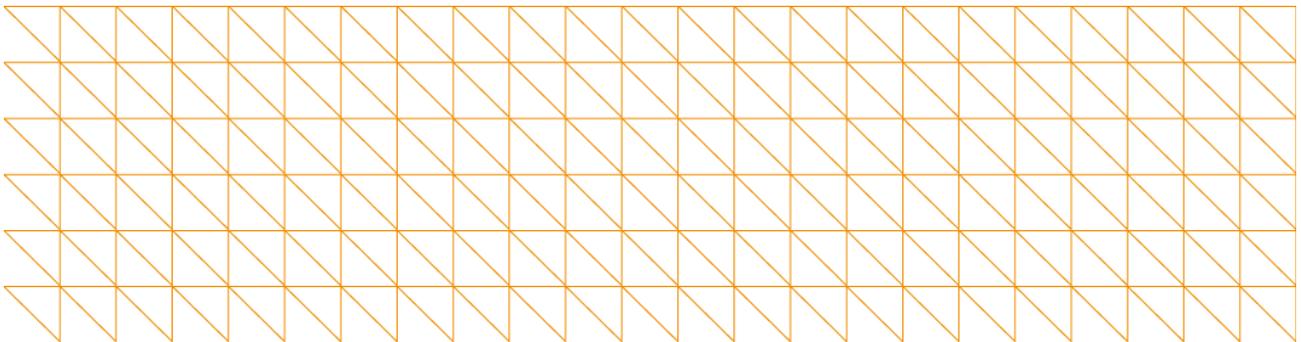




Ministry
of Justice

Transforming Legal Aid: Crime Duty Contracts

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of Justice

Transforming Legal Aid: Crime Duty Contracts

Response to consultation carried out by the Ministry of Justice.

**This information is also available on the Ministry of Justice website:
<https://consult.justice.gov.uk/>**

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Introduction and contact details

This document is the post-consultation report for the consultation paper, 'Transforming Legal Aid: Crime Duty Contracts' which was published on 24 September 2014. It invited comments on the reports produced by Otterburn Legal Consulting and KPMG LLP.

It will cover:

- the background to the report
- a summary of the responses to the report
- a detailed response to the specific questions raised in the report
- the next steps following this consultation.

Further copies of this report and the consultation paper can be obtained by contacting Annette Cowell at the address below:

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This report is also available on the Ministry's website: <https://consult.justice.gov.uk/>

Alternative format versions of this publication can be requested from LegalAidReformMoJ@justice.gsi.gov.uk.

A Welsh language response paper can be found at <https://consult.justice.gov.uk/>

Complaints or comments

If you have any complaints or comments about the consultation process you should contact the Ministry of Justice at the above address.

Ministerial Foreword



Criminal legal aid is a vital part of our justice system. We must ensure it is available for the individuals who need it, sustainable for the lawyers who provide it, and affordable for the taxpayers who ultimately pay for it. We are taking difficult decisions in many areas of public service to reduce government spending, in order to promote economic growth. Legal aid cannot be exempt, and even after the proposed changes - which are in line with the spending reductions right across the Ministry of Justice - we will continue to have one of the most generous legal aid systems in the world - costing around £1.5 billion a year.

I do understand that for the law firms which provide criminal legal aid, these fee reductions and a new contracting mechanism are not welcome. I know the reforms are going to require significant change in the market, if firms are to reorganise themselves in order to be successful at lower fee levels. It is with this in mind

that I believe the Duty Contract approach actually gives law firms the certainty of more work that they need to have confidence in the future and to embark on the organisational changes that are necessary to improve their sustainability. It is also important in discharging my duty to preserve access to justice, by guaranteeing a network of sustainable law firms nationwide to provide a duty service in all police stations.

The most recent consultation exercise has enabled me to consider afresh the number of duty contracts that we make available. Having reviewed the evidence carefully, there will now be 527 contracts, a small increase from the number originally proposed. I think it is important to point out that although the number of contracts will be limited to 527, I am keen there is real scope for a diverse market, with a larger number of firms working together in partnerships and joint ventures, benefiting from economies of scale, delivering a quality service in their local communities. Given we expect the total volume of work to remain constant, I do not foresee a significant change to the number of litigators practising in this area, even if the structure of the market looks different than it does today.

To provide further help to firms in rural areas, we have decided to introduce payments for travelling times in excess of 90 minutes. We will also relax the office requirements in the split procurement areas and London to give greater flexibility. This builds on the support measures introduced earlier, such as introducing interim payments for lawyers involved in lengthy Crown Court cases and establishing a business partnering network to help practitioners with organisational and financial advice, if they need it. We have also worked with the British Business Bank to develop guidance and advice specifically for the legal aid market.

As I have said, I do recognise there are challenges ahead as the market reorganises to adjust to reduced fee levels and new contracts. However, I believe those changes are necessary for the sustainability of the market, in constrained economic times. I also

believe that the new duty provider scheme is the most responsible way of supporting the market to make that transition. The Ministry of Justice and the Legal Aid Agency will do everything we can to work with law firms during the tendering process to deliver the new contracts.

A handwritten signature in black ink, appearing to read 'Chris Grayling', with a long horizontal stroke extending to the right.

Chris Grayling
Lord Chancellor and Secretary of State for Justice

Executive Summary

- (i) The procurement of criminal legal aid services (crime competition) is part of a wider package of reforms in the Legal Aid Transformation Programme. The aim of the crime competition policy is to deliver a fair and sustainable criminal legal aid service. It will do so by offering organisations increased opportunities to scale up to achieve economies of scale and provide a more efficient service that ensures people accused of a crime can receive advice and assistance and, if necessary, representation. The model gives organisations the confidence to invest in the restructuring required in the knowledge they would be in receipt of larger and more certain volumes. This contracting approach also gives the Government the assurance it needs that those accused of a crime will have access to a lawyer by maintaining a sustainable legal aid service. This intention has been consistent since we first consulted in April 2013.
- (ii) The focus of this consultation was on the KPMG and Otterburn reports, the assumptions relied upon in those reports and the taking of a fresh decision on the number of Duty Provider Work (DPW) contracts to offer. Nevertheless, respondents also used this consultation to express general opposition to the dual contracting model. We recognise that many respondents have strongly held views on this point. However respondents largely express views that were considered in previous consultations and have not provided new evidence that the dual contracting model is not viable.
- (iii) We have carefully considered the views of respondents in reaching the conclusions set out in this response. Most respondents disagreed with the KPMG assumptions. Many of the responses expressed views on different assumptions. However, these did not always present a consistent view when taking into account the interplay between those assumptions.
- (iv) To help inform a final decision on contract numbers we engaged KPMG to:
 - Read the consultation response material (summary of key points raised by respondents, responses from the main representative bodies and summary analysis of the responses received via the LCCSA hub);
 - Identify evidence contained within the documentation that related to the assumptions used to underpin the model; and
 - Compare that evidence to what KPMG saw or heard previously and consider the extent to which changes the view of the assumptions.
- (v) KPMG made an assessment of whether consultation responses have offered any new evidence that would make them revise their original report and have concluded that with the exception of the assumption on volumes, respondents have not provided any new evidence which would require them to amend their report. KPMG recommended that the assumption on future volumes of work should be given further consideration, which MoJ has undertaken. As a result of this further work we have decided to tender a total of 527 contracts. Having considered the concerns raised about the application of the dual contract model to rural areas, in recognition of the need to travel across geographical areas, we have also decided to pay for travel time over 1.5 hours. Furthermore, we will allow those with an office in either of

the 'split' procurement areas to bid in the other area if they wish, to allow greater flexibility in the way organisations provide a service.

