

To:	Legal Services Board	
Date of Meeting:	14 July 2016	Item: Paper (16) 47

Title:	The emerging market in authorisation: update for discussion	
Workstream(s):	Performance, evaluation and oversight	
Author / Introduced by:	Kate Webb, Head of Regulatory Reviews and Investigations kate.webb@legalservicesboard.org.uk / 020 7271 Ext. 0090	
Status:	Official	

Summary:

In January 2016 the Board discussed a paper that explored the increasing opportunities for legal services providers to choose their regulator. The Board discussed the risks arising from this “market in authorisation” for consumers, providers, regulators and the LSB.

This paper provides the Board with an update on relevant developments for discussion. In January we remarked on the relatively lower profile of consumers’ interests in the public discussions around switching and choosing. Since then, the Legal Services Consumer Panel has called on regulators to work together to avoid creating consumer detriment as they help firms to switch. This is in response to developments in regulatory approaches to professional indemnity insurance cover, in particular run-off cover obligations. The paper also notes where we anticipate new options for authorisation to emerge in the medium term, and the possible Justice Select Committee’s interest in the topic.

The 2016/17 Business Plan outlines specific work in this area to reflect on the risks to consumers from the changing shape of legal services regulation. Early scoping work suggests this should focus on the main points of difference between regulators, and any risks to consumer and public interest associated with providers switching.

This paper is not seeking a decision in relation to any rule change.

Recommendation(s):

The Board is invited to note and discuss the issues described in paragraph 16.

Risks and mitigations

Financial:	N/A
Legal:	The paper is for discussion and no decision is required. No specific legal risks in the paper.
Reputational:	There is a risk that the LSB’s role and responsibility to oversee the approved regulators may be misinterpreted, damaging the

	LSB's reputation. This can be mitigated through clear and consistent communications about the extent of the LSB's statutory responsibilities and powers to act.
Resource:	A project has been identified on this topic in the 2016/17 Business Plan.

Consultation	Yes	No	Who / why?
Board Members:		x	Early thinking by the executive
Consumer Panel:		x	As above
Others:			

Freedom of Information Act 2000 (Fol)		
Para ref	Fol exemption and summary	Expires
Para 16 – first, third and fourth bullet points	Section 36: free and frank exchange of views. This is presenting early thinking to the Board.	N/A

LEGAL SERVICES BOARD

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The emerging market in authorisation: update for discussion

Recommendation

1. At its January 2016 meeting the Board discussed a paper on the emerging market in authorisation in legal services.
2. This paper provides an update on developments since January and discusses forthcoming LSB project work in this area. The Board is invited to note and discuss the issues described below in paragraph 16.

Background

3. In January 2016 the Board discussed a paper on the emerging market for authorisation in legal services. This reflected that there are now wider opportunities for legal service providers to choose and switch between regulators, and greater competition between regulators as a result. The paper identified some of the risks and benefits that may emerge from these developments for consumers, providers, regulators and the LSB. The Board asked for further discussion on this topic at this meeting.
4. The Legal Services Act 2007 enabled growth in the range of regulatory options for providers of reserved legal activities. It introduced alternative business structures, and permitted the designation of new approved regulators, and for existing regulators to extend the range of activities they authorise. Consequently, when compared to January 2010 today we have more approved regulators, who themselves are regulating a wider range of business models and a broader range of activities, and we expect further growth in the future (see Annex A, updated from January 2016 paper).
5. Over the last twelve months, we have observed that more legal services providers have begun to take advantage of the opportunity to choose their regulator. Reasons cited by providers in support of particular choices include easier authorisation processes, more proportionate regulatory arrangements, easier insurance arrangements and better value for money. Regulators have also indicated their interest in competing for providers' business (see Annex B, updated from January 2016 paper).
6. The opportunity to choose and switch between regulators is based on variation in regulatory approaches. We know there is not a consistent set of processes across the regulators. Indeed, proportionate and targeted regulation should allow

some space for variation in how things are regulated. We would become concerned if these differences could lead to outcomes that had an adverse impact on consumers, for example through tolerance of poor provider performance or lower standards.

7. In January's paper we noted that the needs and interests of providers and regulators seemed to be reflected most in this debate, and that there had been little discussion about the interests of consumers. The Board discussion mirrored the paper's concern and indicated that any future work on this topic should focus on emerging risks to consumers from growth in switching. The Board also asked to revisit this topic after six months.

Recent developments

8. Policy and regulatory developments since the Board's previous discussion are centred on two topics. The Legal Services Consumer Panel have also commented on this area.

