Paper (12) 13 ANNEX A

To:	Legal Services Board		
Date of Meeting:	29 February 2012	**Item:**	Paper (12) 13

Title:	Office for Legal Complaints (**OLC**) Budget 2012/13
Presented by:	Julie Myers, Corporate Director julie.myers@legalservicesboard.org.uk / 020 7271 0059
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Status:	Restricted

Summary:

The Legal Services Act 2007 requires the LSB to consider and approve the annual budget of the OLC. On 25 January 2012, the Board delegated approval authority to a sub-group of its members.

This paper presents the OLC's budget submission for financial year 2012/13 (see **Appendix 1**). Please note that we have NOT received the OLC's final Business Plan ONLY the budget submission.

The proposal is for a total budget of **£16,997,000**. The OLC agreed to submit this budget to the LSB when it met on 20 February 2012. The figure is a reduction of some £2.7m on the consulted on figure of £19.5m but is more closely in line with the predicted out-turn for 2011/12 of £17.3m. This in part reflects revised case number modeling with volumes predicted to be circa 8,500 rather than 10,000 (as estimated in the OLC's consultation document).

In line with the agreed mode of working between LSB and OLC, rather than conduct a de novo analysis, the Board should approve the budget if it has adequate assurance that the OLC Board considered all appropriate aspects in recommending the proposed budget. To assist with this, we provided OLC with a suite of criteria to address in its budget submission to support the LSB approval process. The OLC submission appears to meet these criteria.

The Executive has reviewed the submission and has identified:

a) a small number of areas where the Board sub-group may wish to seek clarification from Adam Sampson (OLC Chief Executive and Chief Legal Ombudsman) and Rob Hezel, (LeO Director of Finance and Business Services) who will be attending the meeting;

b) One aspect on which the Board sub-group should seek explicit assurance from the OLC Board and Accounting Officer before approving.

Risks and mitigations	
Financial:	OLC has its own Accounting Officer and is required to comply with Managing Public Money requirements.
FoIA:	N/A
Legal:	N/A

Reputational:	Successful establishment of the OLC and Ombudsman scheme is also an indicator of LSB's own success.
Resource:	N/A

Consultation	Yes	No	Who / why?
Board Members:		✓	
Consumer Panel:		✓	
Others:	MoJ comments were sought by the LSB and these are included in the paper.		

Recommendation(s):

The Board sub-group is invited to:

a) Review the OLC's submission on its budget for 2012/13;

b) Seek clarification from OLC executive representatives in discussion;

c) Seek explicit assurance from the OLC Board and Accounting Officer in relation to funding of voluntary schemes activity;

d) Delegate authority to the Chairman to communicate its decision to the OLC Chair after the meeting in light of the necessary clarifications and assurances.

LEGAL SERVICES BOARD

To:	Legal Services Board		
Date of Meeting:	29 February 2012	**Item:**	Paper (12) 13

OLC Budget 2012/13

Executive Summary

Recommendation

The Board sub-group is invited to:

e) Review the OLC's submission on its budget for 2012/13;
f) Seek clarification from OLC executive representatives in discussion;
g) Seek explicit assurance from the OLC Board and Accounting Officer in relation to funding of voluntary schemes activity;
a) Delegate authority to the Chairman to communicate its decision to the OLC Chair after the meeting in light of the necessary clarifications and assurances.

Background / context

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. Whilst the Ministry of Justice (**MoJ**) is the sponsor department for the OLC (as it is for the LSB), parliamentary, financial and performance accountability is shared with the LSB. For instance:

    - the OLC gives its annual report to the LSB which in turn presents it to the Lord Chancellor for presenting to Parliament
    - the LSB must approve the OLC's budget
    - the LSB can set or require setting of performance targets for the OLC.

2. Like the LSB, the OLC is required, so far as is reasonably practicable, to act in a way which is compatible with the regulatory objectives and which it considers most appropriate for the purpose of meeting those objectives. It must also have regard to any principles appearing to it to represent the best practice of those who administer ombudsman schemes.

3. Whilst the LSB has a statutory responsibility to approve the OLC's budget, it made clear in 2010/11 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 submission.

Statutory requirements

4. Para 23 of Schedule 15 to the Act concerns the OLC's budget and states:

(1) The OLC must, before the start of each financial year, adopt an annual budget which has been approved by the Board (LSB).
(2) The OLC may, with the approval of the Board, vary the budget for a financial year at any time after its adoption.
(3) The annual budget must include an indication of –
   a. The distribution of resources deployed in the operation of the ombudsman scheme, and
   b. *The amounts of income of the OLC arising or expected to arise from the operation of the scheme*.