- (vi) We are today launching a tender exercise for duty provider work. In June 2015, bidders will be notified of the outcome of the tender and services will commence under the new contracts in October 2015. We intend to implement the second fee reduction, of up to 8.75% in July 2015, subject to the further considerations we have already said we will undertake.

1. Introduction

- 1.1 Criminal legal aid is provided so that those accused of crime can receive advice and assistance and, before a court, representation where they need it. Ensuring that those accused of a crime have the right to a defence is a vital part of our justice system.
- 1.2 The procurement of criminal legal aid services (crime competition) is part of a wider package of reforms in the Legal Aid Transformation Programme. The objective of the crime competition policy is clear and has been consistent since we first consulted in April 2013, namely to deliver a fair and sustainable criminal legal aid service by offering organisations increased opportunities to scale up to achieve economies of scale and provide a more efficient service. The model gives organisations the confidence to invest in the restructuring required in the knowledge they would be in receipt of larger and more certain returns.

Case for reform

- 1.3 The idea that the market needs to change is not a new one. Back in 2006, Lord Carter of Coles undertook a Review of Legal Aid Procurement. He recommended moving away from administratively set rates for legal aid work in favour of best value tendering. He envisaged the competitive selection of legal aid providers based on their ability to deliver a sufficient quantity and quality of work at the most economically advantageous price. He made a compelling case for moving to a market-based approach to legal aid procurement. Lord Carter also highlighted the need for market restructuring, and for increasing the average size of providers through growth, mergers and rationalisation.
- 1.4 Practitioners and representative bodies have, over many years, argued that the market in its current form is not sustainable highlighting that there are too many providers chasing too little work. The fragmentation of the market is starker in some areas compared to others and we recognise that some providers have been proactive in taking steps to address their concerns about their future place in the market. However, we recognise that the majority of the market requires support and some parameters within which to consider restructuring.
- 1.5 When we began the process of reform we had one of the most expensive legal aid systems in the world at around £2 billion a year. Given the financial crisis inherited by this Government, we had no choice but to make significant savings. Even after the implementation of all the legal aid reforms we will still have one of the most generous legal aid systems – spending around £1.5 billion each year. The Government has no choice but to reduce spending and the legal aid scheme cannot be immune. By 2015/16 the department's budget will be reduced by around a third in real terms and, as one of our largest areas of expenditure, our reforms to the legal aid scheme will see that particular budget fall by broadly the same amount.
- 1.6 We have already taken steps to reduce legal aid expenditure through a series of reforms implemented between December 2013 and March 2014, most notably the 8.75% fee reduction introduced on 20 March 2014. We made clear in February, our decision (subject to further consideration) to make a further reduction of no greater than 8.75% in mid 2015.

- 1.7 Given the pressure on public finances and the consequential requirement to reduce expenditure in criminal legal aid, the need for an efficient and consolidated market becomes even more acute. We maintain our view that without any Government intervention the market is likely to consolidate in a disorderly manner and may lead to gaps in provision. This would not be in the interests of clients, providers or the taxpayer.
- 1.8 Therefore, if the majority of those working in the criminal justice system recognise and agree that the current way of commissioning those services and the size and structure of the market is not the best way to achieve that aim, it comes down to how and by how much the market needs to consolidate.

February 2014 – Government response

- 1.9 We announced in February the Government's decision to proceed with the procurement of criminal legal aid services through a competitive process. The final model of procurement was set out in Transforming Legal Aid: Next Steps – Government Response.
- 1.10 The model offers an Own Client Work (OCW) contract to any applicant capable of demonstrating they meet the required quality standards thereby giving clients the opportunity to instruct their own provider (assuming they hold a contract). However, for those who do not name their own lawyer, we must ensure, provided they are eligible for legal aid, that they have access to a lawyer. The aim of the Duty Provider Work (DPW) contracting process is to ensure there are providers in each procurement area with sufficient volume of work to be financially viable given the reduced fees. However, in determining the number of DPW contracts, we must weigh-up a series of factors to offer contract sizes that deliver a financially viable proposition against which organisations will bid, whilst still supporting a diverse market including a range of business structures.
- 1.11 The initial decision to offer 525 DPW contracts was made having considered the responses to the two previous consultation exercises (around 19,000 responses in all) and the research commissioned from KPMG LLP and Otterburn Legal Consulting. Both reports (KPMG and Otterburn) were published¹ alongside the Government Response in February but we did not seek views through consultation on the contents of those reports, including the assumptions underpinning those reports. The independent research provided an important piece of data and modelling work to assist us in determining the appropriate range of DPW contracts to offer in each procurement area. Having weighed up all of the analysis, the independent research, the consultation responses and key risks, we decided in February to proceed with the implementation of a model of procurement whereby the maximum number of DPW contracts in the range set out in the KPMG report would be offered.
- 1.12 As set out in February, we expect the current market will restructure itself, within the parameters set out in the tender rules and contract, to deliver services. We have also relaxed the restrictions on the types of the business structure acceptable for procurement to create more flexibility for those wishing to participate in the tender.

¹ https://consult.justice.gov.uk/digital-communications/transforming-legal-aid-next-steps/consult_view

This will give maximum opportunities to the current provider market to continue to deliver criminal legal aid services.

Crime Duty Contract consultation

- 1.13 In June 2014, the Legal Aid Agency (LAA), the body responsible for the commissioning and administration of legal aid services, completed the first phase of the procurement process and notified over 1,800 applicants that they were successful. However, the commencement of the second phase of the process, the Duty Provider Work contract tender, was delayed when, on 19th September 2014, the High Court issued judgment on a judicial review of the Transforming Legal Aid: Next Steps consultation brought by the Criminal Law Solicitors Association and the London Criminal Courts Solicitors Association. The judgment related to the consultation process, specifically the failure to consult on the two reports (KPMG and Otterburn) used to inform the number of DPW contracts on offer, including the assumptions underlying those reports. In light of the judgment, the Government launched a further consultation specifically on those reports and the underlying assumptions with a view to taking a new decision on the number of DPW contracts that should be offered.
- 1.14 This consultation - which launched on 24 September and closed on 15 October - sought views and evidence relating to the analysis undertaken by Otterburn and KPMG, including, in particular, the findings of and conclusions drawn by Otterburn and the assumptions used to underpin the model set out in the KPMG report.
- 1.15 We made clear in the consultation paper that the dual contracting model and the decision to limit the number of DPW contracts were not within the scope of this consultation.
- 1.16 We have reviewed and considered afresh the Impact Assessment and Equalities Statement we published in February and have concluded that these documents do not require amendment at this stage. In particular, we do not consider that the alteration in the number of DPW contracts outlined in this paper affects the appropriateness of those documents. We accept that there will be a need to monitor outcomes of the procurement exercise and the LAA will regularly monitor providers through their contract management and auditing procedures.
- 1.17 We have consulted extensively with practitioners, representative bodies, specialist associations and other interested parties on the mechanism for procuring criminal legal aid services when the current contracts expire next year. Following two public consultations on the model of procurement and this third consultation on a specific element of that model (throughout which we have listened to the views received and made significant changes where appropriate), we are confident the final procurement model for legal aid will continue to guarantee a defence for those who cannot afford to pay and ensure a fair and sustainable criminal legal aid service. What remains is a final decision on the number of Duty Provider Work contracts to offer.

