



<b>To:</b>	Board		
<b>Date of Meeting:</b>	27 April 2010	<b>Item:</b>	Paper (10) 30

<b>Title:</b>	Practising fee approvals
<b>Workstream(s):</b>	2E – Securing independent regulation
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<b>Status:</b>	Protect

### Summary:

Section 51 of the Legal Services Act 2007 (**'the Act'**) provides that the Legal Services Board (**LSB**) approves the level of the mandatory practicing fees set by each Approved Regulator (**AR**). The LSB has published rules setting out how applications are to be made, considered and decided upon.

The rules set a broad framework for the approval of practicing fees but also provided that the LSB may set out further detail. It was intended that a final application and approval framework would be reached following discussions with the ARs to ensure that the mechanism may work in practice for the fee year 2011 and into the future. The Project Team has recently completed meetings with or received appropriate correspondence from each AR.

This paper **updates** the Board on the position that has been reached following these meetings for them to **note** the final application and approval framework that will apply to each AR as it submits applications for LSB over the next six months. The paper covers the following areas:

- LSB's approach to approvals
- Consultation and transparency
- Criteria and evidence requirements
- Permitted purposes
- Timetables for approval
- Initial thinking on likely internal authorisation process.

### Risks and mitigations

<b>Financial:</b>	N/A
<b>FoIA:</b>	Disclosable.
<b>Legal:</b>	Minimal as rules already published.
<b>Reputational:</b>	High - financial impacts on all ARs and all of their members.
<b>Resource:</b>	Processing applications will be resource intensive but will be mitigated by the approach adopted.

<b>Consultation</b>	<b>Yes</b>	<b>No</b>	<b>Who / why?</b>
<b>Board Members:</b>		✓	Update only
<b>Consumer Panel:</b>		✓	Update only
<b>Others:</b>	Met with and / or corresponded with all ARs		

<b>Recommendations:</b>
The Board is invited to note and to discuss the update.

## LEGAL SERVICES BOARD

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### Practising fee approvals

#### Background

1. Section 51 of the Act provides that a practising fee is payable only if the LSB has approved the level of the fee. Section 51(6) required that the Board make certain rules about the framework for approving applications and that they must make provision in three key areas:
  - a) The form and manner in which applications must be made and material which must accompany such applications.
  - b) Requiring applicants to have consulted such persons as may be prescribed by the rules in such a manner that may be prescribed by the rules before such an application is made.
  - c) The procedures and criteria that will be applied by the Board when determining whether to approve the level of the fee including provision about the time limit for determining an application.
2. The Act also requires that an AR may only apply amounts raised by the practising fees for one or more of the permitted purposes and that the LSB makes rules setting out the permitted purposes (see **Section C of Annex A**). However, the Act includes specified activities that must be included in the permitted purposes. These are not restricted to straight regulatory activities more akin to professional body activity.

#### Introduction

3. Practising Fee Rules as specified above were published, along with the supporting consultation document, on 10 December 2009 (**Annex A**). The rules set out the likely minimum criteria against which we will consider applications and the evidence required to demonstrate compliance. They also provided that we set out criteria and evidence requirements from time to time in respect of **each** AR as well as specifying consultation requirements in establishing the level of the practising fee and the timetable of key submission and decision dates.
4. Following publication of the rules we wrote an open letter to all ARs and their Regulatory Arms offering to work with each to ensure that the approval mechanism works for them in practise. We were concerned that our final requirements must be sympathetic to the budget processes and cycles of each AR so as not to cause undue disruption. This is particularly so for the first year as the planning cycle for the following year would inevitably have started already and significant new requirements could cause real logistical problems.
5. During the first three months of 2010 we had initial discussions with all of the ARs and are in a position to write to each to formally set out the final requirements for the 2011 practising year. We think that it is appropriate to do this by way of general requirements relating to consultation, criteria and

evidence that will apply to all ARs and individual approval timetables for each AR. As provided by the rules we will set out some further detail on the baseline criteria and evidence specified in the rules.

6. We are asking the Board to consider our proposed framework for Section 51 approvals of the practising fee level in advance of receiving the first application which is expected to be received in May from the Master of the Faculties. We then anticipate receiving a steady flow of applications from the remaining seven<sup>1</sup> affected ARs over the next six months. To allow us to process these applications quickly and efficiently it is important that Board members are familiar and comfortable with the framework that we are proposing.