5. The Act also prohibits the OLC from borrowing money without the consent of the LSB (or in accordance with a general authorisation given by the Board) and requires the OLC to give the LSB its statement of accounts for presenting to the Lord Chancellor and Comptroller and Auditor General on its behalf.

6. As an independent NDPB, the OLC also has its own Accounting Officer, Adam Sampson, and Audit and Risk Committee. It has also 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.

Criteria to be addressed by OLC in budget submission to LSB for 2012/13

7. The LSB requested that the OLC address the following areas in its submission:
   - A summary of the key risks to delivering the Plan for 2012/13 and mitigation proposed.
   - The volumes predicted for the year along with a sensitivity analysis illustrating the organisation's response should volumes fluctuate.
   - 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. OLC were also requested to explicitly include within this breakdown staff costs and numbers broken down by function – for instance: enquiries; investigations; ombudsman team; corporate' others.
   - A summary of where the Plan and budget has changed in response to stakeholder responses which should explicitly include the outcome of discussions with MoJ and the extent to which the final Plan and budget takes account of their input.
   - The OLC Board's current thinking on funding for take-on of any new jurisdiction – in particular the funding of planning and establishment work (albeit small) in advance of the take-on of any new jurisdiction bearing in mind that current work is being funded from the current approved regulator levy.

Review of assurances provided by OLC Board

A. Summary of the key risks to delivering the Plan for 2012/13 and mitigation proposed

8. Section 4 (page 7 - 8) of the submission lists the largest risks to the achievement of the budgeted expenditure limit over the 2012/13 period (rather than to delivery of the Plan itself) and describes the mitigation. These are:

- Unplanned variations from contact and case volume.
- Planned investigator efficiency is not met
- Staff turnover varies significantly from plan
- Large legal costs associated with judicial reviews.

9. The submission does not include an assessment of the likelihood of any of these risks but does summarise mitigation in place and this accords with the discussions that we have been exposed to through the Chief Executive's attendance at OLC Audit and Risk Committee (ARC) meetings and the recent joint meeting between Chairmen of LSB and OLC ARCs.

10. Board members may wish to discuss potential risks.

11. In relation to volume fluctuations above 10%, OLC has indicated that it would need additional budget authority and possibly grant-in-aid cash-flow. The former point was the subject of discussion between LSB, OLC and MoJ some time ago, when it was agreed that, without fettering its discretion to properly scrutinise the individual case, LSB would seek to expedite approval of an appropriately justified budget increase in the circumstances of a "spike" in activity. **Board members may wish to invite OLC representatives to discuss why 10% has been identified as the appropriate trigger and, in broad terms, what level of increase might be sought if it were to arise – might a starting point be the marginal cost of additional activity over the 10% threshold?**

12. Board members should be aware that MoJ have commented that whilst they have agreed to the need for additional grant-in-aid cashflow in principle, their view is that, because of lead-times, such a scenario is unlikely to arise as OLC could adjust their business model to cover until the next levy round. This is based on modelling using scenarios such as coal health and the Financial Ombudsman Services PPI experience.

B. Sensitivity analysis used to determine budget assumptions

13. Section 3 (page 5 – 7) of the submission outlines the OLC's volume assumptions and sensitivity analysis. Paragraph 11 above indicates the financial risk attached to budget fluctuations. The submission does not indicate the risk to meeting operational KPIs as a result of volume fluctuations but it is assumed that by taking the actions indicated in the paper eg around recruitment, impact would be mitigated.

14. The baseline volume predicted for 2012/13 is 7.5% above that experienced in 2011/12 but remains below the rate of increase originally anticipated when the Scheme was established.

C. 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

15. Members are asked to refer to the submission:

- Page 4 lists a summary budget including **amounts of income** expected to arise from the scheme. The OLC shows three income streams: levy; case fee income; other income (none predicted).

- Page 6 explains the rationale for the income assumptions. This notes that the **case fee** income is difficult to forecast. It is however clear that case fees are not delivering anything like the up to 10% of OLC's total operational costs originally anticipated. The OLC will consult on the future of case fees during 2012/13. Board members may recall that in approving the Scheme Rules in December 2009, the LSB did so on the basis that the rules around case fees would be reviewed after two years. At that time the Board were keen to support the 'polluter pays principle' (albeit recognising that the OLC does not use this term). **Board members may therefore wish to ask OLC representatives:**
    i. **To confirm that any changes arising from the case fee consultation will take place too late in the year to have any significant impact on case fee income in 2012-13;**
    ii. **What options the OLC is considering consulting on in relation to case fees (the submission erroneously states that the OLC will consult on the future of the levy – this is an LSB responsibility not OLC);**
    iii. **When the proposals for changes to case fees are likely to come to the LSB for consent.**

- The summary budget on page 2 also illustrates how expenditure is distributed across the OLC operation and this is supplemented by further breakdown on pages 8, 10 and 11.