Run-off cover obligations

9. The need to secure run-off cover was highlighted as a barrier to firms' mobility and exit from regulation in 2013 research completed for the LSB.¹ CILEx Regulation also brought this issue to the LSB's attention with a report in December 2015. A firm which wanted to switch between regulators would be required to obtain six years run off cover to secure its "exit" from its original regulator. This cost could be prohibitive and effectively prevent firms switching.
10. Recent developments on run-off cover include:
 - The SRA has consulted on plans to reform its approach to run-off cover for those firms looking to continue to provide legal services under a different AR.² It is proposing to make a variation to the terms of its Participating Insurer's Agreement (PIA) to allow the run-off cover requirement not to be activated where the firm is moving to another AR.
 - The CLC has secured amendments to its PII minimum terms and conditions. In practice this means that the cost of future run-off is taken into account when determining premiums provided, without additional cost to the practice when the business ceases through closure or when moving to another regulator.

¹ *Understanding Barriers to Entry, Exit and Changes to the Structure of Regulated Law Firms*. 2013. Available at: <https://research.legalservicesboard.org.uk/reports/investigating-regulation/understanding-barriers-to-entry-exit-and-changes-to-the-structure-of-regulated-law-firms/> (accessed 4 July 2016)

² See: <http://www.sra.org.uk/sra/consultations/removing-barriers-switching-regulators.page> (accessed 4 July 2016)

Authorisation options for providers

11. The previous Board paper described the expansion seen in the range of activities and persons that can be authorised by the ARs since the Legal Services Act. Since January, developments in this area include:
 - The LSB has recommended to the Lord Chancellor that the Bar Council becomes a licensing authority, operated by the Bar Standards Board
 - CILEx Regulation are intending to submit an application seeking designation as a licensing authority
 - ICAEW have issued a public consultation on its plans to expand the range of reserved legal activities it is designated to authorise
 - The SRA has begun to authorise firms under its revised authorisation rules and grant authorisation to firms without an obligation to carry on reserved legal activities.³ For example, it was recently reported that a will-writing firm had chosen to be authorised by the SRA.⁴
12. The legal services press continue to report providers seeking authorisation with “non-traditional” regulators, such as solicitors’ firms gaining authorisation through the Bar Standards Board. As previously noted, the rationale for these choices usually reflects a view that the regulatory approach is cheaper, more proportionate or “lighter-touch”.⁵ The number of such applications does however still seem to be very low.

Consumer perspective

13. We noted previously that the consumer perspective was lacking in debates and comments around the market for authorisation. It is therefore welcome to note the Legal Services Consumer Panel has recently commented. In response to the CLC consultation on reform of run-off cover it commented on the risks it sees emerging from providers’ switching between regulators, urging ARs to work together to avoid damaging consumers’ interests:

“Approved Regulators must work together to ensure that gaps or loopholes do not result in consumer detriment or lack of clarity. In 2013, the Panel highlighted

³ Legal Services Board. 2016. Decision notice. Available at: http://www.legalservicesboard.org.uk/Projects/statutory_decision_making/pdf/2016/20160128_SRA_Reserved_Activities_Decision_Notice.pdf (accessed 4 July 2016)

⁴ Cross M. 2016. Will-writing firm signs up with SRA. *The Law Gazette*. Available at: <http://www.lawgazette.co.uk/practice/will-writing-firm-signs-up-with-sra/505552.article> (accessed 4 July 2016)

⁵ Smith C. 2016. Sports solicitor signs up for bar regulation. *The Law Gazette*. Available at: <http://www.lawgazette.co.uk/practice/sports-solicitor-signs-up-for-bar-regulation/5054165.article> (accessed 4 July 2016)

Smith C. 2016. Solicitor slashes insurance costs through bar regulation. *The Law Gazette*. Available at: <http://www.lawgazette.co.uk/practice/solicitor-slashes-insurance-costs-through-bar-regulation/5056191.article> (accessed 4 July 2016)

inconsistency across the legal services landscape as an issue that needed to be addressed. Shopping around for a regulator is likely to exacerbate this issue. ⁶

Justice Select Committee

14. This topic was raised in a recent Justice Select Committee evidence session on legal services regulation. Annex B includes a full extract of the exchange. The witnesses – from the SRA, BSB, Bar Council and Law Society – were asked whether they were comfortable with the idea that authorised persons can shop and choose which regulator they think best fits their business.
15. The Director of the BSB reported that it authorised nine entities run by solicitors (either individually or in partnership with barristers), indicating that this was currently a “small-scale shift-around”. While alert to potential for “forum shopping”, regulators assess relevant evidence through authorisation processes. To date no complaints had been raised with these bodies with respect to “persons who may have been shopping around”.

