

To:	Board
Date of Meeting:	25 April 2012
Item:	Paper (12) 27

Title:	Internal Governance Rules - process for 2012
Workstream(s):	C: Statutory Decision Making
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Status:	Protect

Summary:

For the past two years, the LSB has required the 'Applicable Approved Regulators' (AARs) to report to it on their compliance with the Internal Governance Rules 2009 (IGRs). AARs are those Approved Regulators (ARs) who have both regulatory and representative functions and must therefore adhere to the Schedule to the IGRs.

This paper recommends that for 2012, the Board again requires AARs to report on compliance with the IGRs. However, the focus this year will be to gain assurance that the formal arrangements that have been put into place over the past few years ensure independent regulation in practice. Given this focus, coupled with the varying degrees of progress made by the AARs since 2009, it is proposed that the LSB tailors its request to each AAR asking for:

- an update on the issues we highlighted in 2011 (set out at **Annex A**), detail of any changes to their arrangements since last year, as well as confirmation that they are (or not) compliant with the IGRs
- evidence that demonstrates oversight by the AAR is in the regulatory body's view appropriate
- the regulatory body's assessment of the risks that exist to its continued compliance (with reference to the IGR principles about governance, appointments, strategy and resources and oversight).

As the Solicitors Regulation Authority (SRA) and The Law Society are not compliant and still under special measures from last year's IGRs process, we propose not to include them in the formal compliance process at this stage, but will keep this under review.

The paper proposes that the regulatory body is responsible for the return with the AAR provided with an opportunity to comment on and counter-sign in agreement (or highlight any differences to the LSB).

We have written to the AARs and their regulatory arms to outline the proposed approach for 2012 and the timetable for response (subject to the Board's agreement) and will feed any comments we have from them into the Board's discussion.

The Board is asked to agree the approach set out in the paper. Subject to the Board's comments, the requests will be sent out week commencing 30 April 2012, with a view to the Board receiving a full report of AAR compliance with the IGRs at its July meeting.

Recommendation(s):

The Board is invited to approve the approach proposed in the paper for the 2012 IGRs process.

Risks and mitigations

Financial: N/A

Legal: See paragraph 7.

Reputational: Some possible – see paragraph 17.

Resource: N/A

Consultation	Yes	No	Who / why?
Board Members:	X		Barbara Saunders and Nicole Smith
Consumer Panel:		X	Not involved the Panel at this stage but will seek advice should it be necessary upon receipt of responses.
Others:			

Freedom of Information Act 2000 (Fol)

Para ref	Fol exemption and summary	Expires
N/A	N/A	N/A

LEGAL SERVICES BOARD

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Internal Governance Rules - process for 2012

Recommendation

1. The Board is invited to approve the approach proposed in the paper to the 2012 IGR compliance exercise.

Background

2. Independent regulation is central to our regulatory framework, providing assurance that regulation supports the regulatory objectives and is in the consumer and public, not professional, interest.
3. On 9 December 2009, the LSB made the IGRs to give effect to section 30 of the Legal Services Act 2007. The key requirement of the Rules is that each AR must:
 - have in place arrangements that observe and respect the principle of regulatory independence; and
 - at all times act in a way which is compatible with the principle of regulatory independence and which it considers most appropriate for the purpose of meeting that principle.
4. While the IGRs apply to each AR, those which have both regulatory and representative functions, the AARs, are required to be compliant with the Schedule to the IGRs to ensure effective separation of their regulatory and representative functions. The Schedule is based on four principles: governance, appointments, strategy and resources and oversight. We asked AARs to complete Certificates in 2010 and 2011 that were based on the Schedule.
5. The Council for Licensed Conveyancers and the Faculty Office are not AARs as they undertake regulatory functions only. ACCA and ICAS are also not included in the IGR process as they do not currently regulate any reserved legal activities.
6. Rule 9 of the IGRs provides that each AAR, jointly with its regulatory board, must:

- (a) if it considers itself to be compliant [with the IGRs], certify such compliance in the form and manner prescribed by the Board from time to time; or
 - (b) if it considers itself not to be compliant [with the Rules], in some or all respects, notify such non-compliance and set out:
 - (i) why it has been unable to comply in such respects as it has identified;
 - (ii) when it considers that it will be compliant; and
 - (iii) how it plans to achieve compliance, by when, and how much it is expected to cost.
7. The Legal Director has advised that Rule 9 provides the Board with discretion as to how it prescribes the process and that the term ‘certify’ does not carry any particular form with it. We are therefore not restricted by the rules to following an identical process each year nor to taking the same approach for each AAR.
8. The first year compliance exercise in 2010 focused on reviewing the newly established governance arrangements. In 2011, we moved on to review the practical measures taken by AARs to embed independence in systems and the conduct of personnel. We are now into the third year of the IGRs being in force and all of the AARs will be fully compliant with the rules by January 2013. This year, we will therefore focus the exercise on understanding the extent to which compliance with the IGRs is delivering regulatory independence in practice.
9. We wrote to the AARs and their regulatory arms on 4 April to outline the proposed approach for 2012 and the timetable (subject to the Board’s agreement). We have asked that if AARs or their regulatory arms had any concerns about the process or the indicative timetable, they provide them to us by 25 April, and the Board will be updated on any comments at its meeting.

Review of 2011 and lessons learned

10. A full assessment of AARs 2011 compliance against the IGR self-assessment is at **Annex A**. This includes the issues that we said we would raise in this year’s process.
11. In summary:
 - Ilex Professional Standards (IPS)/Chartered Institute of Legal Executives (CILEx) were compliant.

- Intellectual Property Regulation Board (IPReg)/Chartered Institute of Patent Attorneys (CIPA)/Institute of Trade Mark Attorneys (ITMA) were compliant.
- Cost Lawyer Standards Board (CLSB)/Association of Costs Lawyers (ACL) were not compliant but were in the process of establishing a new regulatory function, which is yet to be assessed against our IGRs (see paragraph 17).
- Bar Standards Board (BSB)/Bar Council were not compliant, mainly due to our concerns about the BSB's access to finance and resources and the Board not having a lay majority at the time. However, the BSB has had a lay majority since January 2012.
- SRA/The Law Society were not compliant, mainly due to the SRA Board not having a lay majority until 2013 and the arrangements in place for SRA appointments, remuneration, strategy and resources. This resulted in SRA and The Law Society being subject to a section 55 notice from the Board. The notice requires them to provide a monthly report on the implementation of their agreement to achieve compliance with the IGRs, any relevant shared services issues, a log of information requests between the organisations and their outcome and any other matter relevant to the IGRs. We also require all papers, minutes and agendas for the new Business and Oversight Board. This monitoring is due to continue until September 2012, although we can extend beyond this date or conclude the monitoring early.

12. As shown in **Annex A**, the levels of compliance and the responses we received in 2011 varied widely. As we move into the third compliance assessment, it is becoming increasingly important to use the IGRs process as a means of seeking assurance about the functioning of the formal arrangements and structures.

Approach for 2012

13. Building on our experience of previous years', we propose that for 2012, we are not as prescriptive as before and move away from expecting AARs to undertake a detailed assessment against the Schedule to the IGRs, which has been the template for the forms used in the past. While we will expect the Schedule to be used to guide responses, the key focus for this year's exercise will be to understand to what extent compliance with the IGRs is delivering regulatory independence in practice. Therefore our request will not use the form but will ask regulatory arms of the AARs for:

- An update on the issues we highlighted in 2011 (set out at **Annex A**), detail of any changes to their arrangements since last year, as well as confirmation that they are (or not) compliant with the IGRs.
 - Evidence that demonstrates oversight by the AAR is, in the regulatory body's view, appropriate. This could, for example, include an assessment of the functioning and performance of any joint committees or an assessment of the working relationship between the two Boards. We will also seek information about the regulatory board's committee membership, specifically lay committee membership, and the extent to which such committees exercise powers that could have a bearing on the independence of the organisation as a whole. However, in the executive's view, it is important that we are not too prescriptive to allow regulatory arms to provide us with the information they think sufficiently demonstrates ongoing compliance, using the Schedule to the IGRs as their guide. The Board may then use the evidence provided to take a view as to whether or not it concurs with the regulatory arm's assessment and seek any further evidence it thinks necessary to assure itself of the regulatory arm's conclusion.
 - The regulatory arm's assessment of the risks that exist to its continued compliance with the rules, with reference to the IGR principles of governance, appointments, strategy and resources and oversight.
14. While we do expect the AAR to be involved in the process, the request will be addressed to the regulatory arms. In previous years, seeking a joint response from both the AAR and the regulatory arm has been fundamental to putting in place the formal processes and arrangements that the IGRs require. The request will positively recognise this. However, we think that the regulatory arm would be best placed to assess the operation of the IGRs in practice. This approach will also make the process simpler and quicker than before.
15. Therefore, rather than develop a joint response, AARs will be asked to counter-sign agreement with the regulatory arm's response (or refuse with evidence based reasons). The request will provide for the AAR to be able to comment on the regulatory arm's response. This means that we will retain the constructive engagement between the AARs and their regulatory arms that we have seen previously. We will also be clear that we would not take formal action based on the views of the regulatory arms alone and would seek views from the AAR should issues emerge.

16. The exceptions to the approach will be the SRA/The Law Society and CLSB/ACL. We will not be asking SRA/The Law Society to certify compliance this year as they will be unable to. Following the 2011 IGR process, SRA/The Law Society remain under special measures, as set out at paragraph 10. We will rely on our ongoing, monthly monitoring of SRA/The Law Society under section 55 to track their progress towards achieving compliance with the IGRs and will ask them to certify compliance when we reach a suitable point in the section 55 reporting process. However, we do not expect them to be compliant until January 2013, when the SRA Board achieves a lay majority.
17. CLSB became the approved regulator of costs lawyers on 31 October 2011 meaning CLSB and ACL have not yet undertaken an assessment against the Schedule to the IGRs. We will therefore ask them to undertake an assessment against the Schedule as part of this year's process.
18. We will seek responses to our request in time for the Board to be able to consider them at its 11 July meeting.

Benefits and risks of approach

19. The benefits of moving away from our previous approach are that we will:
 - reduce the regulatory burden on the AARs, in particular those that represent the lowest risk, by taking a more targeted approach to the process, in line with the better regulation principles
 - ensure that we do not duplicate our regulatory standards work
 - focus the AARs on areas that we were most concerned about last year
 - provide an opportunity for regulatory arms to highlight any issues that a strict form filling exercise might not allow for
 - have a process that is less time and resource intensive than previous years for both the LSB and the AARs.
20. The risks include:
 - We may be seen to be sidelining the AARs by seeking the response from the regulatory arms. However, the process will also provide for the AARs to give views on the regulatory arm's assessment and identify to the LSB where views may differ.

- We are changing a process that the AARs will be expecting us to follow. However, the fact that the process should be simpler and less resource intensive for the AARs should alleviate any concerns.
- We miss something important by asking specifically to update us on issues from last year. However, this year's process places the onus on the regulatory bodies to assess current and continued compliance with the IGRs, as well as how they intend to manage those risks. This approach will encourage the AARs to look forward, rather than back, and think about the effectiveness of the IGRs more independently.

Timetable and next steps

25 April	Board meeting to consider 2012 process and timetable
w/c 30 April	Subject to the Board's approval, letters sent to AARs requesting an update on compliance
31 May	Deadline for responses from AARs
June	Executive assess responses
11 July	Board meeting to consider assessment of compliance with IGRs for 2012

12.04.12