D. Changes to Plan and budget in response to stakeholder responses explicitly including the outcome of discussions with MoJ and extent to which the final Plan and budget takes account of their input

16. Section 2 (page 4) is the relevant section. The submission does not make clear where the Plan has changed as a result of consultation responses and as, at time of drafting, we have not received the final Plan so we cannot review. However, the submission does state that the consulted upon budget, headcount and activity assumptions did not draw adverse comment from stakeholders.

17. The changes to the budget are therefore as a result of refinement of OLC planning assumptions and a commitment to delivering value for money..

18. The submission did not include any comments from MoJ. As this was an explicit requirement, we asked MoJ directly for its views and these are included as appropriate across this paper. In summary these are:

- That the assumptions on page 9 regarding pay progression and revalorisation are dependent on agreeing a pay remit with MoJ;
- Whether the OLC has confirmed that there is to be no change in VAT arrangements for Baskerville House arising from the change in landlord. (Landlords can opt whether or not to charge VAT – the previous landlord did charge VAT, the new landlord may or may not continue with this arrangements. If not, this could generate a 20% reduction on accommodation costs);
- That more work needs to be done to clarify how funding for work to plan for and develop new jurisdictions will operate noting that any work done during 2012/13 will be borne by current approved regulators, that it is ultimately for Ministers to decide to lay an Order and for the LSB to decide and make rules on the levy and how that is apportioned;
- A query on the nature of services to be covered by the £0.7m budgeted for 'fees and consultancy';
- A reminder that case fee changes require Lord Chancellor approval;
- Remarks on in-year budget adjustments reported in 11 and 12 above.

Board members may wish to seek OLC representatives' comments on these issues.

E. The OLC Board's current thinking on funding for take-on of any new jurisdiction – in particular the funding of planning and establishment work (albeit small) in advance of the take-on of any new jurisdiction bearing in mind that work is being funded from the current approved regulator levy

19. The executive does not consider that the OLC's submission is adequate on this point as it stands. Whilst the submission states at page 3 that there is an expectation that "*the additional costs of establishing and development of new jurisdictions will be borne by the stakeholders for the new jurisdictions rather than by the existing approved regulators*" it states that "*no material additional costs will be incurred in pursuing this activity*". It then goes on to state "*the budget for 2012/13 does not include any additional costs or other revenues associated with the development of additional jurisdictions as we would expect them to be self-financing.*" The absence of additional costs does not, however, deal with the question of how the costs of previous and planned activity should be accounted for and recovered.

20. The Board sub-group will be aware from the OLC's draft Business Plan and recent commentary in the press that developing possible new jurisdictions is a particular area of focus for the OLC in the year(s) ahead. Bearing in mind that all current work being done by the OLC is being funded by the current approved regulators through the levy rules made by the LSB, the Board needs to be assured that the current levy is only funding leviable expenditure. The Act is

explicit at Section 173(8) in stating that OLC leviable expenditure "*does not include such proportion of expenditure of the OLC incurred under or for the purposes ...as may reasonably be attributed to the exercise of its functions under sections 164 to 166*". Sections 164 to 166 relate to the establishment of voluntary schemes for resolving complaints. The clear implication is that the development costs for such schemes must be recouped from their operating revenue. However the Act appears to be silent on how the costs incurred in developing a proposal that is not subsequently accepted by the Board and/or the Lord Chancellor should be met.

21. Clearly there is a debate to be had about the point at which activity can reasonably be said to be for the purposes of Sections 164 to 166 – but **the sub-group should seek clear assurance that the OLC Board and its Accounting Officer have properly assured themselves that work relating to the establishment of voluntary schemes is being properly accounted for, so that the levy is not being used for purposes that are contrary to the Act**. This should include clarification by the OLC of the point at which it believes it is starting to undertake activity relating to Sections 164 to 166.

Additional observations

22. **Capital expenditure** – the budget for 2011/12 included £1.5m for capital expenditure although the expected out-turn is only £0.3m for the year. A capital budget of £0.6m is sought for 2012/13. The Board sub-group may wish to seek clarification of the capital expenditure cycle.