### **LSB as oversight regulator**

7. The LSB's role of oversight extends to the budget approval process. We should not be drawn into detailed budget analysis and scrutiny that we do not consider it appropriate to undertake and which the requirements of the Act do not demand. The responsibility for setting fees at the correct and appropriate level remains with the front line regulators. The LSB's budget approval process should essentially be limited to satisfying ourselves that:
  - The fees are legal in that they are only to be used to fund permitted purposes as set out in the Act and supporting rules. The Act defines the mandated purposes broadly to cover activity that goes beyond purely regulatory functions.
  - That the AR has acted in compliance with Section 30 of the Act and the supporting Internal Governance Rules in providing independent regulatory arms sufficient resource to define and carry out a strategy for the performance of its regulatory functions.
  - That the AR has followed a rational process in setting the fees in that they are linked to the delivery short and medium term strategy and can explain any significant fluctuations in fee levels year-on-year.
  - That the fees are not so high as to ostensibly instil a barrier to entry or practising especially to non-commercial services, impact on whom Section 51(7)(a) requires us to take into account before determining an application.
  - That the AR is fully accountable to its members who are mandated to pay the fees being set and have been proactive in ensuring transparency and clarity of understanding about how the level of the fees has been settled and how the collected money is being used; and in providing opportunity to members to input into and influence the fee setting process. This is the ethos that underpins our rules and also the Act in that Section 51(6)(b) explicitly requires our rules to specify consultation requirements. Our strategic aim is to drive a culture where the rank and file of each AR actively seeks to provide robust and genuine scrutiny and is empowered to do so.
  - That the AR has undertaken the consultation with the voluntary sector mandated in Section 51(7)(a) of the Act.

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<sup>1</sup> The two accountancy bodies that are approved regulators, ACCA and ICAS, do not yet have any authorised persons as members and do not propose to raise practising fees this year.

8. Given that the above approach demands a far greater level of transparency than most ARs provide at present, our rule of thumb should be that a practising fee application should only be required to contain the same level of information that the LSB expects the AR to make available to each of its members during the settlement process and vice versa. By aligning information requirements in this way we will promote wider accountability through transparency and ensure that the approval process places no unnecessary administrative burden on either the LSB or ARs: we will not receive any information that we will not review nor review any information that we do not need. In the round this approach is in keeping with the better regulation principles and is proportionate to the role of oversight.
9. Through our general powers, we will reserve the right to dig deeper and possibly insist that an AR undertakes to provide audited evidence outside of the standard budget approval process. This would happen if we were presented with a compelling reason to do so such as evidence that practising fee revenue is being spent on purposes that are not permitted, indications that the AR is not properly resourced to undertake its regulatory duties or because members (or potential future members) make a compelling argument that fees are being set artificially high. This activity may form part of a regulatory review process, particularly if at any future point financing and fee levels is considered a priority area for thematic review.

### **Consultation**

10. From our discussions with ARs it is apparent that some engage with their membership during the budget and practising fee settlement process more than others, both in terms of how they invite input and the breadth of the membership that they target. We have accepted the arguments put to us that it is not practicable to require additional advance consultation this year because for many there is not the slack in the budget cycle that has already begun to allow this. However, we will send out the message that we may request more next year. This is permitted by the provision at rule D(9)(c) that in respect of each AR we may specify from time to time "the persons that should be consulted by the Approved Regulator before submitting the application".
11. How hard each AR will need to be pushed will depend on their current level of engagement and how significant changes to fee levels and / or how the fees are spent. It is apparent that all are some way off the ideal of actively promoting a culture of advance scrutiny and influence by as broad a selection of the membership as possible. We stated in our response to the original consultation on Internal Governance and Practising Fee Rules, published in September 2009, that where changes are minimal then consultation with representative governing councils or equivalent should be sufficient. However, this should not fetter our messaging as the messaging itself may encourage some members to seek a greater level of empowerment.

12.





