

To:	Legal Services Board	
Date:	26 May 2016	Item: Paper (16) 34

Title:	Practising Fee Rules Decision Document	
Workstream(s):	Statutory Decisions	
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Status:	Official	

Summary:

This paper sets out the results of the recent consultation on the Practising Fee Rules 2009 (the PCF Rules) and seeks the Board's agreement to the approval of the proposed changes to those rules. **Annex A** to this Board paper summarises the background to the review.

The proposed changes to the PCF Rules were publically consulted on from 10 February to 8 April 2016. The proposed changes were:

1. to include explicit reference that the Board will have regard to the regulatory objectives when considering PCF applications and,
2. to include criteria that approved regulators will need to provide clarity and transparency about: the impact on practising fees in respect of the allocation of all its financial resources, whether or not those resources arise from permitted purposes; and, where the proposal is to increase the PCF, anticipate income (from all sources and its allocation to the permitted purposes) and estimates for the practising fee for the following three years.

Seven responses to the consultation were made. Five were from regulatory bodies of approved regulators and were largely supportive of the proposals. Two were from the representative bodies (the Law Society and the Bar Council) which each made comments on whether the proposals were within the LSB's scope. The LSB sets out the legal advice at **Annex B** addressing the main points raised by the Law Society and Bar Council.

Having considered the responses, we recommend that the changes to the rules are made with one small amendment (other than typographical changes) to the version consulted on. The change proposed to 10(f), is to make clear that any enquiries about the use of financial resources will be made to ensure that the LSB has all the relevant information that it needs to assess the impact on the level of the proposed fee.

A summary of the responses and the LSB's decision have been explained in the consultation decision document at **Annex C** and in this paper. Subject to the

Board's approval, the decision document will be published along with all the individual responses.

Recommendation(s):

The Board is invited to:

1. Note the outcome of the LSB consultation on the LSB's Practising Fee Rules 2009 explained in this paper.
2. As a matter reserved to the Board, approve the changes to the Practising Fee Rules which will be renamed as the Practising Fee Rules 2016

Risks and mitigations

Financial: None.

Legal: [Redacted]

Reputational: Reputational damage to the LSB if the rules and guidance are unclear. The rules have been subject to consultation; the non-statutory guidance (which the Board is not being asked to agree) was also reviewed by the LSB during the consultation period and respondents to the consultation were invited to comment on any additional guidance that might assist them in the making of a practising certificate fee application. Only one suggestion was made (by one respondent) that there should be clarity on exactly how much detail approved regulators are expected to provide in order to be transparent, without providing commercially sensitive information. We will consider how to address this in the guidance.

Resource: No resource risks.

Consultation	Yes	No	Who / why?
Board Members:	√		Board members informed and views sought at 21 January 2016 Board meeting.
Consumer Panel:		√	
Others:	None.		

Freedom of Information Act 2000 (Fol)

Para ref	Fol exemption and summary	Expires
Cover Risk and mitigations: Legal	Section 36(2)(b)(ii): information likely to inhibit the exchange of views for the purposes of deliberation	
Para 4, first sentence;	Section 42 Legal privilege	N/A

Annex B		
Annex C	Section 22: information intended for future publication	N/A

LEGAL SERVICES BOARD

To:	Legal Services Board	
Date of Meeting:	26 May 2016	Item: Paper (16) 34

Review of the LSB's Practising Fee Rules 2009

Background

Reasons for the review and proposed changes to the LSB's Practising Fee Rules 2009

1. We set out the findings of our review of the Practising Fees Rules 2009 (PCF Rules) to the Board in January 2016. The review was started in response to an issue around use of so called, "derivative income", (that is income that arises from PCF funded permitted purposes such as training courses) that arose with respect to a practising certificate fee (PCF) application from the 2015/16 round. In addition, the rules have been in place since 2010 and were due for a review. A summary of the review and its findings is attached at **Annex A**.
2. Neither the Legal Services Act 2007 ("the Act") nor the PCF Rules include reference to the concept of derivative income and how it might be used. Using income to pay for 'non permitted purposes' is not explicitly prohibited. However, since the regulated community have no choice but to pay the PCF, we have questioned whether it is compatible with the regulatory objectives that income from activities funded by the mandatory PCF can be used for representative activities for which there may be little or no benefit to some fee-payers.
3. When considering a PCF application, the LSB must take into account the criteria for deciding applications that are set out in the PCF Rules. But there are also wider considerations beyond the requirements of section 51 of the Act. The PCF approval process is an exercise of the LSB's functions and in delivering that function we must act in way that is compatible with the overall regulatory objectives.
4. [REDACTED]
[REDACTED]
[REDACTED] We therefore proposed new rules and consulted on these. The proposed rules and the result of the consultation are set out below.