2. Analysis of consultation responses/ Government position

- 2.1 We received 3,942 responses to the consultation, mostly from legal aid providers. The majority (71%) commented using an online template hosted on the London Criminal Courts Association (LCCSA) website that asked a number of multiple choice questions related to our six consultation questions.
- 2.2 The detailed analysis below takes each of the questions in turn, and sets out the responses received.

General position

- 2.3 We were clear in the consultation document that having consulted extensively on the overall approach of the dual contract model and of limiting the number of DPW contracts and announced the way forward in February, this was not at issue in this consultation. The focus of this consultation was on the KPMG and Otterburn reports, to inform a fresh decision on the number of DPW contracts to offer.
- 2.4 Respondents nonetheless used this consultation to express general opposition to the dual contracting model (or what respondents refer to as the two-tier model) as a whole, stating that such an approach was wrong in principle.
- 2.5 Consultees suggested that in their view the shortcomings on the assumptions called into question the validity and practicality of the dual contract model. It is clear that a number of consultees hold very strongly felt views on this point and are deeply concerned about the dual contract model.
- 2.6 However, consultees largely expressed views that were previously considered. Consultees have not provided any new evidence about the viability of the dual contract model. Recognising the concerns raised again by consultees, we accept that there will be a need to monitor outcomes of the procurement exercise and the LAA will regularly monitor providers through their contract management and auditing procedures to identify any issues early and take action swiftly to ensure effective representation is maintained.

Question 1. Do you have any comments on the findings of the Otterburn report, including the observations set out at pages 5 to 8 of his Report? Please provide evidence to support your views.

General Views

- 2.7 It is clear that most respondents agreed with the Otterburn report, and felt that MOJ had not taken into account the recommendations and findings made by Otterburn. The main concerns they highlighted were the assessment that providers have fragile finances which would make further investment difficult; that at least nine months would be required for providers to complete the necessary expansion; that delivery partnership arrangements have regulatory, insurance, economic and supervisory issues that act as barriers; that the majority of providers would not survive the fee cuts, and few who were not successful in securing a DPW contract would be viable either.
- 2.8 It is important to remember the objective of the Otterburn survey. The main purpose of the work was to gather data on the current financial position of providers to feed into the financial modelling undertaken by KPMG. Otterburn's survey related to the current market, KPMG used the survey data from Otterburn and, combined with claim data from the LAA, constructed a model to help inform a decision on the number of DPW contracts to offer. Otterburn drew conclusions from the qualitative information received from the survey respondents and made his own observations of the market. These conclusions and observations were considered alongside all other responses to the Next Steps consultation.
- 2.9 The Government has again taken Otterburns' conclusions and the comments of respondents on those conclusions, into account when reaching a final decision on the number of DPW contracts. We assess the key areas that respondents focused on when offering views on his report.

Profit Margins

- 2.10 Respondents generally agreed with the Otterburn analysis suggesting only the most profitable providers at present will remain profitable under the new model. The views were that the majority of providers are likely to be unable to continue to trade with a 17.5% cut in fees, especially ahead of consolidation. Some argued that only a very small proportion of providers will be viable in their present form and that with low volumes and tight profit margins few providers could survive a 17.5% fee reduction. Some felt that the minimum 5% profit margin suggested by Otterburn was too low to be viable, especially given the inherent risks in the contracts.
- 2.11 Otterburn's finding that many organisations would find it difficult to survive a 17.5% fee reduction is in the context of the current unconsolidated market structure. Consolidation of the market will give organisations the opportunity to access a larger share of work, enabling them to explore economies of scale which will in turn help to mitigate the fee reduction and give them the best possible opportunity to make a sustainable profit. There are a number of ways that organisations could achieve scale in order to undertake DPW, such as through mergers, joint ventures or delivery partnerships. Just over 1,800 organisations have applied for, and succeeded in obtaining, an OCW contract which suggests that a very significant number of organisations consider that work (or at least OCW) at the rates proposed is viable and attractive.

- 2.12 Some noted that the most profitable providers are those employing or run by a small number of solicitors, but commented that these providers would be unable to service one of the contracts; others argued that larger providers were the most profitable.
- 2.13 Whilst we note there are a number of smaller providers with high profit margins, we believe the Otterburn report does show evidence of economies of scale in the existing market. Within the report, Otterburn separates providers into two categories: 50% of the market with above median rates of profit, and 50% of the market with below median rates of profit. The fee levels of these two groups are then set out in tables 5.9 and 5.10 of the Otterburn report. This shows, in general, the more profitable providers tend to have larger revenue from fees (median of £510k, upper quartile of £813k), whereas the less profitable providers tend to have lower revenue from fees (median of £320k, upper quartile £486k). This implies that higher fee revenues tend to mean providers are more profitable and suggest economies of scale do exist.
- 2.14 Data from the KPMG report, which was provided directly by Otterburn, supports this further. The report sets out information on total crime fees and total net profit broken down by the number of criminal solicitors. Once this information is aggregated for the various sized firms across regions, it suggests that larger firms are more profitable. The mean profitability of work undertaken by firms with between 1 and 5 criminal solicitors was a loss of 2.1%, whereas the mean profitability of work undertaken by firms with 13 or more criminal solicitors was 8.5%.

		London	Urban	Rural	Total
Total Fees	1-5 solicitors	£3.0m	£14.4m	£9.6m	£27.0m
	6-12 solicitors	£3.8m	£29.0m	£4.8m	£37.6m
	13+ solicitors	£28.0m	£40.4m	£4.3m	£72.7m
Total Net Profit	1-5 solicitors	-£0.2m	-£0.7m	£0.3m	-£0.6m
	6-12 solicitors	-£0.4m	£2.4m	£0.3m	£2.3m
	13+ solicitors	£2.9m	£3.6m	-£0.3m	£6.2m
Total Rate of Profit	1-5 solicitors	-5.4%	-4.8%	3.0%	-2.1%
	6-12 solicitors	-9.9%	8.3%	6.2%	6.2%
	13+ solicitors	10.3%	8.9%	-6.0%	8.5%

- 2.15 In relation to Otterburn’s finding that providers required a 5% profit margin, according to Otterburn’s own survey nearly half of the market is currently operating on less than 5%, when looking at crime profitability. This suggests that whilst providers would like a minimum profitability of more than 5%, in reality this does not always happen.

Finances

- 2.16 Respondents argued that the required increase in scale to service contracts would be too great for many organisations and that at least nine months would be required for mobilisation.
- 2.17 We believe we have struck the right balance between asking organisations to grow and giving them enough work to remain sustainable. In addition, we have decided to pay for travel costs where a provider has travelled for more than 1.5 hours, which should help having to service larger contracts over a wider geography. In terms of

the mobilisation period, providers have been aware of our intention to consolidate the market in light of fee reductions since our first consultation in April 2013. There is evidence that providers are beginning the process of consolidation through mergers. As long as providers who win DPW contracts are able to deliver the service at the outset, they can continue to grow their business over time.

