

To:	Legal Services Board	
Date of Meeting:	23 March 2016	Item: Paper (16) 12

Title:	OLC budget approval	
Workstream(s):	Performance, evaluation and oversight	
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Status:	Official	

Summary:

Steve Green (OLC Chair) and Kathryn Stone (Chief Ombudsman) will attend to present this item.

Schedule 15 of the Legal Services Act 2007 requires the OLC, before the start of each financial year, to adopt an annual budget which has been approved by the LSB. The Act requires that the OLC's annual budget must include an indication of the distribution of resources deployed in the operation of the ombudsman scheme and the amounts of income of the OLC arising or expected to arise from the operation of the scheme.

In November 2015, the LSB established a Board sub-group to consider a number of OLC-related matters including the process for budget approval. The sub-group considered how best the Board could fulfil its budget approval function and agreed a set of criteria for OLC to meet in making its budget submission (in addition to the statutory criteria described above). These were sent to the OLC Chair in February 2016 (see **Annex A**).

The OLC has made a budget submission for 2016/17 to the LSB addressing both the statutory and LSB criteria (see **Annex B**). It has also provided its draft Strategy (currently out for consultation) as additional context (see **Annex C**).

The OLC are seeking a total budget of **£13.63m for 2016/17**, a reduction of £1.21m on its budget for 2015/16 (**a reduction of 8.1%**). This represents a budget of £11.55m for the legal jurisdiction and £2.08m for the claims management jurisdiction.

The budget has been approved by the OLC Board.

The Board should be aware that, in parallel with the approval being sought from LSB, OLC must also gain budget clearance from the Lord Chancellor, both for the amount to be raised by way of the levy and as regards the grant-in-aid provided by MoJ for OLC's claims management company (CMC) jurisdiction. OLC report informal indications that their budget proposals have been favourably received but

that, at the time of drafting, there has been no formal indication of budget approval from MoJ.

Recommendation(s):

The Board is invited to:

- (1) review the OLC's submission on its budget for 2016/17;
- (2) discuss the budget with OLC;
- (3) approve the budget.

Risks and mitigations

Financial: OLC is required to comply with Managing Public Money requirements. Its Accounting Officer status remains retained by an official at the MoJ. MoJ are responsible for financial oversight in year. MoJ also provide Grant In Aid to OLC in respect of the claims management complaints jurisdiction

Legal: N/A

Reputational: Whilst qualification of OLC's 2013/14 and 2014/15 Accounts had the potential to present a degree of reputational risk to LSB this did not manifest. We have been clear throughout the process that the LSB has no remit or authority to intercede in matters relating to ongoing financial management where meaningful oversight must be provided by the sponsoring Department

Resource: N/A

Consultation	Yes	No	Who / why?
Board Members:	✓		Terry Babbs and Marina Gibbs were provided with a draft of this paper.
Consumer Panel:		x	
Others:	John Ward, external advisor to the LSB's ARAC has reviewed this paper. MoJ's formal position has been sought but was not known at time of drafting.		

Freedom of Information Act 2000 (Fol)

