



cutting through complexity

Review of information received in response to the latest consultation on Duty Provider Work contracts

13 November 2014



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13 November 2014

Dear Sirs

The Provision of Consultancy Services for review of information received in response to the latest consultation on Duty Provider Work contracts

In accordance with our contract and its attachments dated 13 November 2014, we enclose our report on the response to your latest consultation on Duty Provider Work contracts. This final written report supersedes all previous oral, draft or interim advice, reports and presentations, and no reliance should be placed by you on any such oral, draft or interim advice, reports or presentations other than at your own risk. Our contract sets out the agreed scope of our work, which is included on page 2. You should note that our findings do not constitute recommendations to you as to whether or not you should proceed with any particular course of action. The Important notice included on this page should be read in conjunction with this letter.

Our report is for the benefit and information of the Ministry of Justice only. The scope of our work for this report has been agreed by the Ministry of Justice and to the fullest extent permitted by law, we will not accept responsibility or liability to any other party (including the Ministry of Justice's legal and other professional advisers) in respect of our work or the report.

Yours faithfully,

KPMG LLP

Important notice

Our work commenced on 4 November 2014 and fieldwork has continued to 10 November 2014. We have not undertaken to update our report for events or circumstances arising after that date.

This report makes a number of references to our report "Procurement of Criminal Legal Aid Services: Financial Modelling" (our "Original Report") dated 11 March 2014. We draw your attention to the important notice which was included on page 1 of our Original Report.

In preparing this Report, in addition to our Original Report dated 11 March 2014, our primary sources have been the responses to the consultation provided to us by the Ministry of Justice and representations made to us by management of the Ministry of Justice ("the Client"). We do not accept responsibility for such information which remains the responsibility of Ministry of Justice management. Details of our principal information sources are set out throughout and we have satisfied ourselves, so far as possible, that the information presented in our report is consistent with other information which was made available to us in the course of our work in accordance with the terms of our contract and scope as agreed with you. We have not, however, sought to establish the reliability of the sources by reference to other evidence.

We accept no responsibility or liability for the findings or reports of legal and other professional advisers even though we may have referred to their findings and/or reports in our Report.

This Report has not been designed to be of benefit to anyone except the Client, even though we have been aware that others might read this Report. We have prepared this report for the benefit of the Client alone.

This Report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the Client) for any purpose or in any context. Any party other than the Client that obtains access to this Report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Beneficiary's Publication Scheme or otherwise) and chooses to rely on this Report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this Report to any party other than the Client.

In particular, and without limiting the general statement above, since we have prepared this Report for the benefit of the Client alone, this Report has not been prepared for the benefit of any other Government Department or Non-departmental Public Body nor for any other person or organisation who might have an interest in the matters discussed in this Report, including for example Ministry of Justice employees, the Trade Unions, customers of the Ministry of Justice, those who provide goods or services to the Ministry of Justice, providers of legal aid services or the Law Society.

Scope of work and information received

Objective

Following the outcome of the Judicial Review brought by the Criminal Law Solicitors Association and the London Criminal Courts Solicitors Association, the Ministry of Justice ran a further consultation exercise seeking views on the two expert reports (KPMG and Otterburn) and their use to inform the Secretary of State's decision on the number of Duty Provider Work contracts to award.

Scope of work:

You have asked us to undertake the scope of work below:

1. Consultation review

- Read consultation response material which MoJ will provide (around 300 pages)
- Identify evidence contained within the documentation that relates to the assumptions used to underpin the model
- Compare the evidence to what KPMG saw or heard previously and consider the extent to which changes the view of the assumptions

2. Consultation workshops

- Attend one or two workshops with MoJ and LAA to discuss KPMG's observations

3. Report findings from consultation review

- Document differences between the evidence used for KPMG's Original Report and the evidence provided to the recent consultation
- Provide a statement which describes, having reviewed the consultation documentation provided, the extent to which KPMG's Original Report should be updated

Other considerations and clarifications

The scope of work described above does not include further analysis or re-running of the models used in the original analysis.