- 2.18 Respondents also agreed with Otterburn that providers have fragile finances (minimal cash reserves and lack of further banking facilities) which would make further investment difficult.
- 2.19 In relation to the concerns respondents expressed about providers having the financial capability to scale up there is some assistance that Government can provide as transitional support as we set out in February. We have established a business partnering support network, operated by the LAA to offer information and guidance to practitioners seeking help with regard to restructuring their business and how to go about seeking financial support. We believe this is important to provide ongoing support to businesses during the first two years of the new market structure.
- 2.20 Whilst the LAA cannot provide financial advice, it will be able to help providers to find the necessary information regarding funding. We have also opened up specific legal aid market discussions with the British Business Bank (BBB), an Arms Length Body reporting to the Department for Business, Innovation and Skills. We have developed guidance specifically for the legal aid market in conjunction with the BBB on which Government-backed financial products, such as the Enterprise Finance Guarantee, are available to the legal aid market, and have tailored information to specific known working capital and investment funding issues in the sector. This information is available on the LAA website at: <http://legalaidtraining.justice.gov.uk/course/category.php?id=131>. The model gives organisations the confidence to invest in the restructuring required in the knowledge they would be in receipt of larger and more certain volumes.
- 2.21 At the time of the Otterburn report the new interim payment provisions for litigators working on lengthy Crown Court cases had not been announced. These provisions, which were introduced in October, are designed to combat cash flow issues. This means litigators will be paid at more regular intervals on the longer and more expensive cases. Those provisions will substantially help to soften the impact of the fee reductions, before the consolidated DPW contracts are offered.
- 2.22 Respondents also suggested consortia have regulatory, insurance, economic and supervisory issues that act as barriers. We do not underestimate the challenges providers face in trying to make the necessary changes, including those looking to establish delivery partnership arrangements or joint ventures. The basis of any delivery partnership is a matter for those involved. While there are issues to consider we do not believe those are insurmountable.

Contracts and Consolidation

- 2.23 Respondents argued that Otterburn was right to conclude that contracts should be flexible in size as a 'one size fits all' approach was not appropriate. We have looked at the number of contracts required in each procurement area, so contract sizes will vary by procurement area, reflecting the different market structures that exist now.

We have divided some of the procurement areas that we originally proposed to reflect concerns about contracts covering large rural areas.

- 2.24 Some noted there is already some evidence that a process of consolidation is happening naturally. We are aware that some consolidation is taking place in the market. However, the reduction in fees means this has to happen more quickly and we recognise that the majority of the market requires support and some parameters within which to consider restructuring.
- 2.25 Otterburn, and many respondents, suggested competition was not viable in rural areas as the supplier base is already consolidated and over-stretched. We do not believe this is a reason we should not compete in rural areas. The model creates opportunities for those organisations to explore opportunities to bid across more than one procurement area or join with others to operate across more than one procurement area without having to formally merge or grow a single business. We have also decided to relax the office requirements for organisations wishing to bid across split procurement areas and London (for further information see the Next Steps section).
- 2.26 Respondents generally felt the procurement areas were too large, particularly in more rural areas. As set out in the Next Steps section below we are making changes in relation to the office requirement in the 'split' procurement areas and London and payments for travel time in excess of 1.5 hours to address issues in rural areas

Own Client Work

- 2.27 Respondents felt that OCW contracts alone would not be viable in the medium term in their own right – currently only a small proportion of providers only undertake OCW (usually specialist VHCC or prison law providers).
- 2.28 In February 2014 we decided to allow an unlimited number of OCW contracts in response to the overwhelming view from the profession that individuals should retain the ability to choose their provider. Since then, 1,800 providers have applied for, and been awarded, own client contracts which suggest they see this work as viable.

Overall Government Position

- 2.29 The Government has again taken Otterburn's conclusions and the comments of respondents on those conclusions, into account when reaching a final decision on the number of DPW contracts. As set out above, the main purpose of the work was to gather data on the current financial position of providers to feed into the financial modelling undertaken by KPMG. Otterburn's survey related to the current market, KPMG used this information and, combined with LAA claim data, constructed a financial model to help inform the decision on the number of DPW contracts to offer. It was beyond the scope of Otterburn's research to provide a view on the number of contracts that would be supported in a post fee reduction market.

Question 2. Do you have any comments on the assumptions adopted by KPMG? Please provide evidence to support your views.

- 2.30 Before dealing with respondents' views on each assumption it is helpful to explain the purpose of the KPMG model. We recognise that each individual organisation will make decisions and choices in respect of their own position in the market, their financial stability, desire to expand, their commercial approach etc., The KPMG model is not attempting to predict exactly how each individual provider will respond, as each will have individual decisions to make. Therefore, the most appropriate way to capture and explore the trade-offs and tensions between those decisions, is to construct a financial model based on a series of assumptions.
- 2.31 We (and KPMG) have always been clear that the model was based on assumptions on future behaviour. Such assumptions always have an element of uncertainty. Self-evidently, we cannot wait until we know whether the assumptions are accurate predictions or not – we will only know once the contracts are live. The model looks at all the options and creates proxies for aggregate market behaviour but ultimately it is up to each individual organisation to decide how they want to proceed.

General views

- 2.32 Most respondents disagreed with the assumptions contained in the KPMG financial modelling. Many felt they did not base their assumptions on Otterburn data or any independent process – instead they claimed they were determined by MOJ. Each assumption is dealt with in turn below, but it is not true to say that they were determined by the MoJ; they were derived from a combination of Otterburns' findings, KPMG's expertise, MoJ experience of the legal sector, and discussions with the Law Society.
- 2.33 Many of the responses criticised some or all of the assumptions as unrealistic or undesirable, claiming that their firm would not take such a course of action.
- 2.34 In commenting on the assumptions in the KPMG report, it is apparent that respondents were thinking in terms of how they operate now under current structures, rather than how they would respond to meet the demands of the new system.
- 2.35 It is important to highlight that the assumptions cannot be considered in isolation as the application of one assumption has an impact on another. Therefore, in our response to each key point raised by respondents as set out below, we have endeavoured to highlight the interplay between each assumption.
- 2.36 In addition to our own consideration of responses, we asked KPMG to review information received during the consultation and consider whether their original report requires amendment or further analysis. The outcome of their work is published alongside this response.

Own Client Work

- 2.37 Respondents felt strongly that providers would just not give up any OCW; therefore the 50% substitution assumption was simply wrong. They said providers do what they can to keep loyal clients, sometimes providing work across a number of years and generations. Respondents were also very clear in their arguments that to give up OCW would in fact damage the reputation of the organisation and diminish what they

feel is at present the 'true quality mark' of the criminal legal aid market. Some pointed out that businesses have greater certainty from own clients, whereas duty work was more of a 'lottery' and that any organisation would need both in order to survive.

- 2.38 We recognise that no organisation would wish to give up any OCW and that in a sector where too many organisations are chasing too little work, providers will do their best to ensure they keep as many clients as possible. However, the model does not force an organisation to take any particular action but assumes that organisations will make a choice. Some firms will choose to keep all of their OCW and may therefore have to grow their business. Others will not grow their business (some consultees have stated this in response) either out of choice or because they are constrained in terms of their capacity. As DPW contracts offer greater certainty of volume, we believe those organisations which do not grow, when faced with that choice, would forego OCW.
- 2.39 We acknowledge that each organisation will behave in different ways depending on their own circumstances and approach to delivery of the services. This level of uncertainty lends itself to the inclusion of an assumption to capture the unpredictability.
- 2.40 However, whilst a number of respondents argued they would not give up any OCW, they also argued they could not sufficiently expand through organic growth or by utilising latent capacity.
- 2.41 The overwhelming majority of respondents who commented adversely on this assumption did not provide any analysis as to how in practice they would discharge their obligations under a DPW contract whilst retaining all OCW (e.g. no evidence of how they would grow to meet the challenge, recruit additional staff etc). There is tension between assumptions regarding OCW substitution and organic growth and latent capacity. Providers that suggest they will struggle to grow by the amount necessary to meet their DPW Contract, will be faced with a choice regarding how they service their DPW contract.
- 2.42 Whilst we have reconsidered the 50% assumption given responses to consultation and KPMG's view (which we agree with) that "No evidence of what will actually happen will be available until contracts are let", we have not run the model with 100% retention of OCW (the figure proposed by most consultees who suggested an alternative figure) because the other points made by consultees (on growth challenge and latent capacity) actually provides a strong indication that organisations would not be able to meet the growth challenge involved in retaining 100% of OCW and holding a new duty contract. This suggests that respondents, in approaching the 50% assumption, were focusing on what they would like to happen in the future rather than what in practice they would be able to do.

