

22 July 2014

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## CMC Cost Apportionment Rules – Draft for discussion

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### Principle

Costs for CMC activities “CMC work” must be paid for by the Ministry of Justice (“MoJ”). Costs for the core Legal jurisdiction activity “Legal work” must be paid for by Approved regulators.

A simple case volume apportionment model, such as that used for apportioning costs between approved regulators is not appropriate because if CMC cases are significantly faster or slower to resolve this basis of allocation would lead to a disproportionate allocation of indirect cost to either the Ministry of Justice or to Approved regulators. A case volume based apportionment model similar to that used to apportion costs between Approved Regulators will also fail to account appropriately for the start up phase. At this stage there is insufficient experience of the level of complexity of CMC cases compared to existing Legal work to determine this with sufficient certainty. The following cost apportionment model is therefore proposed for the implementation phase and from go live to the end of financial year 2015/16. This cost apportionment mechanism should be reviewed during early 2016/17 or sooner if this basis results in a clear misalignment of costs either for the MoJ or Approved regulators.

### Implementation phase

During the implementation phase LeO staff spending a significant proportion of their time on the Implementation project will record this using a simple timesheet recording system. The cost of this time will be accounted for as direct CMC headcount costs (as outlined below). Once an individual has essentially transferred full time to the project they will be treated as dedicated CMC resource and the requirement for timesheets will cease. The aggregated FTE headcount of individual's

timesheets will be added to any full time CMC resource FTE headcount and used to apportion a share of Indirect Costs to CMC Implementation costs as outlined below.

Where costs are incurred specifically for the CMC project these costs will be treated as “CMC Other Direct costs” and charged to CMC implementation cost centre. Likewise, where costs are incurred exclusively for LeO work (e.g. defending a judicial review on a LeO case) then these costs will also be treated as “LeO Other Direct Costs” and hence excluded from the general Indirect costs to be apportioned between the two functions.

## Review and amendment

The basis of apportionment of costs needs to be reviewed to ensure that it results in a fair and proportionate allocation of costs between CMC and Legal jurisdictions. The LSB, MoJ and LeO should therefore meet in September 2015 to review and if necessary decide whether it is necessary modify the basis of apportionment either in respect of 2015/16, or for 2016/17, as is appropriate, and to agree the timetable for any further review thereafter.

## Cost apportionment model

### **Assessment Centre employee costs**

Our understanding of the Assessment stage of the complaint handling process leads us to believe that there should be little if any difference in time required dealing with Legal or CMC cases in this stage of our business process. The proposed operational approach is therefore that the Assessment Centre should deal with all inbound calls. A call routing mechanism will be established to measure and monitor inbound call volumes and Assessors may still be separated into CMC and Legal teams for the purposes of operational management, however all would be able to deal with both CMC and Legal complaints.

As we anticipate no difference in time required to deal with a CMC call compared to existing calls it is appropriate that the costs and FTE Headcount of the whole Assessment centre (including any CMC team) be apportioned based on the number of Legal and CMC case-files created in each financial year: i.e. the number of case files created during the period where the firm (and hence regulator) being complained about

has been identified. The apportioned headcount will be treated as “Direct Headcount” for the purposes of the apportionment of indirect costs.

Operationally a “CMC Assessment Centre” lacks critical mass; Holidays and other absence is likely to result in volatile call response service levels. While dedicated CMC investigators could cover this function this is less efficient and disruptive to CMC investigator performance. Telephony system call routing can assist with directing calls to specific individuals but it is likely that a fair number of callers will end up talking to the “wrong” team, resulting in unintentional cross subsidy between Legal and CMC functions and transfers of call between internal teams once it has been identified that the caller has routed themselves to the “wrong” team. Such internal call transfers would be both inefficient and poor service as consumers are asked to repeat elements of their complaints to a new assessor.

### **Resolution Centre, Ombudsman and other direct headcount costs**

There is significant uncertainty about whether CMC cases will be as, or less complex, than legal cases it is not appropriate to use the number of cases resolved cases as a basis for apportionment of costs. During the start up phase this is doubly true as it takes a significant period of time to start to resolve cases.

Investigators, Team leaders and Ombudsmen shall be 100% dedicated to either “CMC work” or 100% to “Legal” work. Any other employees who are wholly employed on CMC work either permanently or for an extended period should also be treated as a direct headcount cost and their costs accounted for as such.