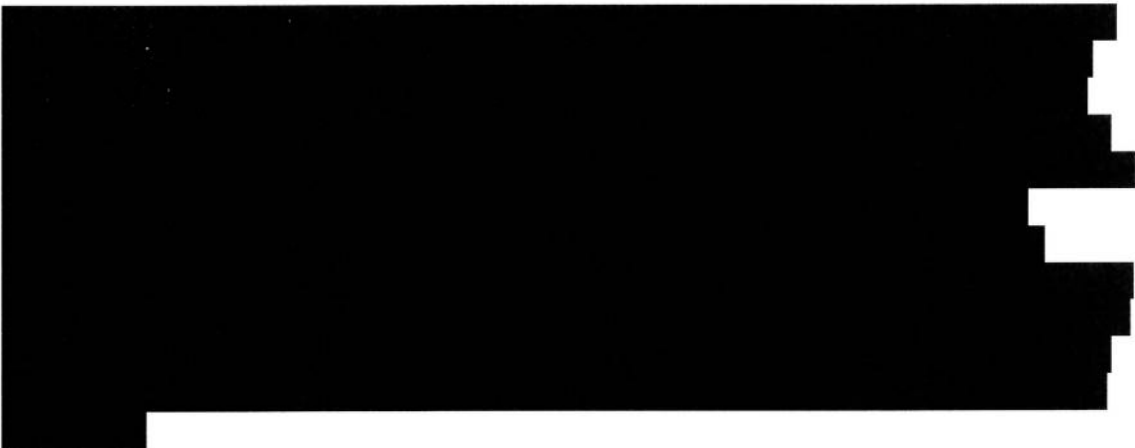


13. Section 51(7)(a) of the Act provides that our rules must contain “provision requiring the Board, before it determines an application for approval of the level of a fee, to consult such persons as it considers appropriate about the impact of the proposed fee on persons providing non-commercial legal services”. Rule D(12) provides that we may consult any person it considers appropriate and in particular the Consumer Panel and we will make all applications available to the Panel. However, to provide reassurance that the impacts on persons providing non-commercial legal services have been considered, we have encouraged ARs to share details of the practising fee level in advance of submission with appropriate bodies such as Law Centres Federation, Citizens Advice and Advice Service Alliance.



#### **Transparency and breakdown of expenditure**

14. We have accepted that we should not specify advanced consultation requirements this year and in any event will have to step carefully with any demands. This increases the need for steadfastness in our commitment to drive transparency and clarity of understanding at the point that the practising fee demand is made in order to provide accountability and the opportunity for members to assert pressure on their AR retrospectively, should they have cause for concern.
15. We have framed our discussions with the ARs with the analogy of the Council Tax leaflets distributed alongside the forward council tax bill each year (but with no requirement for a paper based exercise). Given the statutory requirement to only expend practising fee revenue on the permitted purposes we will also require analysis of spend against each of the permitted purposes. We will require the analysis to provide what expenditure is for purely regulatory functions as opposed to functions that are not purely regulatory by nature but which nonetheless falls within the permitted purposes. This will in effect require each AR to allocate its activities to pure regulation, permitted purposes and purely membership functions.
16. As well as breakdown by the permitted purposes, we would expect to see:
  - detail of the revenue raised in the previous year and how it was spent, broken down between functional department / expenditure head;
  - forecasts of the revenue that will be raised in the forthcoming year and how it will be spent, broken down between functional department / expenditure head;
  - details of variance from the previous year in terms of total revenue, fee level and proportionate split between functional departments / expenditure heads;

- Explanation of any significant variance (say in excess +/- 5%) in any of the above areas.
17. We would also expect there to be a description of the process that was followed in settling the budget and some evidence that it has been settled in light of immediate and medium term budgetary needs, for example by showing how the budget has been developed alongside and to support business plans.
  18. We believe that the criteria above will draw the picture of where the money goes so as to allow the LSB and the AR's members to assess whether the fees are legal and that a rational process has been followed. The information will also allow members to scrutinise whether they think that the level of the fee is appropriate especially as ARs will be required to set out revenue used for the permitted purpose and not just limited to that collected through the practising fee (the only part the LSB has vires over). We also believe that the Council Tax analogy sets the right level of detail to provide transparency without compromising clarity of understanding because of information overload.
  19. Our discussions with ARs have shown a general acceptance of our proposals for transparency and breakdown of expenditure. They are built squarely on the requirements within Section 51(6)(b) of the Act to specify the materials to accompany an application, our rules D(10) and (11) that set the broad criteria and evidence in these terms and rule 9 that provides that we set out further detail from time to time (with the intention to provide clarity of requirement to ARs).