23. **Bad debts** – The forecast out-turn for 2011/13 is for £63,000 of bad debts. A figure for this is not included in the budget for 2012/13. The Board sub-group may wish to seek clarification of the reasons.

Recommendation

24. The Board is invited to:
    a) Review the OLC's submission on its budget for 2012/13;
    b) Seek clarification from OLC executive representatives in discussion;
    c) Seek explicit assurance from the OLC Board and Accounting Officer in relation to funding of voluntary schemes activity;
    d) Delegate authority to the Chairman to communicate its decision to the OLC Chair after the meeting in light of the necessary clarifications and assurances.

LSB Paper (12) 13 Annex A, Appendix 1

Office for Legal Complaints

Budget 2012-13

LEGAL OMBUDSMAN

January 2012

Version: 0.2

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1. Executive Summary

2012-13 will be the Legal Ombudsman's second full financial year of operation. We have successfully navigated the first year, and where appropriate have identified and addressed most of the key challenges as to how the scheme operates in practice. We have adapted our process and procedures to meet the needs and demands of both consumers and lawyers. We are still reviewing and developing our business processes and IT systems to ensure that we continually improve the timeliness with which we resolve complaints and the quality of our work, whilst at the same time aiming to drive down our unit cost. As set out in our Strategy and Business Plan consultation document, as an organisation we aim to remain fluid, adapt to circumstances, pre-empting and encompassing change and striving for excellence in everything that we do. We must therefore carefully balance the requirements to deliver economy with the need to manage the risk of being able to react quickly to external pressures.

The budget and assumptions set out below provide an indication of the distribution of resources to be deployed in the operation of the ombudsman scheme for 2012/13 and the amounts of income the OLC expect to arise from the operation of the scheme.

Funding New Jurisdictions

We anticipate that the additional costs of establishing and development of new jurisdictions will be borne by the stakeholders for the new jurisdictions rather than by the existing Approved Regulators. No material additional costs will be incurred in pursuing this activity.

We believe that the extension of jurisdiction is in the interests of existing stakeholders both in terms of delivering the objectives of the Legal Services Act and also through the sharing of indirect overhead costs with the stakeholders of any additional jurisdictions resulting in a lower unit cost.

As a result of the above, the budget for 2012/13 does not include any additional costs or other revenues associated with the development of additional jurisdictions as we would expect them to be self-financing.

Summary Budget

The 2012/13 budget is detailed below alongside the 2011/12 budget and forecast outturn. The budget reflects a pro-active response to the lower than expected activity being experienced and delivers reduced resourcing and a reduced unit cost. It does though allow for an appropriate response to be enacted for unexpected increases in activity.

	2011-12 Budget £'000	2011-12 Forecast £'000	2012-13 Budget £'000
Levy Income	17,495	16,808	16,785
Case Fee Income	1,944	213	212
Other Income	281	290	-
Total Income	**19,720**	**17,311**	**16,997**
Staff Costs	(12,862)	(11,568)	(11,374)
Travel & Subsistence	(94)	(52)	(66)
Fees & Consultancy	(1,131)	(975)	(768)
IT & Telecoms	(1,272)	(1,149)	(1,121)
Premises & Facilities	(1,896)	(1,664)	(1,766)
Other Costs	(257)	(53)	(54)
Interest & Bad debts	-	(63)	-
Contingency	(180)	-	
Total Cash Expenditure	**(17,691)**	**(15,524)**	**(15,149)**
Depreciation	(2,030)	(1,787)	(1,848)
Total Revenue Expenditure	(19,720)	(17,311)	(16,997)
Capital Expenditure	(1,458)	(300)	(600)

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2. Changes to the plan and budget following Stakeholder consultation

Our business plan 2012/13 for consultation included an initial budget assumption of £19.5 m with a headcount of 312 full time equivalents and an activity assumption of 10,000 case closures. These estimates drew no adverse stakeholder feedback, possibly as they would have resulted in a small reduction to the OLC budget compared to 2011/12. During the consultation period we have had further opportunity to refine our estimates of activity for next year and we now expect to close 8500 cases. In order to deliver a substantial reduction in unit cost (approximately 12%) the budget has been reduced by 2.7m and the average headcount for the year is planned to be 258 full time equivalents. This is pro-active action on the part of the Legal Ombudsman executive to give all stakeholders confidence in our determination to maintain an organisation fit for purpose for the activity it is experiencing whilst delivering value for money.