Consultation on changes to the PCF Rules

5. We published an eight-week consultation on changes to the PCF Rules on 11 February which closed on 8 April. The consultation proposed three main groups of changes:

Reference to the regulatory objectives

6. When considering a PCF application, the LSB must take into account the criteria for deciding applications that are set out in the PCF Rules. While section 51 of the Act provides the basis upon which the LSB may make rules specifying the permitted purposes and requires the Board to approve the level of the fee, there are also wider considerations beyond the requirements of section 51 of the Act. A PCF approval will be an exercise of the LSB's functions and in delivering that function we must act in way that is compatible with the overall regulatory objectives. This was not stated explicitly in the PCF Rules issued in 2009. We therefore decided to emphasise this obligation, and additional criterion was inserted as Rule 10(a) in section D of the proposed rules that the Board and approved regulator should have regard to:

10(a) *compatibility with the regulatory objectives*"; and the following definition of regulatory objectives was added in section A definitions:

"regulatory objectives has the meaning given to it by Section 1(1) of the Act".

Clarity and transparency about the total income and its impact on practising fees

7. We consider it appropriate that the regulated community knows how income and resources will be allocated, and whether they are from permitted or non-permitted activities and sources. Consequently we proposed to introduce a rule that requires the approved regulator to be clear and transparent about its allocation of financial resources in order to ensure accountability in the public interest. We therefore added a criterion inserted as a new rule 10(f) in section D of the proposed rules which states that the Board and approved regulator should have regard to:

10(f) clarity and transparency on the allocation of all the approved regulator's financial resources, whether or not those resources arise from permitted purposes, and the impact on the proposed practising fee.

8. It should be noted that the proposed amendments do not specifically prohibit (or indeed mention) derivative income. We propose to deal with this specific issue in more detail in the non-statutory guidance that supports the rules.

Evidence required by the Board

9. While we are generally asked to approve PCFs for a single year, the proposed level may be determined by the expected expenditure in that year and forecasts for future years.
10. Therefore, in order to assist the LSB in our consideration of a PCF application, we proposed a change to the evidence that is to be submitted where there is a proposed increase in the PCFs, to include future forecasts of budgets. The additional criteria were inserted as 11(b) and 11(c) in section D of the PCF Rules:

11(b) where there is a proposed increase in practising fees, the budget should show anticipated income from all sources and its allocation to the permitted purposes for the current application and, where available, the next three years;

11(c) the proposed practising fees for the current application and, where there is a proposed increase in practising fees and where available, the estimates for the next three years.

Consultation responses

11. Seven responses were submitted and have been summarised in the decision document at **Annex C**. Subject to the Board's approval the decision document and the individual responses will be published on the LSB website.

General response

12. Broadly, respondents were in favour of the changes, particularly in respect of highlighting that the LSB and approved regulator should have regard to compatibility with the regulatory objectives. Some concerns were raised, primarily from the Bar Council and The Law Society. Nonetheless, there was general agreement to requiring clarity and transparency with respect to the allocation of all the approved regulator's financial resources, whether or not they arise from permitted purposes, and for three year forecasts where there is a proposed increase in PCF.

10 a Reference to the regulatory objectives

13. As referred to above, there was general agreement from all the respondents that it was appropriate to include reference to the regulatory objectives. The Bar Council, the Law Society and the SRA suggested that 10(a) should also make reference to the better regulation principles and best regulatory practice. After careful consideration we concluded that it was not necessary to include this level

of detail in the rules. We have regard to the better regulation principles and best regulatory practice whenever we are exercising our statutory functions.

