

To:	Legal Services Board	
Date of Meeting:	23 March 2017	Item: Paper (17) 10

Title:	OLC budget approval	
Workstream(s):	Performance, evaluation and oversight	
Author:	Julie Myers, Corporate Director	
Introduced by:	Steve Green, OLC Chair, Nick Hawkins, LeO Chief Executive Kathryn Stone, LeO Chief Legal Ombudsman	
Status:	Official	

Summary:

Steve Green, Nick Hawkins and Kathryn Stone will attend to present this item, which follows the Board's informal look at this budget proposal in November 2016.

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 2016, LSB and OLC discussed the OLC's draft budget, which provided Members with an opportunity to probe the OLC's planning assumptions. Based on the issues that emerged at that informal discussion the OLC were sent a suite of acceptance criteria which the formal budget submission would need to meet in order to allow the LSB to approve the budget (in addition to the statutory criteria described above). These were sent to the OLC Chair in January 2017 (see **Annex A**).

The OLC has made a budget submission for 2017/18 to the LSB addressing both the statutory and LSB criteria (see **Annex B**). It has also provided its Strategy and Business Plan as additional context (see **Annex C**). This latter document is a final draft.

The OLC are seeking a total budget of **£14.63m**, for 2017/18 with **£11.63m** allocated to the legal jurisdiction and **£3m** to the CMC jurisdiction. These costs are offset by case fee income of £0.94m legal and £1.07m CMC.

This represents an increase on the OLC's budget for 2016/17 which was £13.63m, comprising 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 only been informal confirmation of budget approval from MoJ.**

Recommendation(s):

The Board is invited to:

- (1) review the OLC's submission on its budget for 2017/18;
- (2) consider approving the budget.

Risks and mitigations

Financial: OLC is required to comply with Managing Public Money requirements. 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, 2014/15 and 2015/16 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:		X	
Consumer Panel:		x	
Others:	John Ward, external advisor to the LSB's ARAC has reviewed the OLC submission. MoJ's formal position was not known at time of drafting.		

Freedom of Information Act 2000 (Fol)

Para ref	Fol exemption and summary	Expires
Annex C	Section 22	N/A

LEGAL SERVICES BOARD

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OLC Budget

Executive Summary

Introduction

1. The Legal Services Act 2007 (**the Act**) requires that the OLC must, before the start of each financial year, adopt an annual budget which has been approved by the Legal Services Board.
2. The budget approval process undertaken by LSB is designed not to duplicate the work properly done by the OLC Board in scrutinising the basis on which the budget has been developed. Rather, the approval process is designed to provide adequate assurance to the Board of the robustness of the OLC process in preparing its budget. The LSB provides OLC with a suite of criteria to address in its budget submission to inform that assurance as a basis for approval. For this year, the LSB acceptance criteria were communicated to the OLC in January 2017 informed by the LSB's discussion with OLC in November 2016 (see **Annex A**).
3. The OLC's submission covers its claims management complaints (CMC) jurisdiction, as well as its legal services complaints jurisdiction. The CMC budget is funded by public funds through 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. 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 **£14.63m** for 2017/18 (for both jurisdictions combined) - **£11.63m for legal** activities and **£3m for CMC** activities). This represents **an increase of £1m** on their 2016/17 budget. This is the first time

OLC have reversed what has been a consistent downward budget trajectory since their establishment. (In 2011/12, their first full year of operation, OLC budget was £19.72m (legal jurisdiction only)). The 2017/18 budget compares against a forecast outturn for 2016/17 of £12.8m (against a budget of £13.63m). OLC report the impact of spending controls in the first part of the year and the reduced need for external professional services as major contributors to the underspend.

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 relationship with the MoJ in accordance with Managing Public Money. Hence, while the LSB approves the *level* of the budget, it does not have ongoing 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.

Acceptance criteria

8. The LSB required the OLC to address the following criteria in their budget submission:
 - 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:
 - 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
 - a summary of the **key risks** to delivering the Plan for 2017/18 **and mitigation** proposed.
 - 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
- 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. In particular, this year, confirmation that capital delegations for the Modernising LeO programme have been approved.
 - Finally, we would like to understand more clearly the rationale behind the significant increase in bad debt contingency. This was mentioned when we met in November and it would be helpful to have this rehearsed clearly in writing.

OLC budget submission

9. **Annex B** contains the formal budget submission from OLC to LSB. This comprises their budget submission and their (draft) Strategy and Business Plan 2017-20. The latter document provides useful contextual information for the budget and also confirms the OLC's intention to revert to a downwards trajectory after 2017/18.
10. The budget submission summary notes LeO's ambitious agenda for the next three years, which is set out in more detail in the companion strategy document, and references the plans for organisation modernisation through the Modernising LeO programme. This includes the IT investment discussed with the Board in November.
11. Since the paper presented to the Board in November 2016, the OLC's total budget for 2017/18 has increased by 2 percent (£0.3m), reflecting the challenge the LSB made in November, about whether LeO had sufficient capacity to deliver the ambitious Modernising LeO agenda. LeO have added
 - a) £0.1m to cover a part-time programme manager and to back-fill operational staff devoted to work on the Modernising LeO programme;
 - b) one-off costs associated with the Unified IT workstream of the Modernising LeO programme of £0.185m;
 - c) one-off costs of £0.1m associated with the Enhance workstream of the Modernising LeO programme, principally to cover costs of implementing a new staffing model to manage the loss of the CMC jurisdiction and which LeO Had assumed would take place in 2018/19 when we presented the budget principles to the LSB in November;

