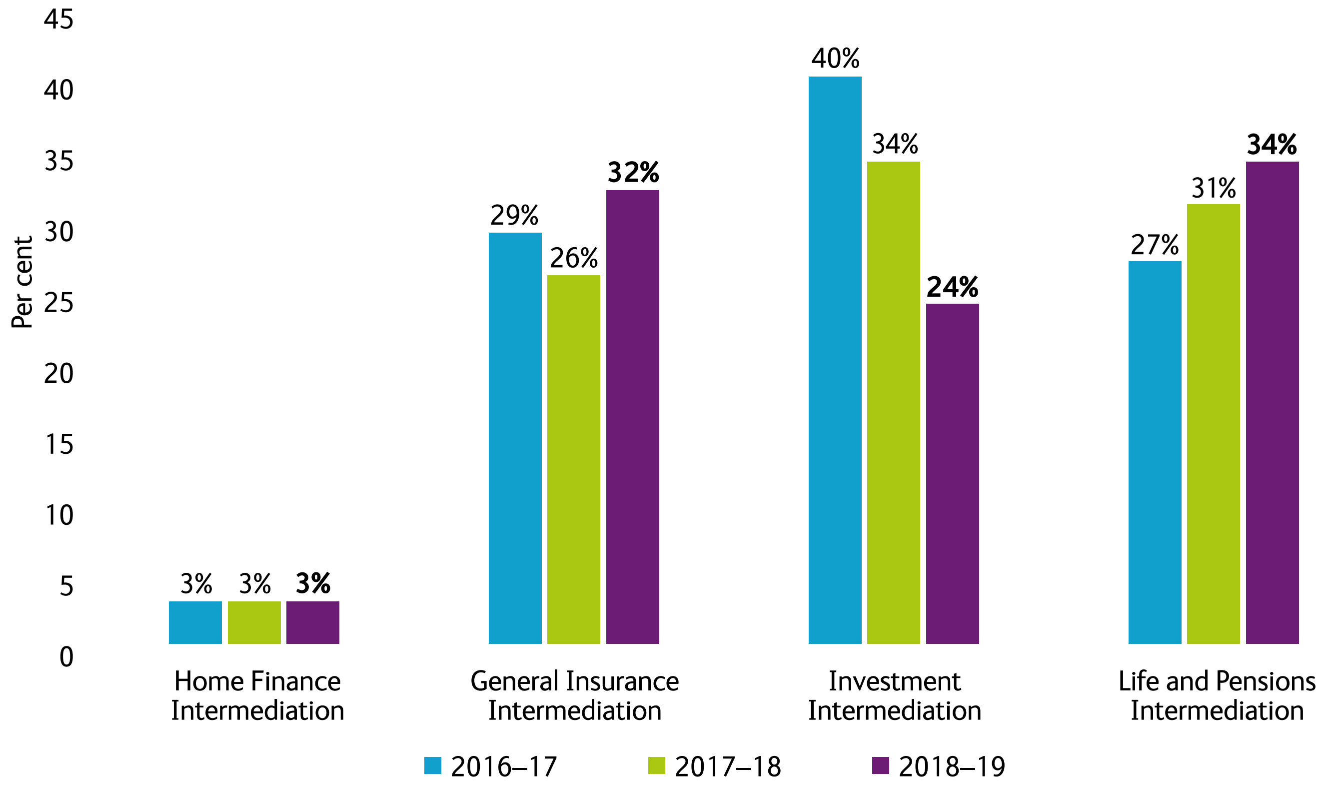
Sub class	Claim type	2017/18 Estimate of completed claims	2018/19 Estimate of completed claims
SA01	Deposits[1]	6,000	6,000
SE02	Home Finance Intermediation	1,044	624
SB02	Insurance Intermediation	4,320	6,720
SD01	Investment Provision	54	1,500
SD02	Investment Intermediation	6,480	5,160
SC02	Life and Pensions Intermediation	6,720	7,162
Total claims excluding insurance payments		**24,618**	**27,166**
SB01	General Insurance Provision[2]	300,000	300,000

Notes:

[1] 2017/18 from original budget

[2] 2018/19 from levy forecast

Figure 7: Decision mix



General Insurance Provision (SB01)

The claims assumptions reflect continuing claims against Gable and Enterprise from last year. We do not expect these failures to produce much new claim activity next year.