Issues and risks

16. While greater choice and switching for providers could lead to more efficient and effective regulation of legal services, the January Board paper discussed a number of risks and issues in relation to this topic. These included:
 - [REDACTED]
 - apparent lack of consideration of interests of public and consumers in these debates when compared to interests of the regulator and the regulated communities
 - [REDACTED]
 - [REDACTED]
17. In our assessment these remain key issues emerging from these developments in legal services regulation. While the extent of switching and choosing may be felt to be relatively small-scale at present, the comments and interest shown by the Panel and the Justice Committee suggests that the potential impact on consumers may require some further assurance.

⁶ Legal Services Consumer Panel. 2016. Response to CLC consultation on professional indemnity insurance. Available at: http://www.legalservicesconsumerpanel.org.uk/publications/consultation_responses/documents/2016-05-20CLCconsultationonPII.pdf (accessed 4 July 2016)

Future LSB work

18. The 2016/17 LSB business plan outlined a piece of work to examine the benefits and risks associated with these developments and the changing shape of legal services regulation. We have begun some early scoping work. It is expected that this project will consider the main differences between regulators, such as in entry, compliance activities, and exit from the regulated market. It will also consider the differences that may drive mobility between regulators and the processes that govern mobility, such as authorisation checks. We will assess the risks to consumers that may arise from these sources of variation, and how they may be managed.
19. One reason for undertaking this project is to support the ongoing development of our risk-based assessment of regulatory performance. It will help us to identify any unintended consequences of the proliferation of authorisation options, and if necessary, areas for further and more detailed review. For example, what information do “receiving” ARs take into account about the regulatory performance and history of applicant firms and individuals? Is there appropriate information and intelligence sharing between regulators at this stage? How is this information processed and used to inform decisions?

Summary and next steps

20. The pace of regulatory reform across the ARs demonstrates that this remains a live issue. The LSB’s project work will allow us to explore systematically the areas of greatest risk to consumers’ interests. We recommend that the Board revisit this topic under the auspices of the project work with a further paper and discussion in circa six months’ time.

04.07.2016

Extent of legal services regulation: 2010 vs current

The provisions when the Legal Services Act 2007 came into force (2010) versus current opportunities to authorise (shaded).

Regulator	Reserved legal activity	Individual	Entities	LA
BSB	The exercise of right of audience The conduct of litigation Reserved instrument activities Probate activities The administration of oaths	Yes	Yes	LSB recommendation sent to Lord Chancellor
CILEx Regulation	The exercise of right of audience The administration of oaths	Yes	Yes	<i>No (application anticipated)</i>
	The conduct of litigation Reserved instrument activities Probate activities			
CLC	Reserved instrument activities Probate activities The administration of oaths	Yes	Yes	Yes
CLSB	The exercise of right of audience The conduct of litigation The administration of oaths	Yes	No	No

Regulator	Reserved legal activity	Individual	Entities	LA
ICAEW	Probate activities	Yes – but only within an entity	No	Yes
	<i>application anticipated - other reserved legal activities</i>			
IPReg	The exercise of right of audience The conduct of litigation Reserved instrument activities The administration of oaths	Yes	Yes	Yes
MoF	Reserved instrument activities Probate activities Notarial activities The administration of oaths	Yes	No	No
SRA	The exercise of right of audience The conduct of litigation Reserved instrument activities Probate activities The administration of oaths	Yes	Yes	Yes

Public commentary by regulators

Bar Standards Board:

Sir Andrew Burns, Chair, Bar Standards Board, Speech, 5 October 2015⁷

“I am intrigued that our regulatory regime has been seen as so appealing that we even have a couple of solicitor-led practice switching to the BSB as their preferred regulator, due to the value for money we provide and reduced red tape.”

Patricia Robertson QC, Vice Chair, Bar Standards Board, Speech to Lincoln’s Inn Bar Students, 9 July 2015⁸

“... the boundaries have blurred, in terms of the spheres of activity of solicitors and barristers, the business models it is open to them to adopt, and how and by whom they are regulated.... if over the medium and longer term we are talking about a shrinking rather than growing number of individuals who are regularly providing advocacy services in the higher courts, then on any view we should do all we can to bring ‘into the tent’ those solicitor advocates who are doing the same work we do, who want to be regulated by the BSB and who want to mark themselves and their firms out as adhering to the higher standards of training we consider necessary. How people originally acquired their professional title should, in future, be less important than the job they are actually doing and their willingness to fully commit to the same standards as ourselves.”

Council for Licensed Conveyancers

Dame Janet Paraskeva, Chair, Council for Licensed Conveyancers, Speech to Society of Licensed Conveyancers, 18 November 2015⁹

“A diversity of approaches offers choice to the regulated community too. Choice of the model that is best aligned to their practice.... Ensuring that practices can in fact make their choice of regulator as Parliament envisaged. But there are some practical obstacles to that still – including the supposed need for run-off cover and interruption of access to lenders panels.”