Organic Growth

- 2.43 The majority response was that a 20% organic growth is not a reasonable assumption to make given the potential 17.5% reduction and the impact this would be likely to have on salaries if that was the means organisations chose to make efficiencies. A number of respondents argue that due to low levels of profit for organisations in this market, providers cannot invest in structural changes needed to recruit new staff, especially if required rapidly. This view was highlighted by Otterburn himself in his response to the latest consultation.

- 2.44 It is apparent that when responding to this assumption that practitioners and representative bodies are thinking in terms of how they operate in the market currently, and their ability to recruit facing a 17.5% reduction in fees and the availability of resource. In a consolidated market, with limited access to DPW, it should be easier for the providers that win DWP Contracts to recruit external staff. In addition, market consolidation will require restructuring of the cost base of organisations, which will generate economies of scale that can drive savings without necessarily having to reduce fee earner salaries. Though organisations may choose to drive down staff costs as well. Providers have not provided evidence of why they are unable to grow. The assumption about new entrants was not that new entrants would be brand new players in this market rather that the market would reconfigure through a process of merger, joint venture and partnerships. Some existing firms might expand into new procurement areas. These arrangements are counted as new entrants in our model.
- 2.45 Whilst some respondents suggested they can grow their business to a greater extent than the model assumes (one suggested by about 40% compared to the 20% included in the model), most respondents that argued that no provider would give up their own client work (see above) also argued that they cannot grow their businesses to the extent required by the proposals.
- 2.46 As set out above, there is tension between assumptions regarding OCW substitution and organic growth and latent capacity. Providers that suggest they will struggle to grow by the amount necessary to meet their DPW Contract, will be faced with a choice regarding how they service their DPW contract. Providers who are unable to expand their business (organic growth) or join with other organisations (through delivery partnerships or joint ventures) can explore opportunities to use under-utilised resource (latent capacity) or give up some of their OCW.

Latent Capacity

- 2.47 Respondents said that the 15% latent capacity was wrong and based on an invalid calculation. Work is undertaken in 'dead' time on duty when not responding to a call. In most areas rotas are also much longer than 8 hours.
- 2.48 Under the new method of allocation, Duty Providers will be awarded an equal share of slots to resource as they see fit (provided it meets the contractual requirements) and not based on the number of Duty Solicitors they employ. The use of accredited representatives and the flexibility of resourcing a specific duty slot by firm rather than by individual will enable organisations to explore further opportunities to exploit any remaining latent capacity.
- 2.49 Respondents argued that there was no evidence that if providers have scaled down in recent years they would have the latent capacity to scale back up. Respondents highlighted that KPMG say there are only 'anecdotal indications' of latent capacity.
- 2.50 On the whole, work volumes have fallen in recent years, but the number of duty solicitors doing legal aid work is broadly the same. This suggests there is capacity in the market to undertake more work even without the flexibility of the new system described above.

2.51 As set out above, there is tension between assumptions regarding OCW substitution and organic growth and latent capacity. Providers that suggest they do not have any underutilised resource in their organisation will be faced with a choice about how they service their DPW contract. Providers who do not have any under-utilised resource (latent capacity) can explore opportunities to expand their business (organic growth) or join with other organisations (through delivery partnerships or joint ventures) can or give up some of their OCW.

Profitability

- 2.52 Respondents said that break-even was not the minimum level of profitability for sustainable trading. Some respondents misinterpreted this assumption, believing that KPMG and MoJ were suggesting that organisations would bid for a contract accepting that they would only achieve a 0.1% profit margin.
- 2.53 0.1% is the floor in the KPMG model – not a suggested aspiration. The model certainly permits providers to make a profit (including a profit over the 5% outlined by Otterburn) and the Government is not preventing providers making such a profit. However, the Government does not consider that it would be appropriate to build into the model for determining how many DPW contracts an assumption that providers should make a significant profit from work which is publicly funded or to specify what that specific level of profit should be.
- 2.54 The model showed that in order to achieve a higher profit margin, organisations would need to explore greater staff efficiency savings. Conversely, organisations may offset the need to find greater staff efficiency savings by exploring mechanisms to use latent capacity. The model focuses on the smallest bidding provider within an area and assesses the staff efficiency challenge for that particular provider to break-even. The larger bidding providers within that area are likely to be more profitable than the smallest.²
- 2.55 A 0.1% profit assumption assumes that all staff including equity partners will be properly paid and all existing costs met. An organisation will not know in advance of being awarded a contract what level of profit they might make, and will clearly not be aiming to make a profit as low as 0.1%. However, on the assumption that (contrary to its own expectations) the organisation only achieves a profit as low as 0.1%, then bearing in mind all staff had been paid and costs met the organisation would not become unviable simply by virtue of only having broken even and could continue to trade. A organisation which did get as low as 0.1% profit would be likely to strive to find ways to make further efficiencies so as to improve its profitability going forward. Conversely, organisations may offset the need to find greater staff efficiency savings by exploring mechanisms to use latent capacity.
- 2.56 No new evidence has been presented by respondents. All of the points raised were either raised by the Law Society, by practitioners or by other representative bodies in previous consultation exercises or through the extensive engagement throughout that process.

² See page 34 of the KPMG report

Volumes

2.57 A number of respondents repeated their observations that crime volumes have fallen over previous years and criminal legal aid expenditure has also dropped. Therefore, they argue that any forecast used to determine volume led contract sizes should include an assumption that volumes will continue to drop.

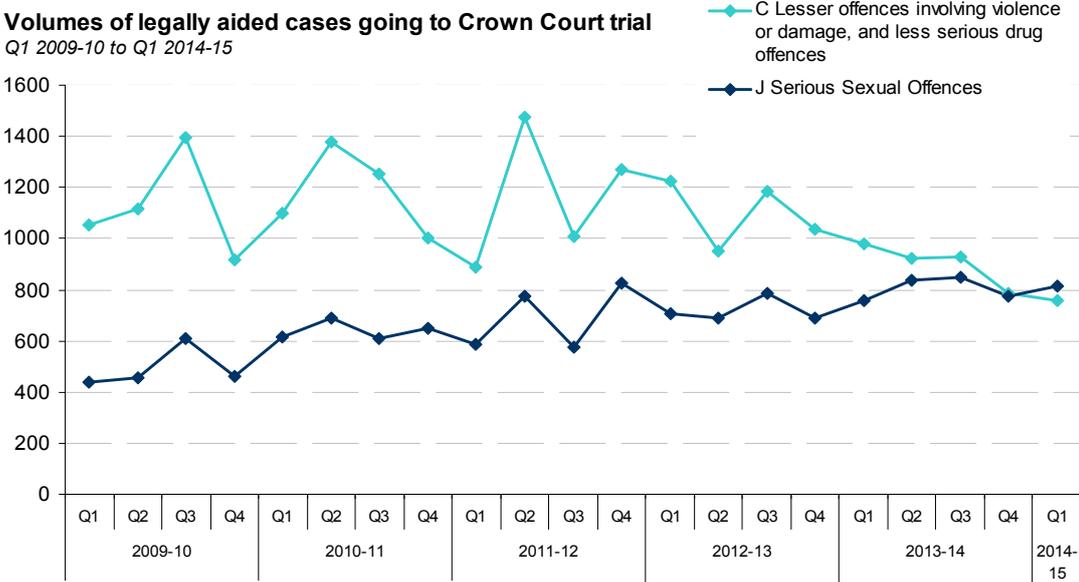
2.58 In light of responses to the consultation, we have given further detailed consideration to our assumption that volumes will remain flat over the period of the contract and have considered the implications of this on the number of contracts on offer. There are two main factors to examine:

- Is a flat volumes assumption, in the medium term, a reasonable one to make (e.g. do we expect volumes to continue to fall in the future)?
- Would using more recent data to assess contract numbers lead us to change anything?