However we do expect to make a very significant number of payments for return of premium on Enterprise in both this year and the start of 2018/19. The payments we make next year will be to policyholders who have not yet had their Enterprise insurance policy cancelled. We expect the value of payments on Enterprise will be similar to last year.

The new claims we expect are in fact largely against the older estates. However, we have seen a decrease in claims against Chester Street, Builders Accident Insurance and Independent Insurance Company Limited, where our experience is similar to that of the live insurance market. The number of claims for employer's liability noise-induced hearing loss is declining and we expect compensation for employers' liability mesothelioma claims will continue at a rate similar to recent years and will remain the most expensive category of claims for which we pay compensation.

We will also continue to make payments on the recent failures of Lemma Insurance Europe Ltd (2012/13), Balva AAS, European Risks Insurance Company (2014/15) and Berliner (2015/16), although no new claims are forecast for next year.

General Insurance Intermediation (SC02)

We expect the volumes of PPI claims already experienced during 2017/18 to continue during 2018/19, driven by a combination of both the recent FCA announcement of a cut-off of August 2019 for PPI claims, as well as marketing efforts by Claims Management Companies.

PPI claims are becoming more complex, for example, claims from customers undergoing Individual Voluntary Arrangements or Bankruptcy lengthening the processing times.

FSCS is actively reviewing whether "Plevin" based claims[1] fall within the scope of its protection. If it transpires these claims are protected by FSCS, we would need to assess each claim individually in the usual way, on its own merits and on the basis of all the available information. We will update our forecasts to take account of these claims when setting the levy in

1 Following the court case of *Plevin v Paragon Personal Finance ("Plevin")* the Supreme Court said that, in some circumstances, an undisclosed commission on PPI could result in an unfair relationship between the lender and consumer under the *Consumer Credit Act 1974*. FSCS is reviewing whether or not these claims are covered by our protection.