3. Planned Volumes and sensitivity

Planned Volumes

The key measures for the organisation are set out below:

	Expected 2011-12 Activity	Budget 2012-13 Activity
Contacts	76,000	81,700
Conversion ratio (Cases ÷ Contacts)	11.5%	11.5%
Expected Number of Cases accepted (approx.)	8,740	9,396
Expected Number of Cases within jurisdiction (85%)	7,429	7,986
Changes to WIP during the year	233	515
Expected Number of Cases resolved (external measure)	7,662	8,501
Unit Cost (Total Budget Expenditure divided by the No. of cases closed (external measure))	2,258	1,999

Our original planning assumptions set out the expected volumes some 3-5 years after the organisation commenced operation. This reflected the expected view that the number of contacts would increase by around 20% over the initial years of operation. This has not occurred. The depressed state of the economy is likely to have suppressed the number of legal transactions over the last 18 months. As a result, the number of contacts that we have experienced in 2011-12 was lower than anticipated. We have planned for a modest increase in contacts (7.5%) during 2012-13 from this low base which is expected to materialise as the awareness of the Ombudsman scheme increases over time and the number of legal transactions increases.

The Conversion Ratio represents the proportion of contacts which result in a Case being accepted for investigation. This has been steady over the last few months and we see no reason to adjust it for projections.

We exclude from our external reporting of activity those cases where we have accepted a complaint for investigation but which we find, on further investigation, are not within our jurisdiction. This is currently running at around 15% of cases accepted, and is planned to remain at this level during 2012-13. While we have budgeted to accept and deal with 9,400 cases in 2012-13, we therefore anticipate that only around 8,500 cases will result in a resolution of issue for the complainant.

In 2011-12 we anticipate that we will resolve around 7,662 cases. This includes a catch up of cases brought forward from 2010-11, a further catch up will occur in 2012/13.

Investigator efficiency has increased steadily throughout 2011-12 as the Resolution Centre process was refined and improved. We have planned to resolve, on average, 7 cases per month per active investigator in 2012-13.

Sensitivity analysis

The impact of increased contact volumes on the Assessment Centre is relatively minor due to the inherently high volume nature of this part of the operation. The ability to re-deploy investigator resource to assist in the Assessment Centre provides the organisation with the ability to manage short term peaks in call volumes. The 4 key factors which drive the capacity of the organisation to deliver an effective service are:

- **Contact Volume:** A 1% change in Contact Volume results in a medium to long term requirement for an additional 1.1 FTE investigators (£41k per annum plus recruitment and training costs).
- **Conversion Ratio**: A 1% increase in the conversion ratio results in an additional 800 Cases and a requirement for an additional 9.5FTE investigators(£352k per annum plus recruitment and training costs)
- **Investigator efficiency**: A 0.25 case per month decrease in investigator efficiency results in a requirement for an additional 3.75 FTE Investigators over the medium to long term (£139k per annum plus recruitment and training costs)
- **Ombudsman's decisions**: A 6% increase in the number of cases requiring an Ombudsman's decision results in a requirement for an additional Ombudsman(£104k per annum plus recruitment and training costs)

Operational stepped costs are incurred in the form of a requirement for 1 additional Investigation Team Leader (£46k per annum plus recruitment and training costs) for each additional 8 FTE investigators, and an additional Operations Manager (£56k per annum plus recruitment and training costs) for each 40 Investigators.

We have detailed plans in place that would allow us to respond to larger increases in demand of 10% to 40%. These plans will allow us to have additional staffing trained and active within 2 months, however they would require additional budget authority and possibly grant in aid cash flow support in year. These are summarised at appendix I.

The budgetary impact of such large changes in activity is detailed below:

Increase in demand	Additional budget requirement
10%	£965k
20%	£1881k
30%	£2797k
40%	£3713k

We have now agreed with the MoJ that they will support the GIA requirements of these costs and under such circumstances we would expect to obtain in-year LSB budget approval to increase our budget accordingly.

4. Key risks and mitigating actions planned

The largest risks to the achievement of the budgeted expenditure limit are detailed below:

Risk: Unplanned variations from contact and case volume

A short term increase in calls to the service is manageable through the re-deployment of investigator resource to the Assessment Centre. All Investigators are trained to work in the Assessment Centre and are rotated through the Assessment Centre periodically in order to ensure that their call handling skills remain practiced and are maintained. In the event that contact volumes fell substantially, we would review the underlying causes of this change to ensure that this was a “structural” change, and suspend replacement of leavers from the Assessment Centre until the causes were more clearly understood.