⁷ Available at: <https://www.barstandardsboard.org.uk/media-centre/speeches/bsb-chair-sir-andrew-burns-sets-his-vision-for-the-future-of-the-bar-regulator/> (accessed 4 July 2016)

⁸ Available at: <https://www.barstandardsboard.org.uk/media-centre/speeches/future-proofing-the-bar-lecture/> (Accessed 4 July 2016)

⁹ Available at: <http://www.clc-uk.org/CLCSite/media/Corporate-Docs/SLC-Conference-2015-Janet-Paraskeva-Speech-for-publication.pdf> (Accessed 4 July 2016)

ILEx Professional Standards (now CILEx Regulation)

Alan Kershaw, Chair, ILEx Professional Standards, 15 January 2015¹⁰, discussing the opening of its entity regulation scheme:

“This presents a great opportunity for many new and existing firms, who have a real choice of regulator for the first time. We are very clear about what that choice means. It does not mean a chance to escape scrutiny, or a decline in regulatory standards – it means a regulatory model that is best for your business, giving consumers the protection they need when seeking legal services. It also means that, if they want it, students starting out on the CILEx route are not limited in their career destinations, and can go on to be authorised to provide reserved legal services in one or more branches of the law either running their own practice, or as an employed lawyer.”

CILEx Regulation has devoted a section of its website to supporting existing regulated firms with move to CILEx Regulation, with scenarios and FAQs.¹¹ For example:

“Scenario 2: Jayne Lau is a solicitor working on her own as J Lau Limited carrying out civil litigation regulated by the SRA. She will remain a solicitor, regulated by the SRA individually, but seeks entity regulation from CILEx Regulation. She will demonstrate the knowledge and skills she has gained as part of the application process but will not need to obtain a litigation qualification from us. She will describe herself as a solicitor to her clients but be authorised by CILEx Regulation for civil litigation.”

¹⁰ Available at: <http://www.lawgazette.co.uk/practice/legal-execs-regulator-sets-sights-on-solicitor-firms/5046051.fullarticle> (accessed 4 July 2016)

¹¹ Available at: <http://www.cilexregulation.org.uk/entity-regulation/applying-to-be-regulated/application-procedure/scenarios> and <http://www.cilexregulation.org.uk/entities/opportunities/faqs/existing-regulated-firms> (accessed 4 July 2016)

28 June 2016

Q22 Alberto Costa: ...I turn the panel's attention to regulator shopping. One of the purposes of the 2007 Act is to give the opportunity to authorised persons to decide which authorised regulator should regulate their particular business. As Mr Philip said, there are nine approved regulators that sit under the LSB at present. My first question is for the two regulators before us. Are you comfortable with the idea that authorised persons can shop and choose which regulator they think best fits their business?

Dr Davies [Director, Bar Standards Board]: You are looking at me, so I will start. Almost inevitably, the Act set up the possibility of what one might see as competition between regulators—that people would be able to move between them. That was presumably a deliberate bid to shake up the market and to stimulate different forms of provision among different legal services professionals.

We are cautious. We currently authorise six entities run by an individual solicitor, one two-solicitor entity and two entities that have one solicitor and one barrister at the helm. The SRA probably authorises 76 entities in which at least one barrister holds a manager position. It is still a very small-scale shift-around. We would be concerned if we thought that a barrister was deliberately forum shopping in order to try to escape duties that we see as integral to a barrister's work. Of course, the Act puts us in the position that, where there is an entity and an individual regulator, it is the entity regulatory rules that prevail. We are cautious and we take a risk-based approach. We look at the evidence before us when dealing with whatever is before us. To date, we have not had any complaints in respect of the behaviour of persons who may have been shopping around.

Paul Philip [Chief Executive, Solicitors Regulation Authority]: I said earlier that we regulate about 86% of all lawyers in England and Wales. About 50% of all practising barristers work within solicitors' firms. I would hazard a guess that a very large percentage of paralegals and licensed conveyancers work within solicitors' firms. Your proposition, I think, is that nine legal regulators seems like a bit much. It certainly leads to competition between regulators and the possibility of people hopping from one to the other, and we have seen a few examples of that, particularly between us and the Council for Licensed Conveyancers.

Do we think it is a good thing? As I said in my introductory statement, we are very much on a journey in terms of legal services regulation. The fact is that many people have criticised legal regulators for being over-bureaucratic and having too many rules. I certainly agree with that criticism. Competition between legal regulators creates a thought process whereby legal regulators have to think about whether their model is correct. Do I think that in the fullness of time there should be nine legal regulators? No, I do not. Consolidation is a foregone conclusion, but right now the system has worked in the public interest and it is a good thing.

¹² Justice Select Committee. 28 June 2016. Oral Evidence – Legal Services Regulation. Available at: <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/justice-committee/legal-services-regulation/oral/34707.html> (accessed 4 July 2016)