Figure 8: General Insurance Intermediation (SB02) Decisions and uphold rate

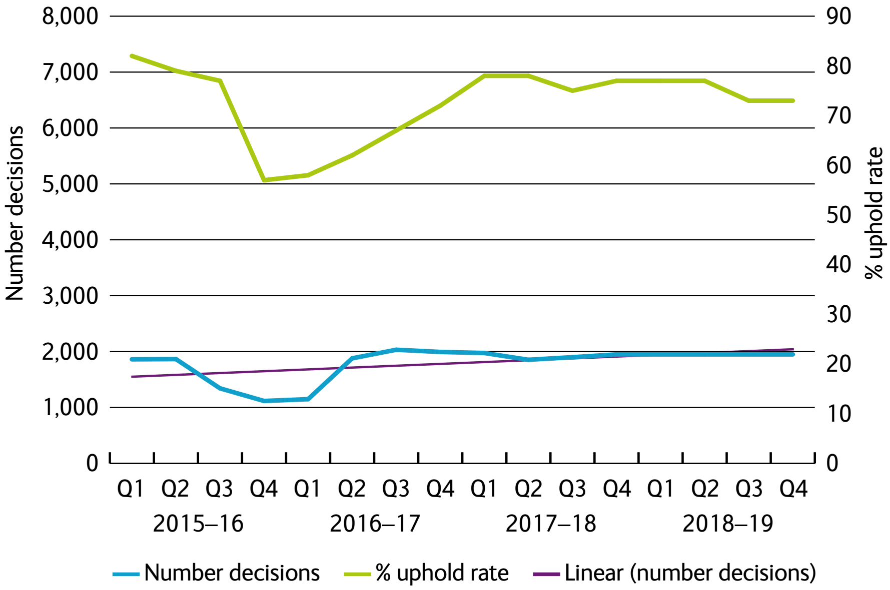


Figure 9: Life and Pensions Intermediation (SC02) Decisions and uphold rate

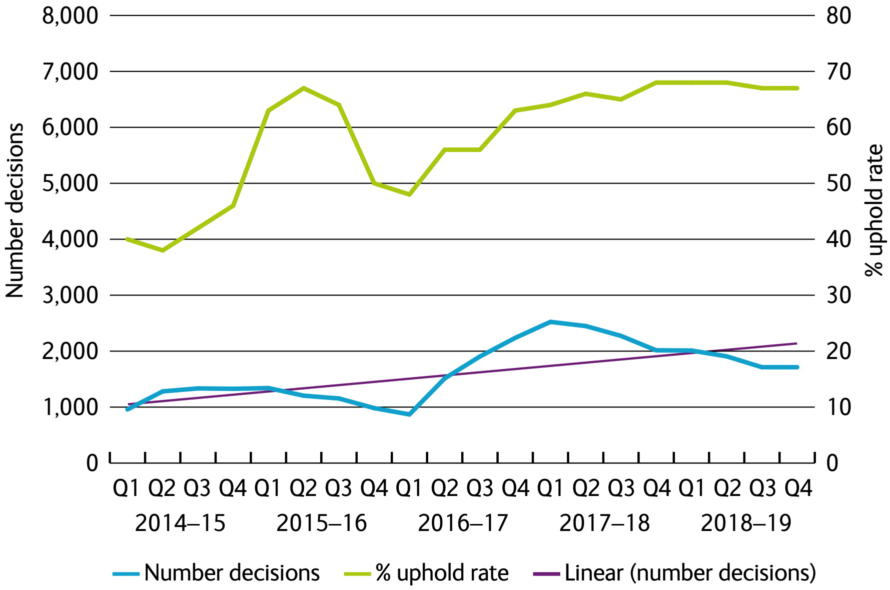


Figure 10: Investment Intermediation (SD02) Decisions and uphold rate

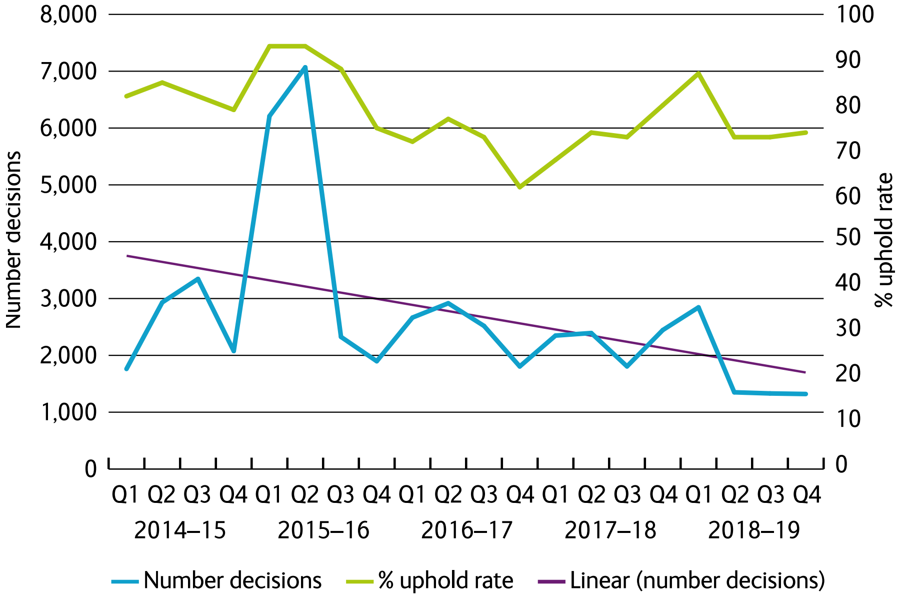
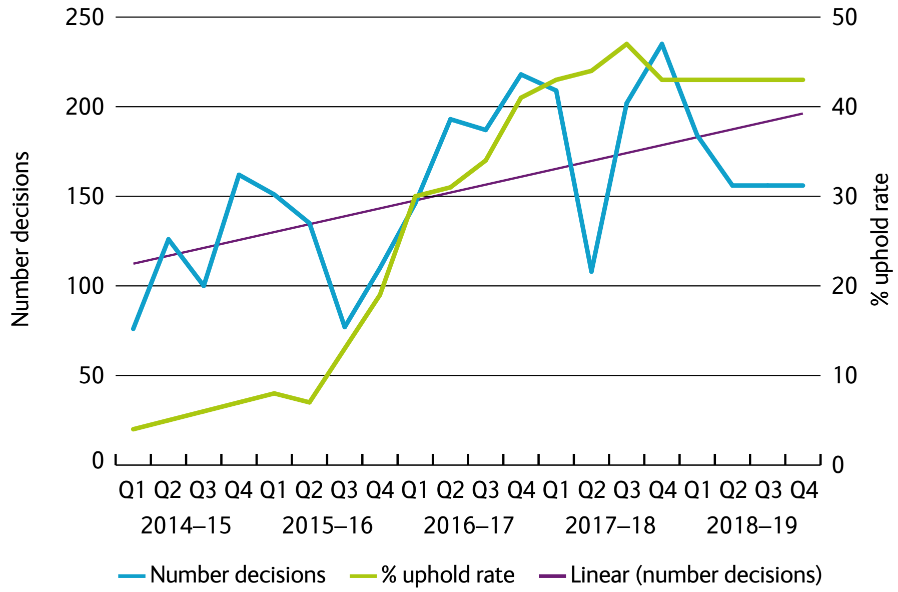


Figure 11: Home Finance Intermediation (SE02) Decisions and uphold rate



April. To the extent claims are against Welcome Financial Services, in part at least costs may be met from the funds already available to FSCS.

Life and Pensions Intermediation (SC02)

FSCS continues to receive significant numbers of claims against independent financial advisers regarding advice given to customers to transfer existing pension arrangements into SIPPs.

The vast majority of these claims relate to advice to invest pension monies into high risk, non-standard asset classes within a SIPP wrapper. Owing to the risky nature of these investments, many of the funds became illiquid and often insolvent. These investments are unsuitable for the majority of investors.

FSCS expects to continue to see increased numbers of this type of claim, along with other types of life and pension related claims in 2018/19. This will lead to an increase in compensation costs because of the typically high value of these claims. That said, uncertainty remains as to the number and value of claims that FSCS will receive in the coming period.

SIPP-related
claims continue to rise

The forecast funding requirement for the Life and Pensions Intermediation class is £87m to the end of March 2019. This figure exceeds the proposed class limit of £75m by £12m. This means that the maximum would be levied for the fourth consecutive year and the retail pool would be triggered for the third year in a row.

Investment Provision (SD01)

FSCS has received a number of claims against three SIPP operators (Stadia Trustees Limited, Brooklands Trustees Limited and Montpelier Pension Administration Limited) in relation to due diligence failings. The FCA has previously highlighted concerns in the SIPP market where operators accepted business from non-authorised introducers, or other due diligence failings.

FSCS is satisfied that certain claims are eligible and we have now declared these firms in default, and we forecast the funding requirement for the Investment Provision class will be £34m for 2018/19. So far, FSCS has received around 150 claims against the three failed SIPP operators but we expect to receive many more claims in 2018/19. FSCS will monitor claim volumes and update our forecast ahead of the final levy announcement in April.

