To:	Legal Services Board		
Date of Meeting:	21 January 2016	**Item:**	Paper (16) 03

Title:	The Solicitors Regulation Authority application seeking approval of changes to its regulatory arrangements: SRA Amendments to Regulatory Arrangements SRA Authorisation Rules for Legal Services Bodies and Licensable Bodies 2011 (SRA Authorisation Rules 2011)].
Workstream(s):	Statutory Decisions
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Status:	Official

Summary:

Allowing licensed bodies not carrying out reserved legal activities to continue to be authorised by the SRA

The purpose of this paper is to seek a decision from the Board for **approval of a change to the SRA regulatory arrangements.** The Board's approval is needed as the specific change was the subject of a warning notice under Schedule 4 of the Act which indicated that we were considering refusing to approve the change.

The change is to the SRA Authorisation Rules and **removes the need for a licensable body to include a statement in its application for authorisation about those reserved legal activities for which the body seeks authorisation.** It will also **remove the SRA's power to revoke or suspend a body's authorisation where it is satisfied that the body has no intention of carrying on the legal activities for which it has been authorised.**

The purpose of the changes, as set out in the SRA's application, is so that firms authorised by the SRA to carry on reserved activities can retain their authorisation (if they are considered suitable to deliver reserved legal activities) even if they choose not to do so at any particular point in time.

The LSB, in issuing the warning notice, had the following key concerns about approving changes which have the effect of allowing firms, by choice, to seek authorisation when they do not need to be authorised:

- Whether this would be a proper exercise of regulatory functions
- Whether the effect of the proposals would be to introduce a form of accreditation, rather than authorisation
- Whether the changes would have a potentially detrimental impact on consumers and the public interest.

The LSB's further assessment in considering these concerns is that, for the reasons set out in this paper and in the draft Decision Notice, the proposed changes do not satisfy any of the refusal criteria in Schedule 4 of the Act (which is the only basis upon which the LSB can refuse the changes) and the Executive therefore recommends to the Board that the changes to the regulatory arrangements proposed by the SRA should be granted.

Recommendation(s):
The Board is invited: (1) to agree that the part of the application from the SRA relating to alterations to the regulatory arrangements in respect of reserved activities be approved. (2) to note the draft decision notice set out in **Annex A** and to delegate the finalising of the wording of the decision notice to the Chairman and Chief Executive.

Risks and mitigations	
Financial:	None
Legal:	[redacted]
Reputational:	As a consequence of this change, the SRA may be perceived to be extending its regulation to firms that would not normally be regulated. By allowing this, the LSB may be seen to be allowing the extension of regulation rather than deregulating. The LSB is not extending regulation. Regulation will only apply through the choice of the legal services provider. Moreover, our legal advice is that this rule change is within our powers and that it is a matter for the board's discretion to consider whether these changes are consistent with the Regulatory Objectives and are in the public interest. Firms seeking authorisation in these circumstances would be doing so as a matter of commercial choice. It would be incorrect to characterise this change as the SRA extending its regulation, or increasing regulatory burden.
Resource:	None

Consultation	**Yes**	**No**	**Who / why?**

Board Members:	√		Anneliese Day and Marina Gibbs have provided input as the application has progressed.
Consumer Panel:		√	
Others:	The LSB does not conduct a public consultation process on any rules change application it receives. However, when we published the SRA's application, the Law Society made a representation. The LSB invited the SRA to respond to the submission but it chose not to do so.		

Freedom of Information Act 2000 (FoI)		
Para ref	**FoI exemption and summary**	**Expires**
Risks and mitigations: Legal; Para's 11-14; Annex B	Section 42: information protected by legal professional privilege	
Annex A	Section 22 – this is the draft version of the document. The final version is intended for future publication which may include some minor changes depending on the outcome from the Board meeting.	

LEGAL SERVICES BOARD

To:	Legal Services Board		
Date of Meeting:	21 January 2015	**Item:**	Paper (16) 03

Solicitors Regulation Authority's (SRA) application seeking approval to changes to regulatory arrangements: SRA Amendments to Regulatory Arrangements SRA Authorisation Rules for Legal Services Bodies and Licensable Bodies 2011 (SRA Authorisation Rules 2011).

Background / context

1. On 29 October 2015, the LSB approved, in part, an application from the SRA to alter its regulatory arrangements. The application, titled 'Regulatory Reform Programme', covered a range of proposed changes, most of which the LSB approved and which were listed in the LSB's Decision Notice of 29 October[1]. The LSB recorded in the notice that it welcomed the overall intentions of the SRA Regulatory Reform Programme and supported the SRA's drive to remove unnecessary regulatory barriers and restrictions (which can inhibit economic growth in the sector) while at the same time making its regulatory framework targeted and proportionate.