Para ref	Fol exemption and summary	Expires
tbc		

LEGAL SERVICES BOARD

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OLC Budget

Executive Summary

Introduction

1. Part 6 and Schedule 15 of the Legal Services Act 2007 (**the Act**) describe the arrangements for the handling of complaints about legal services professionals and provide the framework for the relationships between LSB and OLC. Within the framework is the requirement that the LSB must approve the OLC's budget.
2. Whilst the LSB has a statutory responsibility to approve the OLC's budget, it has made clear in all years to date that it does not want to duplicate the work properly done by the OLC Board in scrutinising the basis on which the budget has been developed. As such, an approval process was designed to provide adequate assurance to the Board about the robustness of the OLC process rather than seeing the LSB conduct a de novo analysis. To assist with this, the Board provided OLC with a suite of criteria to address in its budget. For this year's budget approval, the LSB acceptance criteria were formulated by a Board sub-group and communicated to the OLC on 3 February 2016 (see **Annex A**).
3. As in 2015/16, the OLC's submission also includes budget to fund its claims management complaints (CMC) jurisdiction, as well as for its traditional legal services complaints jurisdiction. The CMC budget is funded by public funds known as Grant In Aid (GIA) from the Ministry of Justice (MoJ) and not by the levy on approved regulators. MoJ must therefore agree to provide the necessary GIA. Whilst MoJ have laid regulations based on OLC's estimated CMC budget need, they have stressed that the actual amount of GIA they will pay will need to be reviewed as the year progresses and in light of actual complaint numbers. Additionally, the Lord Chancellor must approve the amount to be raised by way of the levy on approved regulators to fund the OLC's legal complaints jurisdiction. Whilst the Act therefore requires the LSB to approve the entirety of the OLC's budget, the decision must be mindful of these two additional decision points (required by the levy rules and Managing Public Money).
4. OLC has adopted a methodology for apportioning costs that are shared by both the legal and CMC jurisdictions so that they can be recovered from the relevant funding source – levy or GIA, which has been agreed with both LSB and MoJ. The apportionment basis relates to the number of operational employees dedicated to the legal or CMC jurisdiction. This mechanism will be kept under

review by all parties and may be modified by agreement.

5. The OLC are proposing a budget of **£13.63m** for 2016/17 (for both jurisdictions combined) - **£11.55m for legal** activities and **£2.08m for CMC** activities). A reduction of 8.1%. This maintains their downward budget trajectory since establishment when, in 2011/12, their first full year of operation, OLC budget was £19.72m (legal only). (For reference, LSB is proposing a reduction of 5.8% on its own budget for 2016/17).

Statutory requirements

6. Para 23 of Schedule 15 to the Act concerns the OLC's budget and states:
 - a. The OLC must, before the start of each financial year, adopt an annual budget which has been approved by the Board (LSB).
 - b. The OLC may, with the approval of the Board, vary the budget for a financial year at any time after its adoption.
 - c. The annual budget must include an indication of:
 - i. The distribution of resources deployed in the operation of the ombudsman scheme, and
 - ii. The amounts of income of the OLC arising or expected to arise from the operation of the scheme.
7. As an independent NDPB, the OLC has its own Accounting Officer and Audit and Risk Assurance Committee. It also has its own independent sponsor-body/sponsor relationship with the MoJ in accordance with Managing Public Money. Hence, while the LSB approves the *level* of the budget, we do not have any responsibility in relation to in-year financial control issues (unless these cause the budget to be varied) nor in relation to the propriety of spend. The Board will be aware that a senior official at the MoJ remains the OLC's Accounting Officer at this time.

Acceptance Criteria

8. The LSB required the OLC to address the following criteria in their budget submission:
 - a. in accordance with the Act, an indication of **the distribution of resources** deployed in the operation of the ombudsman scheme and **the amounts of income** OLC expect to arise from the operation of the scheme. This should include a clear breakdown of:
 - i. staff costs and numbers broken down by function – for instance: enquiries; investigations; ombudsman team; corporate, others
 - ii. any possible variation around the income prediction eg in response to volume changes, or should changes to the case fee structure be introduced in-year

- b. a summary of the **key risks** to delivering the Plan for 2016/17 and **mitigation** proposed
- c. the **volumes predicted** for the year, along with a **sensitivity analysis** illustrating the organisation's response should volumes fluctuate. In particular,
 - i. what is the resourcing strategy for responding to in-year fluctuations (up or down) particularly in the climate of recruitment and spend controls
 - ii. if activity to address the question of numbers of contacts that turn into cases results in a change to volumes, what would be the resourcing strategy response
- d. a summary of where the budget has changed in response to **stakeholder responses** to consultation. I should emphasise that the Board will expect to see the **outcome of discussions with MoJ** and the extent to which the final budget takes account of their input covered explicitly before it reaches a decision.
- e. the OLC Board's most up to date thinking on the extent to which the budget is designed to deliver transformational change eg around the operating model to allow for a more flexible response to demand change. In particular, what elements within the budget are intended to deliver system improvements ie 'one off' costs and what could more reasonably be considered 'steady state'