Information received

Party/Respondent	Document
Ministry of Justice	Consultation Paper
London Criminal Court Solicitors Association (LCCSA)	Consultation response and summary analysis of responses received via LCCSA Response Hub
Criminal Law Solicitors Association (CLSA)	Consultation response
The Law Society (TLS)	Consultation response
Legal Aid Practitioners' Group, (LAPG)	Consultation response
The Bar Council	Consultation response
The Criminal Bar Association (CBA)	Consultation response
Otterburn Consulting	Consultation response
The Law Society (TLS)	Email
The Law Society (TLS)	Letter regarding latent capacity
Ministry of Justice	Summary of key points raised by respondents

Clarification of the basis of our Original Report

The focus of our Original Report was to inform MoJ as it considers the following question:

For each procurement area, how many contracts should be let in order to create a sustainable market at the reduced rates?

On page 8 of our Original Report we identified the trade-off between financial viability and sufficient capacity and competition. This means that there is not a single answer for each area. Instead a range is proposed within which MoJ must make a judgement around the balance between these competing aims.

We developed a bespoke methodology, in conjunction with MoJ, based on the data available. This is outlined on pages 27 to 36 of our Original Report. The methodology requires a number of assumptions to be made to illustrate the potential impact of letting alternative numbers of contracts.

- To the extent data was available to support the use of an assumption, even where such evidence was scarce, we sought to identify the extent to which the assumptions made were consistent with the sources made available to us
- Where no relevant evidence existed, the methodology shows the implied assumptions which would need to apply within a scenario in which a given number of contracts are let

In order to enable MoJ to consider in as quantitative a manner as possible the potential impact of each strategy, the model illustrates each market as if the changes to contracting had been implemented and the contracts were being let for the first time. By comparing with the current situation, the extent to which the market would need to change can be seen.

For example, the market participants in such a scenario who do not currently have sufficient capacity would face a range of choices comprising:

- Restricting themselves to an Own Client only contract
- Reallocating resources from Own Client work to support duty contracts
- Expanding capacity through recruitment
- Use of under-utilised capacity or staff currently specialising in non-crime law
- Consolidating with other firms

The extent to which firms would adopt one or more of the strategies are, in effect, decision variables rather than professional judgments as to the likelihood or otherwise of the strategies being employed.

To understand the degree of challenge faced in each procurement area in a comparable way, it is necessary to fix a number of the decision variables and allow two to move (within thresholds), namely the degree of market consolidation and average staff efficiency

We did not seek to provide a judgement around the likelihood or willingness of parties to adopt a particular course of action. On page 55 of our Original Report we highlighted that the strategy for achieving capacity growth will differ on a firm by firm basis and will ultimately be a business decision that reflects each firm's circumstances and profitability requirements.

It is recognised that market participants may have found themselves commenting upon market changes which they would not wish to be imposed, while also planning contingent strategies to pursue should the changes be implemented. It is important to distinguish between the current preferences of firms, pre-change, and the potential future strategies they may adopt, post-change.

On pages 56 to 59 in our Original Report we highlighted other considerations which MoJ should consider. In this review, we have not commented on those consultation responses which repeat matters which were already noted in our Original Report, unless there are sources of evidence identified which were not previously available.

Respondents' comments on assumptions used within the model

Proportion of Own Client capacity considered available for Duty Work – 50%

The assumption on the degree to which firms would reallocate resources from own client work was based on the rationale that providers may view duty contract revenues as more stable than Own Client. Consultation responses disagreed with this view. However, all responses were based on opinion and assertion. No evidence of what will actually happen will be available until contracts are let.

This decision variable was highlighted in our Original Report, on page 55, where we noted that “firms may be reluctant to redeploy staff from own client work and may therefore prioritise other options”. *Therefore, we do not consider it necessary to update our Original Report.*

Capacity growth achievable through use of latent capacity – 15%

This was another decision variable on potential options to meet capacity shortfall. The value used had a degree of evidence to support it given that volumes had declined between 2007/8 and 2012/3, but firms were understood to have not yet right-sized and would therefore currently be employing under-utilised staff.