2. We did not, however, approve at that time the part of the application referred to in the application as 'reserved activities changes' and which comprised the following alterations:

    - The removal of rule 4.2 from the SRA Authorisation Rules for Legal Services Bodies and Licensable Bodies 2011 (SRA Authorisation Rules) which would mean that an application by a licensable body for authorisation would no longer need to include a statement of the reserved legal activities ("RLA") for which the body seeks authorisation.
    - The removal of rule 22.1(a)(iii) from the SRA Authorisation Rules, which means the SRA will no longer have the power to revoke or suspend a body's authorisation where it is satisfied that the body has no intention of carrying on the legal activities for which it has been authorised.

[1] Decision Notice of 29 October 2015
http://www.legalservicesboard.org.uk/Projects/statutory_decision_making/pdf/2015/20151029_Regulatory_Reform_2015_Decision_Notice.pdf

- Simplification of rule 4.3 of the SRA Authorisation Rules so that it states that the SRA may grant an application [for authorisation of a licensable body] in relation to one or more reserved activities.

LSB's handling of the application

3. On 28th October 2015, the LSB issued a 'warning notice' under the Act notifying the SRA and the Law Society ('TLS') that it was considering refusing the reserved activities proposals under the refusal criteria in the Act. The effect of a warning notice is to extend the decision period in which the LSB can consider the application. The Act provides that the Board has a period of 12 months from the date of the applicant receiving the warning notice to continue considering the proposed rule change.
4. The LSB's focus of further consideration has been exclusively in respect of the removal of rules 4.2 and 22.1(a)(iii) from the SRA Authorisation Rules part of the application. The simplification of rule 4.3 of the Authorisation Rules has not caused us concern as it is a minor drafting adjustment. The change does not alter its meaning. The SRA expressed the view, however, that the alteration to rule 4.3 should only be made if removal of rule 4.2 is approved. Consequently, rule 4.3 was also not approved and became technically subject to the warning notice process.

Reasons for LSB issuing a warning notice

5. The SRA's current regulatory arrangements list the circumstances where it may revoke or suspend a firm's authorisation, including where it is satisfied that the body has no intention of carrying on the legal services for which it has been authorised. One effect of this is that unless firms are able to establish that they have undertaken some reserved legal activity (the example of one oath a year was cited) they could lose a licence to carry on activities for which they are competent but have not been carried out by their business over a particular period. The removal of rule 22.1(a)(iii) will mean the SRA's ability to revoke or suspend a body's authorisation is removed even though an entity has not carried out the legal activities for which it has been authorised.
6. The removal of rule 4.2 will also mean that an application by a licensable body for authorisation will no longer need to include a statement of the RLA for which the body seeks authorisation. This requirement to provide this statement can be a potential barrier to entry. Some firms may wish to be able to undertake RLA even though it will not be clear in advance whether the legal services sought are reserved activities.
7. However the change could be perceived as extending the scope of regulation. One potential outcome of the removal of the rules is that that firms that do not currently carry out RLA (and so therefore do not need to be authorised) and have no intention of carrying out RLA, could choose to seek authorisation,

thereby generating a perception that the SRA has extended regulation. There is a risk in this that that it could be perceived as a 'quasi-voluntary' accreditation scheme for firms who do not undertake RLA, but who choose to be authorised by the SRA in order to attain the potential market benefit and credibility of having regulated status. Of particular bearing with respect to the refusal criteria in the Act, was whether:

- granting the application would be contrary to any provision made by or by virtue of the Act or other enactment
- granting the application would be prejudicial to the regulatory objectives, including, protecting and promoting the public interest, and protecting and promoting the interest of consumers
- granting the application would be contrary to the public interest.

Letter from the Law Society

8. The Board will wish to note that the LSB received a letter from the Law Society during the warning notice period setting out its concerns. They questioned whether this was a proper exercise of regulatory functions; and whether the removal of the rules amounts to the introduction of an accreditation scheme. The LSB rules change process does not normally involve "consultation". In the interests of fairness and transparency, the letter was, however, sent to the SRA who were invited to comment on the issues raised. It chose not to do so. The LSB considered the matters raised by the Law Society and the LSB's conclusions are set out in the notice.

The LSB's assessment and conclusions

9. In making decisions on applications for alterations to regulatory arrangements, the LSB has to consider whether it has sufficient evidence and cause to refuse rule changes against the refusal criteria in Schedule 4 of the Act. Considering the refusal criteria set out in the warning notice we have reached the following assessment.