20. 

**Permitted Purposes**

21. We will require each AR to provide self-analysis that activities that are funded through the practicing fees fall within the permitted purposes. As the permitted purposes are broad and extend beyond pure regulation, considerable scope exists for ARs to argue that activity fits within the permitted purposes even if it feels representative in nature.   

22. We do not think that it is a priority to divert LSB resource to undertake our own detailed scrutiny of the AR's analysis. However we do not wish to be solely

reliant on self-analysis. As stated earlier, the information that we will require within practising fee approval applications will build a picture of where the money goes. The transparency requirements that we are proposing will allow members, the trade press and other interested parties to scrutinise and expose any large scale misuse of the mandatory practising fee. The permitted purposes were originally introduced in the 1990s following The Law Society undertaking a large scale campaign against legal aid provisions that saw large amounts of the mandatory practising fee expended on media exposure that was publicly criticised from various corners.

23. It is also recommended that, after the first round of approvals when we have built up the suite of information provided by each AR and their analysis of expenditure against the permitted purposes, we undertake a more systematic review. This may help inform whether there are compelling reasons to dig deeper in relation to particular ARs or whether consideration should be given to this area generally when setting priorities for future thematic regulatory review. It may also lead us to consider the scope for tightening definitions of permitted purposes within our rules (if not the Act), should the evidence support this.

### **Independence**

24. We will require clear evidence that there is sufficient resource to allow regulatory arms to define and carry out a strategy for the performance of its regulatory functions. This will be evidenced and self-certified through the Internal Governance Rules compliance process. Completed dual self certificates are required to be returned by all Applicable ARs by the end of April. An update of our analysis following the returns will be presented to the Board on 29 June.

### **Authority and timetable for approving applications**

25. We have been supportive in our commitment to work LSB approval around the budget cycle of each AR. Following the recent round of meetings, the Project Team is currently plotting a complete map of preferred submission and approval points for individual ARs through the remainder of the year.
26. It is anticipated that the first submission will be from The Faculty Office and will seek approval at the next meeting of the Board. The Project Team will present the complete map at that time. It is anticipated that the practicalities of the timetable will make some form of delegated authority for approval desirable. A suitable proposal will be presented to the meeting of the Board on 27 May.



The Legal Services Board has, on 9 December 2009, made the following rules under Legal Services Act 2007 (c.29), section 51(3) and (6):

## **PRACTISING FEE RULES 2009**

### **A. DEFINITIONS**

1. The words defined in these rules have the following meanings:

<b>Act</b>	the Legal Services Act 2007 (c.29)
<b>Applicable persons</b>	includes “relevant authorised persons” as defined in Section 51(8) of the Act but extends also to other persons over which the Approved Regulator has regulatory powers
<b>Approved Regulator</b>	has the meaning given in Section 20(2) of the Act
<b>Board</b>	the Legal Services Board
<b>Consumer Panel</b>	the panel of persons established and maintained by the Board in accordance with Section 8 of the Act
<b>legal services</b>	means services provided by a person which consist of or include “legal activities” as defined by Section 12(3) and 12(4) of the Act
<b>permitted purposes</b>	the purposes which an Approved Regulator may apply amounts raised by practising fees, as set out in Rule 6 of these Rules
<b>person</b>	includes a body of persons (corporate or unincorporated)
<b>practising fees</b>	has the meaning given by Section 51(1) of the Act

**regulatory functions** has the meaning given by Section 27(1) of the Act

**reserved legal services** has the meaning given in Section 207(1) of the Act.

## **B. WHO DO THESE RULES APPLY TO?**

2. These Rules are the rules that the Board has made in compliance with 51(3) and 51(6) of the Act relating to the control of practising fees charged by Approved Regulators.
3. Accordingly, these Rules apply to each Approved Regulator that proposes to charge practising fees as part of its regulatory arrangements.
4. In the event of any inconsistency between these Rules and the provisions of the Act, the provisions of the Act prevail.