14. The Law Society also proposed that, “compatibility with the regulatory objectives”, should be given, “its ordinary meaning i.e. that the LSB’s assessment of this factor will not extend to compatibility with non-regulatory objectives of an approved regulator (which the LSB is unable to do in view of the limitations in Section 29(1) of the Act)”. Section 29(1) of the Act specifies that nothing in the Act authorises the Board to exercise its functions in relation to a representative function of an approved regulator.
15. We are explicit in paragraph 14 of the decision document that we recognise that we are not able to do anything that would amount to the LSB exercising its functions in relation to the representative functions of an approved regulator. However, we have also made clear that there are sufficient powers in the Act to request reasonable and proportionate information in order for the LSB to make statutory decisions that it is required to make.

10f Clarity and transparency about the total income and its impact on practising fees

16. Most of the respondents were in favour of greater transparency with respect to showing total income. The SRA, for example, believed greater clarity and transparency will assist the LSB in making its decisions, and said that its experience of the operation of the rules shows that the interplay between the activities which may be funded through fees raised through section 51 can be complex. The Bar Council and The Law Society, however, raised concerns and objections which focussed on whether the information and scrutiny required was proportionate and a proper use of the LSB’s powers.
17. The Law Society queried the legal basis upon which the information required under 10(f) on financial resources may be taken into account by the LSB for the purpose of approving the PCF level. The Law Society’s and Bar Council’s concerns are set out in further detail in the decision document. The LSB sets out its legal advice addressing the main points raised by the Law Society and Bar Council at **Annex B**.
18. The LSB’s view is that there are sufficient powers in the Act to obtain reasonable and proportionate information to make a robust decision on whether to approve a PCF application. As we explain in paragraph 18 of the decision document, the LSB is aware that an approved regulator engages in activities that are not permitted purposes and are not funded by PCF. We would not be interested in

those activities unless they affect the practising fee (for example, where revenue generated from non-permitted purposes is used to subsidise permitted purposes, thereby reducing the PCF or where revenue generated from permitted purposes subsidises a non-permitted purpose instead of being used to off-set against the PCF). We think it is reasonable and within the scope of the Act to require clarity and transparency on such matters.

11 b and c Evidence required by the Board

19. There was a general understanding that the contextual information provided by a three year forecast would be helpful in cases where there was the intention to increase PCF. The SRA for example said that this would help to highlight the issues underlying an increase.
20. The Law Society queried whether the requirement was necessary or permissible under the Act, using the same arguments as for their objections to 10(f). The CLSB said that the requirement was burdensome and the need was not backed up by evidence. The Bar Council thought that three years was too short and prescriptive and suggested five years. The BSB argued that the requirement should be made whether or not the fee was to be increased. CILEx asked for an adequate transition period to enable adjustments to their financial modelling.
21. Provision of a three-year forecast is appropriate in order for it and the regulated community to see how an increase is positioned within the longer term budgetary and strategic direction of the approved regulator. As we said in the consultation document, the proposed level may be determined not only by the expenditure in that financial year, but also by forecasts for future years.
22. So that we do not overburden approved regulators, we are only requesting this information if there is an intended increase and we think that three years is a realistic expectation of what approved regulators could provide. As we said at the time of the publication of the consultation, we believe in the importance of reducing regulatory costs in legal services. As such, we hope that in most years and for most approved regulators, they will not be required to provide the three-year forecast. We will talk to individual approved regulators on a case-by-case basis in the pre-application phase to ascertain and agree what they are able to supply with respect to forecasting, taking account of their systems and resources to provide the information.

Conclusions

23. We have carefully considered the feedback received from the consultation respondents. We have also sought a legal view from our LSB legal team and external lawyers on some of the major issues raised by respondents.
24. We have determined that one small amendment should be made to the proposed rules at paragraph 10(f). This is to make clear that any enquiries about the use of financial resources will be made for the purposes of enabling the LSB to assess the impact of the proposed fee, therefore fulfilling our statutory decision making functions. The new rule is:
- “for the purposes of enabling the LSB to assess the impact on the proposed practising fee, provide clarity and transparency on the allocation of all approved regulator’s financial resources, whether or not those resources arise from permitted purposes;”
25. The Board should note that the guidance (which does not require Board agreement) that will support the rules and is non-statutory, will be drafted and cleared by the Chief Executive and published at the same time as the decision document.

Recommendation

26. The Board is invited to:
- Note the outcome of the LSB consultation on the LSB’s Practising Fee Rules 2009 explained in this paper.
 - As a matter reserved to the Board, approve the changes to the Practising Fee Rules which will be renamed as the Practising Fee Rules 2016