Would granting the application be contrary to any provision made by or by virtue of the Act or other enactment

10. One of the SRA's arguments was that the current rules go beyond what is required in the Act. The LSB sought legal advice from counsel; a copy of the advice is in **Annex B**.

11. [redacted]

[redacted]

12. [redacted]

13. [redacted]

14. [redacted]

Would granting the application be prejudicial to the regulatory objectives, including, protecting and promoting the public interest, and protecting and promoting the interest of consumers? Would granting the application be contrary to the public interest?

15. The potential detrimental impact for consumers is that the cost to firms of being authorised by the SRA (when there is no statutory obligation for them to be authorised) could be passed on to the clients of those firms. While this may be a risk for those clients, this effect seems likely to be small or even non-existent as a result of competition with those firms that choose to be unregulated by the SRA.

16. The possible risk of detriment to consumers, also needs to be balanced against other considerations. There is no evidence that a number of firms in the current market who are not undertaking RLA, would seek to be authorised by the SRA if the rules were removed. There is an argument that only firms in such a position would already be authorised by the SRA (for example, firms offering one oath a year). In the absence of evidence of such “pent up demand” it would be difficult

for the LSB to refuse the application on the basis that there might be an adverse impact on consumers from non-RLA firms becoming authorised by the SRA. The rationale for our decision cannot be based on a speculative assessment of the potential wider market consequences of removing specific rules.

17. There is also the counter argument that consumers might benefit from the protections afforded by being clients of firms that choose to become authorised by the SRA, even if this entails increased costs.

18. One of the reasons for the SRA removing the rules is that they have, according to the SRA, acted as barriers to entry, with some potential applicants being advised that they need to carry on an RLA to gain and maintain authorisation. It is reported by the SRA that firms who may not be able to show they are conducting RLA at a particular point in time (but have every intention of doing so or wish to be in a position to do so should their clients require it) are being discouraged from seeking authorisation as an ABS. This could have an impact on consumer choice

19. These consumer protection concerns lead into the wider public interest point of the potential for authorisation (and the regulation that comes with it) being extended to firms who do not need to be authorised. A major consideration is that the SRA is not introducing an 'obligation' on any firm to be authorised; firms would be choosing to operate in a regulatory environment. This would not be a compulsory regulatory burden on such firms as they would be able to carry on all their activities outside of regulation if they chose to do so.

20. In its arguments supporting the application, the SRA pointed to the difficulties in policing what firms "intend" to do; as a consequence it has not made use of the power to revoke or suspend authorisation under rule 22.1(a). Where regulatory arrangements are difficult to enforce, then consideration must be given to whether this is in the public interest and the arrangements should be removed.

The decision for the Board

21. In recommending to the Board that we approve the application, we recognise the decision is finely balanced, and brings in wider issues around the regulation of the legal services market. In making the decision the Board must have regard to best regulatory practice. The Board will also be conscious of the current deregulatory environment.

22. The Board may wish to consider and discuss whether it is in the interest of consumers, or the public, for the SRA to have in place regulatory arrangements that will allow it to authorise firms to provide RLA who are not in fact undertaking RLA. The effect of this would be that firms can choose to be regulated; there is no compulsion.

23. Our view is that there is merit in the arguments about the current arrangements being unnecessary, difficult to enforce and a potential barrier to entry and that these arguments support the removal of these rules. While we recognise that the

changes may mean that some firms not undertaking RLA could become authorised, our assessment cannot be speculative, and we do not consider there is evidence of significant risk that removing the rules in themselves will lead to an expansion of regulation. In this regard we are reassured by the SRA's commitment to review the impact of these changes and, most importantly, not to market the rule change as a quasi-voluntary accreditation scheme.

Conclusion and recommendations

24. Having completed the further assessment of the reserved activities part of the SRA's Regulatory Reform Programme application, and acknowledging that there are some concerns about removing the rules, we conclude that granting the application would not be contrary to any provision in the Act or other enactment. Furthermore, on balance, there is insufficient evidence to recommend to the Board that it refuse the changes on the basis that they are prejudicial to the regulatory objectives or contrary to the public interest under Schedule 4 of the Act.

25. We therefore recommend that the reserved activities changes proposed to the Authorisation Rules should be granted.

26. The Board is invited:

(1) to agree that the part of the application from the SRA to alterations to the regulatory arrangements in respect of reserved activities be granted.

(2) to note the draft decision notice set out in **Annex A** and to delegate the finalising of the wording of the decision notice to the Chairman and Chief Executive.