12. The only recurrent addition to the November budget is due to Microsoft increasing their service and licence costs by more than a third (£0.08m).
13. As indicated in the strategy and business plan document at page 16, indicative budgets for future years are projected to be: £12.27m in 2018/19; and £11.8m in 2019/20. This would appear to indicate that the spike in budget in 2017/18 represents costs that do not recur: this could be described as an 'invest to save' strategy.

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***

14. Sections 4, 5 and 6 of the OLC's budget submission document illustrate 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.
15. OLC compare their budget for 2017/18 against the forecast **outturn** for 2016/17 as opposed to their 2016/17 **budget**. Whilst this makes for a more meaningful comparison of spend, the point is made in a number of places that underspends in 2016/17 have been heavily influenced by the impact of spend controls and restrictions, and that spend in some areas has been delayed rather than recurring savings made.
16. For the legal jurisdiction, the most significant points to note are: the proposal for higher staffing related costs (explained in 4.1.3); and the proposal for a greater spend on research, surveys and communications than was achieved in 2016/7 (para 4.1.6). Cases accepted are expected to be static at 7000. For the CMC jurisdiction there appear to be increases across most budget lines as against forecast outturn with a corresponding increase in contacts and cases.
17. The changes in indirect costs are harder to assess as they include proposals for restructuring including the establishment of an Office of the Chief Legal Ombudsman and the associated restructuring of the Operational, Insight and Engagement Team. More specifically, it is not always easy to deduce from the narrative which costs are one-off and which recurring. The narrative around indirect costs of data and surveys was also unclear as para 6.1.8 appeared to

refer to surveys already referred to in 4.1.6. This may represent the apportionment of such costs as opposed to duplication but it would be worth exploring. More generally, the narrative in this section is not as helpful as it could be describing the reasons for changes with much being descriptive about the service rather than the changes.

18. The Board may also wish to explore with OLC the consequences for indirect costs after the loss of the CMC jurisdiction where the submission states that these are not expected to reduce significantly as a direct result of the transfer. The Board may also want to explore whether OLC are seeking transitional costs to fund the depreciation changes for any CMC exclusive assets which will not be taken on by FOS.

19. The submission touches on volume fluctuations for legal at page 13 and CMC at page 17. A formal consultation on case fees is referenced and its likely impact is anticipated as being cost neutral.

Summary of the key risks to delivering the Plan for 2017/18 and mitigation proposed

20. At 8 (page 26), OLC reference the risk to operational delivery as remaining 'similar to those outlined in previous years including for example variations in demand, efficiency and resource levels'. They also have identified four operational risks to delivering the scheme:

- Credibility – scheme loses credibility as a result of service failure
- Demand – delivery of scheme compromised by unplanned changes
- Operational resource – insufficient resource to deliver scheme effectively
- Quality of service – failure to consistently deliver a quality service.

21. Additionally, OLC note that they are accepting a higher degree of risk than usual in 2017/18 in order to make the changes that the organisation needs to deliver sustainable improvement. This decision has been informed by their consideration of the risks of proceeding more slowly or with less ambition. The Board may wish to explore the potential for negative impact on customer experience that this higher risk tolerance may result in.

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.***

22. The submission touches on volume fluctuations for legal at page 13 and CMC at page 17. The sensitivity analysis undertaken is referenced at 7 (page 25) and there is high-level reference to resourcing options should demand increase or decrease.

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. In particular, this year, confirmation that capital delegations for the Modernising LeO programme have been approved

23. At the time of drafting, OLC had received informal budget approval from MoJ and their submission at page 6 and 7 notes the status of discussions with MoJ finance. Stakeholder reactions, which are in line with the sort of reactions LSB receives to its business plan and budget, are at page 7.

To understand more clearly the rationale behind the significant increase in bad debt contingency. This was mentioned when we met in November and it would be helpful to have this rehearsed clearly in writing.

24. The explanation of bad debt in the context of the CMC jurisdiction is explained in detail at 5.1.7 (page 19) and reflects the discussion held with the Board in November.

Observations from the external advisor to ARAC

25. The external advisor observed that:

- the forward projections for the budget post 2017/18 suggested that this would be an invest to save year, although he remained unclear about what were 'one-off' costs for 2017/18 and what would be part of the baseline going forward.
- the suggestion in the submission that indirect costs would remain unchanged post the loss of the CMC jurisdiction were concerning as regards future budgets.

26. The Board will wish to explore these areas with OLC colleagues attending in person.

Recommendation

27. The Board is invited to:

- (1) Review the OLC's submission on its budget for 2017/18;
- (2) Consider approving the budget.