An increase in case volumes, whether generated by an increase in contact volumes or simply by more contacts requiring investigation, would impact directly upon the investigator resource pool. The initial consequence of this is likely to be a backlog of cases waiting for investigation and deterioration in the speed with which we resolve cases (our Timeliness KPI).

These risks are mitigated through our recruitment strategy and flexible working policies. Our flexitime working policies allow employees to increase their hours over the short term and to recover these additional hours in the form of “time off” in future months. We have also put in place arrangements to enable us to quickly recruit additional investigator resource to respond to any medium term increase in demand. Although these new investigators will not initially deliver the same efficiency as our established investigators, the additional resource will enable us to minimise any backlog that arises and provide the additional capacity required to eliminate the backlog and minimise the impact upon the time taken to resolve cases.

Risk: Planned Investigator efficiency is not met

Investigator efficiency is key to our resource planning and overall cost; a relatively small change in investigator efficiency makes a significant difference to the number of investigators required to maintain the quality and timeliness of our service.

We have mitigated this risk by ensuring that our resourcing is based on prudent assessments of investigator efficiency. We monitor our Work in Progress, the rate of cases accepted for investigation and cases resolved weekly, and our Investigator efficiency levels monthly to ensure efficiency levels are within the expected range.

We continually review our business process and the way that we perform our investigations in order to seek to streamline and improve these. In the event that planned levels of efficiency were to fall significantly below or above those expected we would initially seek to increase resource while we work to restore and achieve the required efficiency levels.

Risk: Staff turnover varies significantly from plan

The budget allows for a reduction in operational staffing based on current staff turnover trends. Should the rate of staff turnover alter then this will create pressure on the budget. If the turnover was to decrease this would result in higher than expected payroll costs. Given the recruitment activity being undertaken in the local labour market and our experience to date we consider our assumptions to be prudent. The budget features no vacancy factor and this should provide an additional level of insurance in this area.

Risk: Large legal costs associated with judicial reviews

To date we have incurred very little expenditure on external legal support with General Counsel adopting a pro-active approach to cost minimisation. The budget features a £250k reserve for legal costs which in previous years would have been ample. The LSB should be aware that an adverse pattern of JR's would threaten the appropriateness of this figure and the overall achievement of the budget. This is not a new risk however the LSB should be aware of its ongoing presence.

5. Organisation Structure & headcount

The budget reflects a pro-active response to the lower than expected activity being experienced and is based on a re-alignment of corporate staffing levels and a planned in year reduction to operational staffing levels. Assumptions have been made about the likely reduction to operational resources that we expect to happen through staff turnover. The figures below therefore reflect the average headcount budgeted for the year. The 2011/12 budgeted figures and average forecast actuals are included for information.

Headcount plan (FTE)	Budget Average headcount 2011-12	Forecast as at March 2012	Average Budget Headcount 2012-13	Budget Pay Cost 2012-13 £'m
Ombudsmen, & General Council	10	11	11	1.1
Operational Management	11	8	8	0.7
Assessors & Team Leaders	40	40	36	1.1
Investigators & Team Leaders	184	150	145	4.9
Coordinators	13	8	8	0.2
Quality	1	5	5	0.2
Finance and Business Services	28	30	27	1.5
Policy and Communications	15	13	13	0.6
CEO, Compliance and Change	8	5	5	0.6
	310	268	258	10.9

6. Income & Expenditure

Income

Our income is made up of two streams;

- Case Fees – which are charged to Firms which have more than two cases closed in each financial year; and
- The Levy – which is equal to the expenditure incurred by the Legal Ombudsman in delivering the Ombudsman scheme, less Case fees charged.

Case Fee Income is particularly difficult to forecast because this requires us to forecast the proportion of firms which have more than two cases closed in each financial year out of all the cases which we investigate. We have therefore based our forecast income for 2012-13 on our experience the levels of case fees arising during 2011-12. The level of case fee income is substantially below that we expected and we shall consult on the future of the levy during the year. Dependant on the responses to the consultation the levy rules may alter and the amount recovered could be materially different from that collected in 2011/12. However prudence dictates that our budgeted estimate should be in line with our past experience: Levy income for 2012-13 is therefore anticipated to be £16.8m.

Key Assumptions:

Pay Progression & Revalorisation: Existing staff have been recruited on the basis that they must demonstrate competence in their role as part of their probationary period and pass mandatory training and that thereafter they are expected to progress within the organization.