## **C. THE PERMITTED PURPOSES**

5. Monies raised through practising fees must not be applied for any purpose other than one or more of the permitted purposes.
6. The permitted purposes are:
  - (a) the regulation, accreditation, education and training of applicable persons and those either holding themselves out as or wishing to become such persons, including:
    - (i) the maintaining and raising of their professional standards; and
    - (ii) the giving of practical support, and advice about practice management, in relation to practices carried on by such persons;
  - (b) the payment of a levy imposed on the Approved Regulator under section 173 of the Act and/or the payment of a financial penalty imposed on the Approved Regulator under section 37 of the Act;
  - (c) the participation by the Approved Regulator in law reform and the legislative process;

- (d) the provision by applicable persons, and those either holding themselves out as or wishing to become such persons, of legal services including reserved legal services, immigration advice or immigration services to the public free of charge;
- (e) the promotion of the protection by law of human rights and fundamental freedoms;
- (f) the promotion of relations between the Approved Regulator and relevant national or international bodies, governments or the legal professions of other jurisdictions;
- (g) increasing public understanding of the citizen's legal rights and duties.

#### **D. THE APPROVAL MECHANISM**

7. Where an Approved Regulator proposes to charge practising fees as a part of its regulatory arrangements, the Approved Regulator must apply to the Board for approval of the level of that practising fee.
8. In making an application under Rule 7, an Approved Regulator must comply with the provisions of this Part of these Rules.
9. In respect of each Approved Regulator, the Board will set out from time to time:
  - (a) a timetable including key decisions and submission dates that must be observed by the Approved Regulator and the Board respectively;
  - (b) the persons that should be consulted by the Approved Regulator before submitting its application;
  - (c) the criteria against which the Board will decide on applications put to it; and
  - (d) the evidence required by the Board to satisfy it against the agreed criteria.
10. Insofar as the criteria mentioned in Rule 9 (c) are concerned, the Board and Approved Regulator should have regard to factors including the following:
  - (a) evidence which demonstrates that reasonable care was taken in settling the application in the context of the budget necessary for the immediate and medium term;

- (b) evidence which demonstrates that the revenue raised through the practising fee charge will be applied solely to purposes which are permitted purposes;
- (c) clarity and transparency over the revenue raised through practising fees to be applied for permitted purposes which are regulatory functions;
- (d) clarity and transparency over the revenue raised through practising fees to be applied for permitted purposes which are not regulatory functions; and
- (e) evidence that persons paying practising fees will have explained to them how revenue raised through the charging of practising fees will be applied as between the Approved Regulator's performance of regulatory functions and any other functions also carried on by the Approved Regulator.

11. Insofar as the evidence mentioned in Rule 9 (d) is concerned, the Board and Approved Regulator should have regard to factors including the following:

- (a) a description of how the application was developed and settled, including any consultation carried out, whether or not such consultation was required by the Board;
- (b) a budget showing anticipated income from practising fees, all other expected income to be applied to permitted purposes and planned expenditure of income against the permitted purposes;
- (c) an explanation of how the cost to each regulated person is to be broken down as between income to be allocated to the discharge of regulatory functions and income allocated to any other functions;
- (d) an explanation of contingency arrangements where unexpected regulatory needs arises in-year;
- (e) evidence of how the previous year's practising fee income was allocated only to permitted purposes; and
- (f) a regulatory and diversity impact assessment.

12. In considering an application submitted to it under this Part of these Rules, the Board reserves the right to consult any person it considers appropriate. In particular, it reserves the right to consult the Consumer Panel about the impact of the proposed fee on persons providing non-commercial legal services.

13. If the Board approves an application under this Part of these Rules, it must notify the Approved Regulator concerned.

14. If the Board does not approve an application under this Part of these Rules, it must:

- (a) notify the Approved Regulator concerned;
- (b) give reasons for its decisions;
- (c) require the Approved Regulator to submit a revised application which addresses the Board's reasons for withholding approval previously; and
- (d) specify the circumstances (if any) in which the Approved Regulator may charge a limited practising fee under its regulatory arrangements as an interim measure pending consideration and approval of its full application.