Is a flat volumes assumption appropriate?

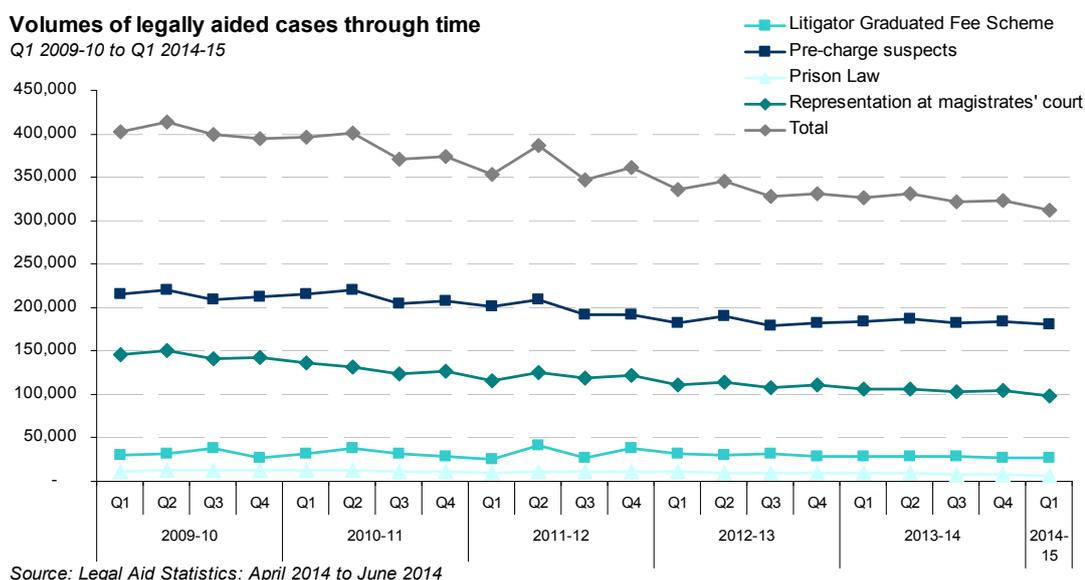
2.59 It is important to note that case volumes alone do not drive legal aid expenditure. There are other factors which are important:

- Supply side factors - In practice HMCTS will consider a range of factors in setting its sitting day levels for any given financial year including unprocessed cases, receipts, disposals and the impact that these have upon the wider justice system. These decisions on volumes going through the court also have a significant bearing on legal aid spending in any given year. A future increase in sitting days might lead to an increase in legal aid spending.
- The case mix matters - the mix of crime has a big impact upon legal aid expenditure – LAA analysis of recent trends shows that the lower levels of less serious crime are decreasing but that this is not the case for complex, more expensive crimes. The graph below shows how there are a decreasing number of trials for less serious violence, damage or drug offences, whilst the number of trials for serious sexual offences is increasing. Having more serious and complex cases in the Crown Court puts upward pressure on legal aid expenditure.



Source: Legal Aid Statistics: April 2014 to June 2014

- 2.60 These factors affect legal aid expenditure to different degrees depending on whether the work is pre-charge, post-charge or litigation work in the Crown Court.
- 2.61 For expenditure on pre-charge work at the police station, the volume of legally aided cases moving through the police station is clearly an important factor. However where the case arises geographically will also have an impact on overall spend as cases are paid at different rates depending on their location.
- 2.62 While case volumes also drive legal aid expenditure in the magistrates' and Crown Court, the complexity of the case mix and the number of sitting days also play an important role.
- 2.63 The MoJ currently assumes flat future volumes when forecasting legal aid expenditure because it is very difficult to forecast crime. There are a number of drivers behind crime volumes which are hard to predict.
- 2.64 The most recent published data from the Legal Aid Agency indicates the total volumes of legally aided work have fallen in recent years. However, the data also shows that there is volatility in the volume of work each year, particularly in the Crown Court, and that overall volumes are beginning to flatten. In fact, the volume of pre-charge cases in 2013/14 was higher than in 2012/13, the first year on year increase since 2008/09.



- 2.65 In addition, some indicators suggest that we also may expect volumes in other areas to rise in future years; for example, legal aid applications in the Crown Court increased from 112,607 in 2012/13 to 122,094 in 2013/14, which may suggest future upward movement in Crown Court volumes (which tend to be the most expensive cases).
- 2.66 Given the difficulty in forecasting crime and the most recent data on volumes, it would not be prudent for the MoJ to assume that crime continually falls into the future.

2.67 Taking all these factors into account, our view remains that assuming that legal aid volumes remain constant at current levels into the future is a prudent assumption both for financial planning purposes, and for analysing the appropriate number of duty contracts to award.

Does the more recent 2013/14 data change our views on contract numbers?

2.68 To assess whether more up-to-date information would have led to wholesale changes in contract numbers, we have considered whether 2013/14 data is materially different to the data provided to KPMG for the analysis published alongside the February 2014 consultation response. When KPMG did their original analysis the latest data available was for the period October 2012 to September 2013 (hybrid financial year). Since the KPMG report was published, the full financial year of data for 2013/14 has become available. On an aggregate level, DPW in the new data is very similar to the data used by KPMG. As such the MoJ believes that wholesale revisions to the KPMG analysis are not necessary.

2.69 However, we do acknowledge that the data available at the time KPMG undertook their original analysis may have in some areas not been a 'typical' indication of the volume of duty work available (as a result of operational issues at particular police stations) and so these areas may warrant further attention. In each procurement area, we have made an assessment of whether we observe a large shift in estimated duty work when examining 2013/14 data compared with the hybrid year. This is so we are able to make a judgement about whether we should take a different view on the number of contracts to be offered.

2.70 Aside from any changes to volumes and values, when making a judgement about the number of contracts in each area, there are a number of other factors to consider. These are:

- If the procurement area has a minimum of 4 contracts awarded for access to justice reasons.
- The staff efficiency challenge in each procurement area and how changes in contract values may affect this.
- The consolidation challenge in each procurement area and how changes in contract values may affect this.

2.71 At the individual procurement area level we looked closely at the most recent year of data (2013/14) compared with the data provided to KPMG (October 2012 to September 2013) to determine whether duty work in each procurement area provided to KPMG, was a typical representation of duty work in that area. When the analysis indicated that the October 12 to September 13 year may not have been a typical representation of work in an area, we considered whether it was necessary to revisit the number of duty contracts on offer, also taking into consideration the factors set out above.

2.72 Careful consideration of this analysis has led us to judge that the 2013/14 data is more representative of what we expect future DPW to be in five areas. Two areas, Richmond-upon-Thames and Suffolk 2 had reductions in duty work that needed further consideration; however the minimum of four contracts had already been offered in these areas and so no changes to contract numbers have been made.