Our pay policy agreed with the MoJ allows us to reflect the increasing competence and effectiveness of our staff as the organisation matures and they become more experienced. We anticipate this will be recognised in the pay remit we agree with the MoJ in 2012/13 as it has been in previous years. The budget reflects the pay policy and the opportunity for performance reviews in October each year.

An average of 1% has been budgeted for revalorisation from July 2012 when the organisation exits from the pay freeze period.

The actual costs in this area will of course depend on both their affordability against this budget and compliance with the pay remit we will agree with the MoJ.

National Insurance: Employer's National Insurance has been budgeted for based on the current rate of 13.8%.

Average Employer's Pension contribution: LeO operates a defined contribution scheme. For the first 190 staff the average Employee contribution to the LeO pension scheme is around 3%. LeO contributes twice the employee contribution up to a maximum of 10%. It is expected that a number of those currently declining to contribute to the pension scheme will eventually join the scheme, and that following the change to automatic enrolment made in January 2011 a higher take-up will be experienced in future. Therefore, an average Employer's Pension contribution assumption of 6% has been used for 2012-13*.*

Core benefits

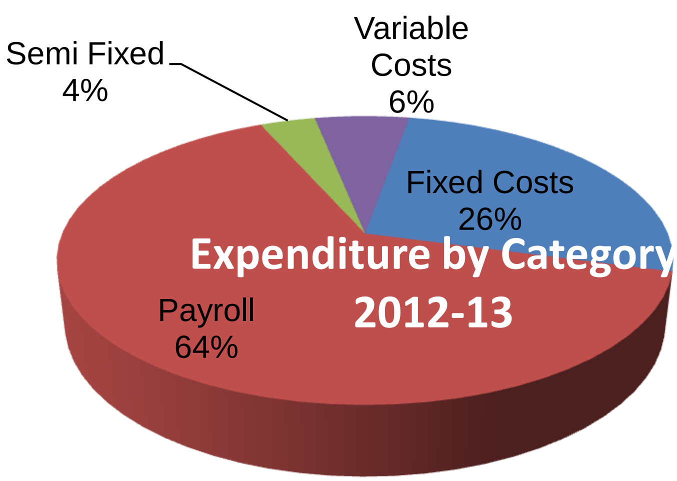
Death In Service and Group Income Protection Benefits have been procured in line with remuneration policy and have been included in the budget as part of the costs of these benefits.

Flexible Benefits: As part of the organisational set up a flexible benefit scheme has been included in the total remuneration package. Employer costs of the Flexible benefit scheme are capped at 3%of basic pay. This has been budgeted in full as part of employee's total remuneration package.

VAT Increase: All VAT-able costs have been budgeted to include VAT at 20%.

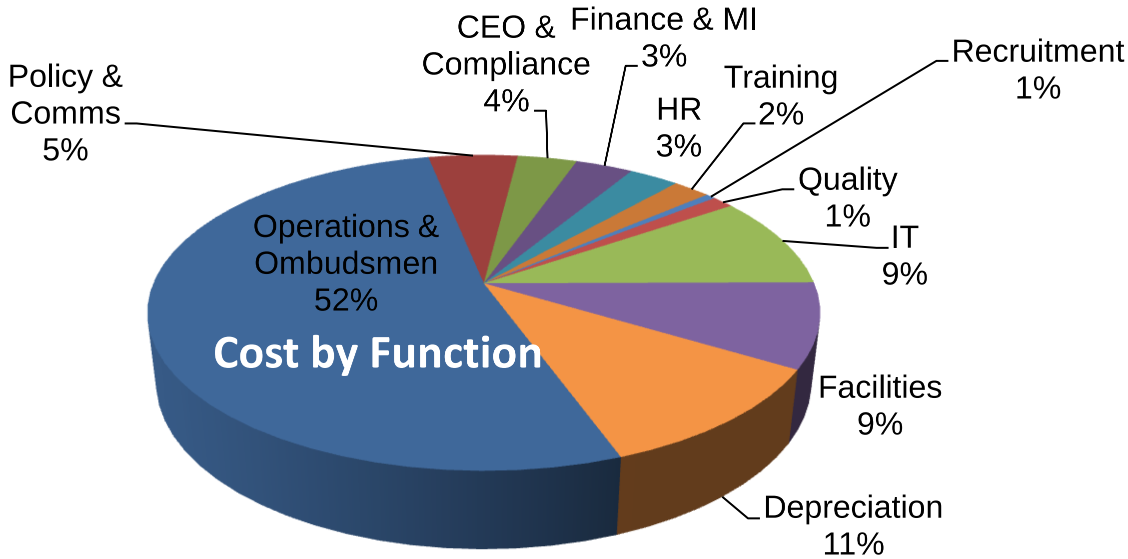
Costs Breakdown

The following charts set out the breakdown of our costs by expenditure type. This shows that a significant proportion 26%of our costs are fixed in nature (comprising Depreciation and other expenditure committed on long term contracts) with a further 4% of expenditure being either demand led or where the opportunity for cost reduction is limited. A further 64% of our costs relate to our people, of which three quarters relates to our Operations and Ombudsman teams This leaves only 6% of truly variable costs.