Investment Intermediation (SD02)

In recent years the volumes of these claims has been particularly difficult to forecast, mainly because of the number of product categories and firms in this class, but FSCS continues to see sizeable volumes of investment claims against independent financial advisers in relation to negligent advice to invest in unsuitable funds and other types of investment, but the trends we are seeing show these types of claims start to reduce in 2018/19.

Historically FSCS has also had to respond to unexpected failures where firms have been placed into the Special Administration Regime (e.g. Alpari). Whilst we have no reason to believe that a large investment default is likely, there is an uncertainty around the costs to FSCS from Strand Capital. Strand entered the Special Administration Regime in May 2017 and we expect compensation costs of £6m for client assets and potentially additional compensation for mis-selling or negligence claims.

Accordingly, FSCS has elected to raise levies on a 36-month rolling average in recent years as we consider this the best way of making reasonable allowance for unforeseen failures.

Home Finance Intermediation (SE02)

In recent years FSCS has seen an increase in claim volumes and compensation costs for Home Finance claims. One firm in particular, Fuel Investments Limited, accounts for a large proportion of our forecast costs. Claims against Fuel typically relate to advice to re-mortgage residential properties in order to raise funds to invest in high risk property schemes. Customers are paid compensation for losses directly caused by the regulated mortgage advice, which can include significant losses arising from the property investments. These meant a marked increase in our uphold rate and compensation paid over the past few years, which are also reflected in our levy forecast.

Appendix: Vision for a Confident Future

FSCS

Target	Achievement
Handle 60% of claims online	Handling 97% of claims online
Claimants have greater choice	Payments made by bank transfer not cheque in 75% of non-deposit cases
Pay deposit claims in 7 days of failure	96% of claims within this target
Handle non-deposit claims in 3 months	Between January 2017 and December 2017 we handled 70.76% of non-deposit claims within 90 days. The turnaround time continues to fall
Continuity of cover	We have supported flexible payments for broker defaults in special administration proceedings and the continuity of cover for Enterprise motor policyholders
70% of UK adults aware of FSCS or a protection scheme	77% of UK adults are aware
Claimant satisfaction at 70%	Satisfaction is at 83%
80% of firms' customer contact mentions FSCS	89% of deposit takers display FSCS information inside the branch and 90% outside, but much lower in other sectors

Industry

Target	Achievement
Easy access to performance indicators for levy payers	Regular updates and a separate class statements report published for 2016/17
More advance notification of failures and certainty of levies for firms	Traffic light reporting adopted in Outlook
Maximising recoveries	Significant recoveries achieved both in insolvencies but also through third party action e.g. Keydata and PPI litigation
Protection for insurance is part of awareness	A working group has been set up with industry for this purpose
Work with regulator on changes to funding model	FCA's Consultation Paper is out for consultation
Resolve legacy deposit cases	Bank legacy loans repaid except for B&B, which is due to be repaid in 2018

Authorities

Target	Achievement
Contingency planning and responses with authorities	Walkthroughs and planning with the authorities and pay-out simulations carried out
Test contingencies across sectors	FSCS has contingency plans for all sectors, even those regularly triggered in reality
Leading source of expertise	Regular and prominent contributions to international bodies and the evolution of standards for guarantee schemes

Our people

Target	Achievement
Investor in people and Best Companies accreditation	We achieved Investor in People accreditation in January 2015; we will be undertaking a further assessment against the revised standard in 2018. We have consistently been recognised as One to Watch by Best Companies
20% rise in employee engagement	We have achieved a 5% increase
Career development plans	We started the roll out of a new approach to Performance Achievement this year, providing personal development plans for all employees
Internal and external role rotation	15 employees have moved role internally and there are a number of external secondees to the FCA
Four days of learning a year	We've delivered more than 1,500 learning events
Family friendly environment and policies	We have relaunched our Family Leave Policy; increased access to a wider range of benefits and are rolling out new flexible working arrangements during 2018

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