Budget submission

9. **Annex B** contains the formal budget submission from OLC to LSB. This comprises a letter from the OLC Chair and a document providing full detail on the OLC's budget and how it meets the LSB's acceptance criteria. The budget document's Executive Summary notes the OLC's intention to see 2016/17 as a year of stability and consolidation building on the new permanent appointments at Chief Executive and Chief Ombudsman and the new Board's experience of a year working together. In light of the turbulence that the organisation has faced over the past one to two years, this seems a reasonable aspiration, providing that it also delivers the improvements in performance that are needed. To that end, the OLC's draft strategy for 2016-17 (attached at **Annex C**) proposes an in-year focus on:
- a. Continuing to improve operational efficiency using lean principles to make the most efficient use of resource and improving quality
 - b. Continuing to drive learning and improved complaint handling across the sectors and informing consumers of these services
 - c. Continuing to work openly and constructively with a wide range of stakeholders and engaging fully on debates around regulation, redress and consumer protection.

Review of budget submission against LSB acceptance criteria

An indication of the distribution of resources deployed in the operation of the ombudsman scheme and the amounts of income OLC expect to arise from the operation of the scheme. This should include a clear breakdown of:

- ***staff costs and numbers broken down by function – for instance: enquiries; investigations; ombudsman team; corporate, others***
- ***any possible variation around the income prediction eg in response to volume changes, or should changes to the case fee structure be introduced in-year***

10. Sections 4, 5 and 6 of the OLC's budget submission document at Annex B illustrates the distribution of resources across the legal and claims management jurisdiction and breaks down the indirect cost budget. The submission provides the breakdown of staff costs and numbers by function.

11. Changes in categorisation of costs mean that it is not possible to compare directly the 2016/17 budget with that submitted to LSB in 2015/16. The bulk of savings are, however, being made from non-staffing costs. Staffing costs are actually increasing from £7.17m 2015/16 to £7.36m 2016/17. Unlike past years, a budget line for contingency has been removed (£240k in 2015/16).

12. Whilst the submission does address volume fluctuations, there is little analysis of the impact of case fee income or modelling for possible variation around the income prediction. This may be because only 8% of the legal jurisdiction budget derives from case fee income. OLC also report that they intend to revisit their case fee structure in 2016/17.

Summary of the key risks to delivering the Plan for 2016/17 and mitigation proposed

13. The OLC have identified four key risks to delivering the plan in 2016/17 in section eight (page 20 - 21). A brief summary of the risks and their mitigations are provided below:

- ***Variations from planned contact and case volume.*** Identical to 2015/16, the mitigation for this risk would depend on whether the variation led to a rise or fall in volumes. Action would be taken through their recruitment strategy and flexible working policies.
- ***Planned investigator efficiency is not met.*** Identical to 2015/16, this risk has been mitigated by making a prudent assumption on investigator efficiency based on actual achievement which is regularly monitored (this is reported in monthly KPI reports). In the event that levels of efficiency fell significantly, investigator resource would be adjusted.

- **Staff turnover varies significantly from the plan.** Identical to 2015/16, depending on whether the rate of attrition rises or falls the management team will review staffing requirements to consider whether a redundancy programme is necessary or, conversely, will review activity and efficiency levels to determine whether a programme of recruitment should be initiated. In addition, the management team have mitigated this risk further by planning to recruit and train smaller blocks of operational staff to enable them to more closely meet the demands of variations in activity. There is no reference at all to the impact of recruitment controls on the mitigation for this risk. And it has not been updated to reflect the latest position as regards the flexible benefits scheme.
- **Large legal costs associated with judicial reviews.** Identical to 2015/16, due to the nature of any challenge (which may or may not result in significant financial impact), the OLC and management team manage this risk through regular discussion with General Counsel.