2.73 Three additional London procurement areas required further consideration and we are adjusting the number of contracts in these areas. In Camberwell Green we will offer an additional two contracts, in Kingston-upon-Thames one additional contract and in Wimbledon one fewer contract. Because we have observed large differences in DPW in the recent data – due to operational reasons, which are set to continue into the future – we are able to vary the number of contracts in these areas whilst maintaining a similar staff efficiency and consolidation challenge to that which is reported by KPMG.

2.74 Overall, this assessment provides us with two additional contracts - taking the final number to 527.

Minimum bidders for competitive tension/ staff efficiency/ incumbents of scale/ market consolidation thresholds

2.75 Respondents thought the assumption about new entrants was unlikely to be true given the low profits in this area. The assumption about new entrants was not that new entrants would be brand new players in this market, rather that the market would reconfigure through a process of merger, joint venture and partnerships. Some existing firms might expand into new procurement areas. These arrangements are counted as new entrants in our model.

2.76 Respondents also thought it would be unlikely organisations would be able to make large savings in staff costs, given that remuneration has been frozen for a number of years, and cut further in recent years. Market consolidation will require restructuring of the cost base of organisations, which will generate economies of scale, which will drive savings without necessarily having to reduce fee earner salaries. Though organisations may choose to drive down staff costs as well.

2.77 Respondents noted that KPMG's report, dated 11 March, only identified 23 areas that would be viable and have sufficient capacity for the new contracts. KPMG's report set out the financial modelling undertaken to advise on a range of DPW contracts in each procurement area, based on a series of assumptions and the consolidation and financial viability challenges for the current market. The report set out a number of areas in which the market consolidation challenge and/or financial viability challenge exceeded thresholds beyond which further inspection would be required. KPMG have confirmed that there is no new evidence within the responses to the most recent consultation which make an update to their report necessary. We have considered this advice and the consultation responses and are not persuaded that there is evidence to necessitate a change in our position.

Overall Government Position

2.78 In commenting on the assumptions in the KPMG report, it is clear that most respondents were thinking in terms of how they operate now in the current environment, rather than thinking about the future and how they would respond to meet the demands of the new DPW system.

2.79 In light of the consultation responses and the further advice from KPMG, we have reconsidered the assumptions. We think that the assumptions remain appropriate predictions of future behaviour on which to base our decision. This does not mean that we can be sure that markets will indeed behave in "compliance" with the assumptions – but we regard them as sound assumptions on which to base a decision. For the reasons outlined above, we do not think there are other

assumptions that are more appropriate predictions of future behaviour than the assumptions used by KPMG.

- 2.80 The views from respondents, in particular with regard to the 50% OCW substitution assumption, illustrate the extent to which the KPMG model is precisely that – a model – and organisations will take decisions that are best for them rather than necessarily act precisely in accordance with the model. No model is capable of reflecting all of the individual decisions organisations might make.
- 2.81 KPMG presented a range of DPW contract numbers for each procurement area having assessed the market's ability to cope with two challenges: consolidation and financial viability. The decision announced in February, in line with the request from the Law Society, was to offer the maximum number of DPW Contracts in the KPMG range.
- 2.82 As discussed above, the KPMG model is not attempting to predict exactly how each individual provider will respond, as each will have individual decisions to make. For example, virtually all respondents disagreed with the assumption that organisations would substitute any OCW in order to undertake DPW, instead arguing that organisations would keep 100% of their own client workload. The majority of respondents also disagreed with the assumption that it would be possible to achieve a 20% growth in capacity through recruitment. Furthermore, they argued that organisations do not have latent capacity. These three arguments appear to be in tension. The retention of OCW could be achieved by reallocating resources from OCW, by expanding through recruitment, or by using under-utilised capacity. As above, we understand that all of these strategies may appear undesirable within the current structures, but they are the choices organisations will face when awarded or deciding to bid for a DPW contract.
- 2.83 Having reconsidered the assumptions and sought the views of KPMG, we gave further consideration to one of the assumptions – that volumes will remain flat. As noted above, our further consideration has led us to conclude that a flat volumes assumption remains the most appropriate. We consider that there is no new convincing evidence that the assumptions are not a reasonable reflection of the decision variables that new duty contract holders will need to consider. While almost all the 3,942 respondents did not agree with the assumptions (and some presented arguments on one assumption in contradiction to their arguments on other assumptions) they did not provide evidence that the assumptions were wrong and, when taken together, indicated that respondents were not considering how they might react if awarded a duty contract in the future.
- 2.84 Whilst we recognise the concerns about a number of the assumptions relied upon by KPMG, we note that the concerns are likely to pull the number of contracts in different directions. Even if we accepted there was a case for changing the assumptions it is not clear that this would result in a range of contract numbers that is materially different to the range provided by KPMG.

**Question 3. Do you have any comments on the analysis produced by KPMG?
Please provide evidence to support your views.**

- 2.85 Most respondents said the KPMG's analysis was based on flawed assumptions. Some said that the KPMG report does not take delivery partnerships into account when determining the minimum revenue required to be viable. Some noted that KPMG highlighted the challenges for the market in consolidating in the way the model requires. In relation to London it was suggested that if an organisation is one of the largest bidders in more than one area, its' expansion will have a knock on effect on the scaling up required by other organisations in these areas, which may mean the expansion required in London has been underestimated.
- 2.86 KPMG's approach to the development of the model is clearly set out in KPMG's report. As set out above, the views from respondents regarding the different perspectives and approaches illustrate the extent to which the KPMG model is precisely that – a model – and organisations will take decisions that are best for them rather than necessarily act precisely in accordance with the model. KPMG made no assumptions about how the market could grow.
- 2.87 As set out above, we do not agree that organisations that win duty contracts will not be able to grow. We have established a business partnering support network, operated by a team of business support experts in the LAA to offer information and guidance to practitioners seeking help with regard to restructuring their business and how to go about seeking financial support. We have also opened up specific legal aid market discussions with the British Business Bank (BBB), an Arms Length Body reporting to the Department for Business, Innovation and Skills. We have developed guidance specifically for the legal aid market in conjunction with the BBB on which Government-backed financial products, such as the Enterprise Finance Guarantee, are available to the legal aid market.
- 2.88 In addition, the new interim payment provisions for litigators working on lengthy Crown Court cases that we recently introduced are designed to combat cash flow issues. Those provisions will substantially help to soften the impact of the fee cuts, and will help providers to manage any cash flow challenges posed by the transition.
- 2.89 We are already seeing some evidence of scaling up. Some criminal legal aid firms have already taken steps to prepare for the procurement by merging.

Question 4. Do you have any views on the MoJ comments set out in this document? Please provide evidence to support your views.

- 2.90 Respondents said MoJ was wrong to accept the assumptions contained in the KPMG report and wrong to believe that consolidation necessarily produces economies of scale. Respondents argued that quality levels will fall and that client choice will be illusory if large numbers of providers have to close. Respondents also said that MOJ has not followed up on KPMG's recommendations for further consideration and analysis – e.g. the nine areas facing the biggest challenges.
- 2.91 As set out above we believe the assumptions remain reasonable assumptions for modelling purposes. The model will ensure that, as now, clients have a choice of representative. Although there will be a smaller pool of duty contract holders we have already let 1,800 own client contracts. Otterburn data suggests that there are economies of scale in this market as providers with higher rates of profit tend to have higher levels of revenue. In the procurement areas we have split organisations will be able to bid in both areas if they wish to do so. As set out above we are allowing payment for travel time over 1.5 hours to make duty contracts more sustainable in rural areas.