Costs by Functional area

The following charts provide a breakdown of all budgeted expenditure by the key functional areas;



7. Capital Expenditure & Cash flow

As we head into 2012-13 we have allowed for some ongoing development of our case management system in order to ensure that this can be developed to enhance the quality, efficiency and productivity of the way that we deliver our service. We have also allowed for additional IT hardware to enable flexible working by our employees which we believe will develop and enhance the efficiency and capacity of our workforce over time, and in the medium to long term provide flexible resource able to improve our ability to react to peaks and troughs in demand.

Anticipated Capital expenditure	**£'m**
Systems development	0.25
Hardware replacement	0.20
Other Minor IT	0.05
Office Facilities	0.10
Total	0.60

Our office environment is now fully operational. Final remedial work to enhance soundproofing is expected to be completed during 2011-12 and therefore the budget for 2012-13 allows for only minor ad-hoc capital expenditure for the purchase of replacement of minor equipment items.

Cashflow

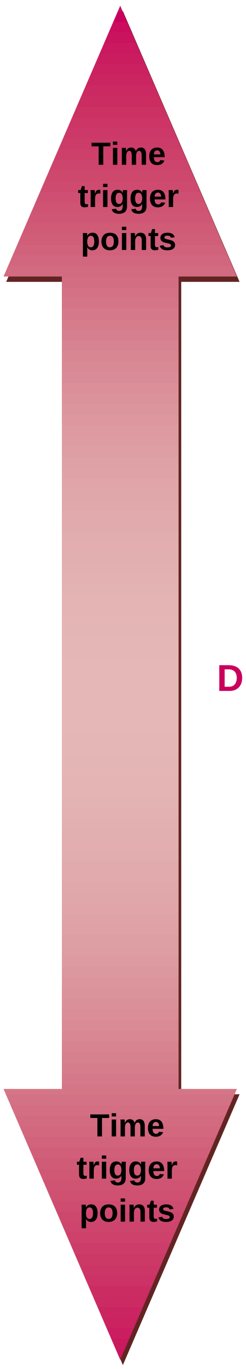
We have forecast Levy receipts for 2011-12 of £16.5m, after deduction of amounts received over and above those actually spent in 2010-11. After final Grant in Aid, Income from the LSO work performed during 2011-12, and Case fee receipts, we forecast an Opening cash position of £17.6m at the start of 2012-13. Our planned expenditure including capital expenditure before Depreciation is budgeted as £15.7m. We would therefore anticipate a cash balance at the end of 2012-13 in the region of £2.1m prior to receipt of 2012-13 levy funds. We do not therefore expect to require additional Grant in Aid during 2012-13.

8. Approval

The LSB board is requested to approve the Budget for the year 2012-13 and note the additional budget requirements should we need to respond to material increases in demand.

Appendix I

Activities & timeframes



Month 5 onwards Permanent	• Recruitment takes 12 weeks + 4 weeks training • Regular cycle of recruitment (quarterly) to replace turnover and maintain profile of LeO as an employer
Months 3 & 4 Temporary	• Procured panel of agencies who are pre-briefed • Contract staff can be recruited and trained in 8 weeks
Months 1 & 2 Existing	• Mixed workforce including, contract / agency staff and permanent staff on variable hours contracts • Ask staff to work extra hours and pay or 'bank' these against time off in lieu • Increase hours on variable hours contracts • Maintain transferrable skills so that staff can be re-deployed (e.g. Investigators to Assessment Centre

DEMAND

Month 1 Existing	• Bring all existing work up-to date and reduce work in progress • Increase training, encourage use of banked hours and take up of annual leave • Reduce hours on variable hours contracts Use resource to create knowledge, complete improvement projects and encourage internal secondments • Encourage take up of part time contracts (with option to revert)
Month 2 Temporary	• Release contract staff
Month 3 onwards Permanent	• Put recruitment on hold • Unpaid leave • Redundancy