Some respondents misinterpreted this as requiring productivity improvements from staff. Instead, this evidence was used in our Original Report (page 35) to indicate that, within existing processes, individuals had the capacity to take on more work.

Other respondents have claimed that staff are currently fully utilised, but no evidence/data points to demonstrate capacity/utilisation have been provided.

In the absence of evidence for an alternative value for this decision variable we do not consider it necessary to update our Original Report.

Capacity growth achievable through recruitment (organic growth) – 20%

This was a decision variable. Respondents' main concern appears to be around cost to recruit and train new staff, in the absence of investment funding. The challenge around funding is discussed in our Original Report on page 57. *As this challenge was discussed in our Original Report we do not consider it necessary to update it.*

Definition of viability – breakeven assumption

Otterburn's report showed that firms are currently achieving profit levels between a loss of 19% and a profit of 20%, with an average profit level of 5%. For the purpose of modelling, breakeven was adopted as the minimum level for sustainable trading. This was on the basis that Otterburn made provision for a notional salary for equity partners and that therefore all operating costs, including an income for equity partners, are met if breakeven is achieved.

During our discussions with MoJ, it was recognised that this minimum profit level was not the level which firms would aim to achieve, and on pages 57 and 58 of our Original Report we highlighted factors not allowed for in the breakeven assumption including:

- Funding of increases in working capital;
- Investment required to achieve growth, staff efficiency savings and consolidation; and
- Adequately rewarding equity partners for the risk they take and for the capital they employ.

A number of respondents have questioned the use of breakeven. Respondents appear to interpret the 5% average profitability quoted by Otterburn as a minimum acceptable profit level. No other figure is proposed in the responses.

Were the 5% level to be applied within the model this would have the effect of increasing the average staff efficiency requirement by the amount required to achieve the higher profit level.

The modelling describes the degree of staff efficiency required in each area to achieve breakeven. There is an opportunity to achieve a greater level of profitability if further efficiencies were achieved.

On the basis that the risks highlighted by respondents with regard to breakeven are already set out in our Original Report, we do not consider it necessary to update it.

Respondents' comments on assumptions used within the model

Volumes of work – remain constant

The level of demand within each market was assumed to remain constant at the levels experienced in the 12 months to September 2013 (based on the MoJ/LAA dataset referred to on pages 15 and 16 of our Original Report). After consideration of the evidence, MoJ concluded that this was a reasonable forecast of demand.

Respondents have challenged this assumption and highlight that volumes in aggregate have continued to decline beyond the end of September 2013. The sources cited are “Legal Aid Statistics in England and Wales, 2013/4” and “Legal Aid Statistics in England and Wales, April to June 2014”.

We note that it is possible that the trend in aggregate information may not apply to Duty Work, nor in all procurement areas. We also note that the rate of decline has reduced when compared with the previous periods.

Having reviewed the consultation documentation provided, we recommend that further consideration should be given to the demand forecast used as the basis for the scenarios. With the benefit of additional data, MoJ may wish to consider whether a forecast which predicts constant levels of spend on Duty Work is reasonable for all procurement areas.

Other assumptions you raised in your consultation paper

MoJ also sought responses on a number of other modelling parameters including:

- The necessary number of bidders to ensure competitive tension
- The number of incumbents of scale initial threshold
- The market consolidation initial threshold
- The staff efficiency initial threshold

One respondent questioned the achievability of the threshold level of staff cost reductions, but did not present any evidence to support the point. No alternative value was proposed.

In the absence of evidence for an alternative value for this decision variable we do not consider it necessary to update our Original Report.

There were no other responses commenting on the other parameters.

A number of respondents raised the risk that unsuccessful bidders would not be able to continue trading long enough to participate in subsequent competition rounds and that there was therefore a risk to sustainability. *This risk was identified on page 58 of our Original Report and therefore we do not consider it necessary to amend it.*



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