The volumes predicted for the year, along with a sensitivity analysis illustrating the organisation's response should volumes fluctuate. In particular,

- ***what is the resourcing strategy for responding to in-year fluctuations (up or down) particularly in the climate of recruitment and spend controls***
- ***if activity to address the question of numbers of contacts that turn into cases results in a change to volumes, what would be the resourcing strategy response.***

14. Assumptions on case volumes are within section four (page 8) for legal and section 5 (page 12) for CMCs. Section seven (page 19) outlines the sensitivity analysis.

15. The OLC budget is based on an expectation of:

- investigating 7000 legal cases in 2016/17 and resolving 6,700.
- receiving 17,500 CMC contacts and accepting 2,000 cases.

16. Numbers of legal cases have fallen in almost every year since establishment with figures for 2015/16 predicted to be the lowest yet. The proposals for 2016/17 are higher than the predicted out-turn for 2015/16 but remain lower than the numbers predicted for 2015/16. It is difficult to deduce from the analysis why OLC believe that there will be a reversal in complaint trends, beyond some indications that contact levels in Qs1 – 3 of 2015/16 were unusually low. Bearing in mind the importance of this indicator to the budget assumptions there is little analysis in support. For CMC cases, this will only be the second year of operation and the analysis suggesting a downward trend seems reasonable.

17. Section 7 (page 19) contains the sensitivity analysis and Appendix 1 (page 25) the resourcing strategy for dealing with variations. The analysis and response appears to be identical (bar adjusting for changes in budget) to that received in 2015/16. There is a passing reference to MoJ permissions but no indication that the organisation has changed its resourcing strategy in light of experience or to reflect potential changes in working practices since March 2015. We might have expected to see this given the OLC's recent experience with permissions for recruitments and the changes to eg Ombudsman working practices of which we are aware. There also appears to be no reflection of the experience of this strategy in practice eg where we know from S120 reporting that long-running shortages of investigators have had a negative impact on timeliness performance.

A summary of where the budget has changed in response to stakeholder responses to consultation. I should emphasise that the Board will expect to see the outcome of discussions with MoJ and the extent to which the final budget takes account of their input covered explicitly before it reaches a decision

18. The submission does not make any reference to responses received to the consultation beyond a statement in the cover letter that the budget has not changed as a result of stakeholder responses to consultation.

19. The cover letter makes reference to the submissions OLC has made to MoJ regarding current and future budgets but, as yet, no formal position has been indicated. The cover letter explains that these discussions have, however, informed the budget.

The OLC Board's most up to date thinking on the extent to which the budget is designed to deliver transformational change and in particular whether any elements of the budget are 'one-off' costs to deliver systems improvements versus costs that are more reasonably steady state.

20. The cover letter states simply "*Having, hopefully, now completed the resolution of the issues which arose from the previously qualified accounts, the OLC's aspirations for 2016/7 are focussed upon sustainable consolidation rather than any further attempts at 'transformational change'. This approach does not require significant 'one off' budgetary provision. The Board is aware that there are efficiencies to be gained from developing a more flexible staffing model, exploiting the new IT system and adopting best practice, as developed in either of the jurisdictions. These initiatives will all be included in the Legal Ombudsman business plan and will assist in meeting the MoJ's spending expectations.*"

Observations from the external advisor to ARAC

21. The external advisor observed that the budget submission was a sensible document and showed a welcome direction of travel that the direction. He

commented that expectations in terms of activity appeared reasonable. He made the following observations:

- a. That it was unusual for a consultation on the strategy for the year in question to follow the budget consultation as the former would usually inform the latter
- b. That the lack of analysis provided for income fluctuations was unfortunate but not unduly problematic bearing in mind the limited impact any such fluctuation was likely to have
- c. That the significant risk facing OLC appeared to be the ability to flex resourcing levels quickly enough to respond to increases in demand or high levels of turnover and queried whether the response outlined in Appendix 1 was adequate in light of the experience of operating under current MoJ controls.

Recommendation

22. The Board is invited to:

- (1) Review the OLC's submission on its budget for 2016/17;
- (2) Discuss the budget with OLC;
- (3) Agree the budget.