### **Indirect Employee FTE cost apportionment**

Where LeO employees (FTE) are not 100% dedicated to either CMC or Legal work, the costs of these FTE (“Support employees FTE”) shall be apportioned to the MoJ and Approved regulators in proportion to the Direct Headcount dedicated to CMC and Legal work respectively. These FTEs are primarily expected to consist of those who provide LeO’s non operational functions (Managerial and Corporate support services such as Facilities, Finance, Human Resources, IT and Communications etc).

### **Direct “Other costs”**

Those non employee costs that can be identified as relating directly to CMC work, these costs shall be coded to an appropriate CMC cost centre to be recovered from the MoJ. Direct “Other costs” are expected to mainly comprise printing and inbound scanning. Direct “Other costs” will also include, for example, training and development costs when these are directly linked to training or development of Claims Management direct headcount (FTE). These will also include external

legal costs involved in defending judicial review challenges to decisions on CMC cases. Costs that cannot be identified as exclusively relating to CMC work shall be treated as Indirect other costs.

### **Indirect “Other costs” apportionment**

Those costs which are not incurred wholly/exclusively for Legal work or wholly/exclusively for CMC work, but which are required to support both CMC and Legal work and for the effective operation, development and improvement of LeO’s service, shall be apportioned to the MoJ and Approved regulators in proportion to the numbers of Operational employees dedicated to CMC and Legal work respectively.

### **Depreciation**

Depreciation shall be treated as an “Indirect Other Cost”. For the avoidance of doubt, fixed assets shall not be assigned to Legal or CMC work, but are available to support both activities. Hence depreciation costs shall be treated as Indirect Other costs and apportioned in the same manner. Only in the event that there is material expenditure on an asset that is exclusively for the benefit of either CMC work or Legal work will the depreciation on such expenditure be treated as a Direct Other cost.

- Example of an Asset where depreciation which might be treated as a “Direct Other cost”: LeO incurs significant cost to develop a case management system module that is not related to and does not benefit CMC work. Depreciation on such an asset would be treated as a “Direct Other cost” and hence not be charged to CMC cost centres or included in the apportionment of indirect costs.
- Example of fixed assets where depreciation which would be treated as an “Indirect Other cost”: LeO acquires laptop and desktop hardware and associated software which is initially assigned to CMC operational staff.

## **Glossary of terms:**

- Approved regulators; has the meaning described in the Legal Services Act 2007, but excluding the Claims Management Services Regulator.
- MoJ: Ministry of Justice
- CMC: Claims management Companies
- CMC work: Handling and resolution of complaints about CMCs in accordance with s.161 of the Legal Services Act and the Legal Ombudsman’s scheme rules.

- Legal work: Handling and resolution of complaints about authorised persons in accordance with the Legal Services Act and the legal Ombudsman's scheme rules (excluding for the sake of clarity CMC work).
- LeO: The Legal Ombudsman

**Example** – (Numbers shaded green are required to complete the calculation – these are purely to illustrate the calculation required and do not represent any headcount or cost assumptions)

			CMC	Legal	
CMC Cases Created	A	5,000			
Legal Cases Created	B	20,000			
			$C = A/(A+B)$	$D = B/(A+B)$	
AC headcount apportionment (based on cases created)			20.0%	80.0%	
AC FTE headcount	E	30			
CMC FTE AC Headcount			6.0		$F = E \times C$
Legal FTE AC Headcount				24.0	$G = E \times D$
Direct Investigator FTE Headcount	H		30.0	110.0	H
Other Direct FTE Headcount	I		1.0	4.0	I
Ombudsman FTE Headcount	J		2.0	12.0	J
CMC Operational FTE Headcount			39.0		K = Sum of CMC column F to J
Legal Operational FTE Headcount				150.0	L = Sum of Legal column F to J
Indirect Costs apportionment			$M = K/(K+L)$ 20.6%	$N = L/(K+L)$ 79.4%	
		Total Cost	CMC Costs	Legal Costs	
Indirect Costs	O	7,000,000	1,444,444	5,555,556	O x M and N respectively
Assessment Centre - Direct Cost	P	1,050,000	210,000.0	840,00	P x C and D respectively
CMC Investigator Direct Cost	Q	1,500,000	1,500,000		
Legal Investigator Direct Cost	R	5,000,000		5,000,000	
CMC Ombudsman Direct Cost	S	250,000	250,000		
Legal Ombudsman Direct Cost	T	900,000		900,000	
Other CMC Direct Cost	U	50,000	50,000		
Other Legal Direct Cost	V	30,000		30,000	
		15,780,000	3,454,444	2,325,556	