Question 5. If the assumptions and data on which the KPMG recommendations are based remain appropriate, do you consider that there is any reason not to accept the maximum number of contracts possible (525), as the MoJ have done? Please provide evidence to support your views.

- 2.92 Respondents did not generally suggest specific numbers of contracts. Some suggested KPMG should revisit their modelling, using the assumptions suggested by Otterburn and the professions. Some felt more contracts were needed, especially in the areas with fewest contracts to avoid conflicts of interest.
- 2.93 As set out above we have reconsidered contract numbers and are proposing net increase of two contracts in light of our examination of changes in volumes in each procurement area that might suggest a different number of contracts should be awarded.
- 2.94 As we said in February, there will always be a pool of cases that involve more than one defendant. We need to ensure there are a sufficient number of contractors in each Criminal Justice System (CJS) area to provide advice and assistance and representation to clients where there may be a conflict with another defendant. We have determined that a minimum of four contractors in each area would address this factor. We stand by our analysis set out in Next Steps that less than 1% of police station cases and less than 0.1% of Crown Court cases involve more than four defendants. We believe this would be a manageable number of cases to allocate to another contractor in a neighbouring CJS area or to a pool of reserve contractors when such conflicts arise.

Question 6. Do you have any other views we should consider when deciding on the number of contracts? Please provide evidence to support your views.

- 2.95 Respondents questioned the need to make savings at all given falling volumes. Respondents felt that the ability to make economies of scale was limited due to low capital reserves, redundancy payments, length of time for mergers and economies already made. A number of providers have already outsourced IT infrastructure and development and the majority of micro providers have already reduced their overheads to a minimum. Some felt economies of scale might be achieved through mergers, but not through the use of delivery partners due to the administrative burden and regulatory issues. The model requires organisations to provide services over much larger areas, which incurs extra infrastructure and management costs which are diseconomies of scale, which would be a particular problem in rural areas. Some suggested there would be a disproportionate impact on BAME providers, as the smallest providers. Some respondents questioned why the dual own client and duty provider model was not being re-considered.
- 2.96 As we set out above, respondents used this consultation to express general opposition to the duty contract model as a whole, stating that a two tier model was wrong in principle. We were clear in the consultation document that decisions on the overall approach we consulted on last year and confirmed in February. All of the arguments against moving to the proposed duty contract system were considered properly and taken into account prior to the decision being confirmed in February

3. Next steps

Procurement process

- 3.1 Today we are launching a tender for 527 duty provider contracts. Full details can be found at <https://www.gov.uk/government/publications/legal-aid-crime-tender-2015>. The indicative timetable is as follows:
- 29 January 2015 – tender closes
 - w/c 12 June 2015 – notification of tender outcomes
 - July 2015 – subject to further consideration, second fee cut implemented
 - 1 October 2015 – service commencement
- 3.2 One criterion which will be applied to the Duty Provider Crime contract tender is the requirement for applicants to have an office in each procurement area in which they are bidding. However, in those Criminal Justice System areas we have split to create two procurement areas and especially with regard to London (split into 32 procurement areas), this requirement would be overly burdensome on applicants. Therefore, in order to allow greater flexibility for those wishing to deliver services across split procurement areas and/or London, we are relaxing this criterion. Applicants will only need to have one office in either one of the split procurement areas in order to access the other half. With regard to London this would mean that an office in one London procurement area, would grant an applicant access to all immediately adjacent London procurement areas.

Travel Payments

- 3.3 In the February response to consultation we decided that travel time would be bundled into fixed fees. We also said that 1.5 hours travel time was the maximum that people would need travel – which we also said was reasonable. However, separately from the consultation we have seen evidence that travel times will exceed 1.5 hours in some instances. Therefore, in order to support providers who may exceptionally be required to travel long distances, we have decided to pay separately for travel time in excess of 1.5 hours (subject to such costs being reasonably incurred as provided for in the 2015 Duty Provider Crime Contract). This is likely to be of particular benefit to those organisations wishing to deliver services in rural areas.

Fee reduction

- 3.4 In February, we announced in the Government Response, the decision to implement the 17.5% reduction in fees for advice, litigation and magistrates' court advocacy services (contracted work) in two phases, an interim fee reduction of 8.75% in March 2014 followed by a further reduction introduced in June alongside the implementation of the new 2015 Crime Contracts via a number of changes to the fee schemes for this work. The interim fee reduction was implemented through secondary legislation on 20 March 2014.
- 3.5 The first phase of the procurement process to award new 2015 Crime Contracts commenced in April 2014 and the LAA awarded Own Client Work contracts to just over 1,800 providers. However, in light of the judicial review challenge against the

Next Steps consultation process and the consequential further consultation, we delayed the start of the next phase of the procurement process (Duty Provider Work) and consequently the contracts (both DPW and OCW contracts) will now not commence until October 2015.

- 3.6 Despite the delay to the procurement process, the financial challenge faced by the Department, like many Departments across Government, has not diminished. Therefore, we have taken the decision to proceed with the planned implementation of the second reduction in fees in July 2015, subject in particular to the further consideration announced on 27 March 2014:

“The Government will... take into account the outcomes of the reviews by Sir Bill Jeffrey and Sir Brian Leveson, as well as any impact on legal aid spend from falling crime rates, and earlier remuneration changes... before introducing the second fee reduction for litigators.”³

- 3.7 This approach will create a three month gap between the implementation of the fee reduction and the start of the new 2015 Crime Contracts and so depart from the approach announced in February. Assessing the likely impact of such an approach on providers, suggests that this gap would not be expected to pose a threat to service provision. This is because a number of factors help to reduce the impact of this headline reduction in fees.
- 3.8 The second fee reduction will only apply to new cases. Much of the value of work that providers bill for during this three month gap will have started before July 2015 and will therefore be under previous, higher fee schemes. Consequently, as it takes time for new cases to complete and be billed for, it follows that providers will not be immediately operating with all of their fees at 17.5% lower levels for this period.
- 3.9 Interim payments also reduce the impact of fee reductions on providers in the short term by improving cash-flow. Following our agreement with the Law Society in March to bring forward the implementation of interim payments for litigators in Crown Court cases (which was originally planned for next summer but was implemented on 2 October) providers are already able to benefit from improved cash-flow. This will have a substantial positive effect on provider revenues in the period from July to October 2015.
- 3.10 Using 2013-14 billing data, we have made an assessment of how the mix of cases on different fee schemes, combined with interim payments, impacts the level of fee reduction that providers face during the 2014-15 financial year until the October 2015 service commencement date. We acknowledge that providers will all be affected differently by interim payments and this will be largely dependent on the amount of Crown Court work a provider does. Indicative analysis suggests that the average firm will be subject to an overall reduction in the legal aid fee income⁴ they receive of, on average, approximately 5% during the period April 2015 to October

³ https://consult.justice.gov.uk/digital-communications/transforming-legal-aid-next-steps/consult_view

⁴ Criminal legal aid fee income from Police station, magistrates' court and litigation in the Crown Court

2015 when compared with fee income prior to the first and second⁵ fee reductions (i.e. fee income prior to 20 March 2014).

- 3.11 The current 2010 Standard Crime Contracts will be extended to ensure continuous service coverage up to the start of the new 2015 Crime Contracts. The LAA will issue notices of extension to all 2010 Standard Crime Contract holders in due course.

⁵ Assuming the second fee reduction is the maximum 8.75%.

Consultation principles

The principles that Government departments and other public bodies should adopt for engaging stakeholders when developing policy and legislation are set out in the consultation principles.

<http://www.cabinetoffice.gov.uk/sites/default/files/resources/Consultation-Principles.pdf>

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