

To:	Legal Services Board	
Date of Meeting:	11 July 2012	Item: Paper (12) 46

Title:	Regulatory independence - 2012 assessment and future plans	
Workstream(s):	C: Statutory Decision Making	
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Status:	Protect	

Summary:

The focus of this year's regulatory independence exercise, the third undertaken by the Board to ensure compliance with its Internal Governance Rules 2009 (IGRs), has been to gain assurance that the formal arrangements that have been put into place over the past few years are ensuring independent regulation in practice. Each Applicable Approved Regulator (AAR), other than the Solicitors Regulation Authority (SRA), was provided with a tailored form seeking information about compliance and the risks to ensuring continued compliance with the IGRs, as well as an update on previously identified issues.

The paper recommends that the Board agrees that:

1. The Bar Standards Board (BSB) and Bar Council are assessed as potentially compliant with the IGRs, meaning that if the process and governance arrangements referred to in its response have the planned effect, they will be compliant.
2. The Costs Lawyers Standards Board (CLSB) and Association of Costs Lawyers (ACL) are assessed as compliant with the IGRs.
3. Intellectual Property Regulation Board (IPReg), the Chartered Institute of Patent Attorneys (CIPA) and the Institute of Trade Mark Attorneys (ITMA) are assessed as compliant with the IGRs.
4. ILEX Professional Standards (IPS) and the Chartered Institute of Legal Executives (CILEx) are assessed as compliant with the IGRs.

Following the Board's discussion about the IGRs process at its April meeting, the second part of this paper considers various options for the future of the IGRs process as we begin to develop a wider piece of work for consideration by the Board later in 2012.

Recommendation(s):
The Board is invited: (1) to agree the assessment that CLSB/ACL, IPReg/CIPA/ITMA and IPS/CILEx are compliant with the IGRs and that the BSB/Bar Council is potentially compliant (2) to provide comments about future plans for regulatory independence work.

Risks and mitigations
Financial: N/A
Legal: N/A
Reputational: N/A
Resource: N/A

Consultation	Yes	No	Who / why?
Board Members:	X		Barbara Saunders and Nicole Smith reviewed an earlier draft of the paper and their comments have been reflected (in the future plans section in particular).
Consumer Panel:	X		Elisabeth Davies and Steve Brooker reviewed an earlier draft of the paper and their comments have been reflected (in the future plans section in particular). Elisabeth is attending the meeting and so may speak on this item.
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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Regulatory independence - 2012 assessment and future plans

Context

1. This paper is presented in two parts:
 - An assessment of responses to the 2012 request for certification of compliance with the IGRs.
 - Following the Board's discussion about the future direction of the IGRs process at its 25 April 2012 meeting, an opportunity for the Board to provide early comments on the next phase of the independence process.
2. The full responses from the AARs will be available at the Board meeting. The responses and our assessments will be published on our website in due course.

Background – the 2012 exercise

3. Building on our experience of previous years', the 2012 process moved away from expecting AARs¹ to undertake a detailed assessment against the Schedule to the IGRs, which has been the template for the forms used in the past. The key focus of this year's exercise was to understand to what extent compliance with the IGRs are delivering regulatory independence in practice. The process of the dual self-certification was again used, albeit in a more focused way.
4. The exceptions to this approach were the SRA/The Law Society and CLSB/ACL. Given the ongoing reporting (under section 55 of the Act), we concluded that we should not seek a certificate from the SRA/The Law Society at this time. We are therefore relying on our ongoing, monthly monitoring of SRA/ The Law Society to track their progress towards achieving compliance with the IGRs. We will ask them to certify compliance when we reach a suitable point in the section 55 reporting process. However, they cannot be fully compliant until the SRA Board has a lay majority (from January 2013). We will report in more detail on our current assessment in the Autumn.
5. On 31 October 2011, the separation of the professional and representative arms of ACL was achieved when regulatory functions were delegated to CLSB. This meant that CLSB and ACL had not yet undertaken an assessment against the Schedule to the IGRs. We therefore asked them to undertake an assessment

¹ The AARs do not include the Faculty Office and the Council for Licensed Conveyancers, which have regulatory functions only.

against the full Schedule of the IGRs and submit a dual self-certificate as part of this year's process.

6. Unlike previous years, the request to the AARs was addressed to the regulators, with the professional bodies provided with the option of commenting on the regulator's assessment and counter-signing it.

Assessment of 2012 compliance

7. We have been pleased with the speed and relative ease of this year's process. Almost all of the AARs returned their responses within a month of the Board's request being issued. The responses provided to this year's process demonstrate how far the AARs have come in the past three years. There have been few issues or queries about the responses and we are satisfied that all of the AARs who have been involved in the process are either fully compliant with the Board's IGRs or potentially compliant, meaning that if the governance and processes described in the response have the intended effect, they will be compliant.
8. A summary of AAR responses and an assessment of their compliance with the IGRs is set out below.

BSB and The Bar Council

Background

9. The Board will recall that last year it had concerns about the BSB's control of resources. Specifically, the provision of access to the financial and other resources reasonably required to meet the strategy adopted by the BSB; effective control of those resources; and the BSB's freedom to govern all internal procedures. BSB committed to provide details of the new arrangements and how they were working in practice during this year's exercise. The Board also stated last year that it regarded "all options for action as open" in 2012 "should there be outstanding issues at that stage."

Summary of response

10. The BSB and Bar Council certified compliance with the IGRs.
11. Of note in the BSB's response were the following points:
 - The BSB has recently split its Finance and Audit Committee into two separate committees and has introduced a new finance manual. It believes that these changes should help ensure that there is appropriate independent control of resources and resourcing decisions. However, it did caution that vigilance may yet still be required.

- While the BSB has control over virement within its own budget envelope, that envelope is set by the Bar Council, with regulatory activity fitting into it, rather than being the starting point of decisions about budget.
- If the BSB underspends and the Bar Council needs funds to undertake a section 51 activity (a permitted purposes activity under the Act) then the BSB may not be able to keep any underspend.
- Service Level Agreements have been working “adequately” but need to be reviewed to operate more like contracts than is currently the case.
- A decision about a Chief Executive for the Bar Council is yet to be made.
- The response stated that the Board of the BSB makes “most” significant decisions itself. The BSB has clarified that where decisions are delegated to a committee, then a lay majority on the committee is required and in its view, there is no regulatory capture possible in its decision making.
- The Bar Council countersigned its agreement of the response. However, it used the opportunity to comment that it had some concerns as to whether the BSB always targeted regulatory activity at where action is needed “consequent upon the diversion of planned effort or resource caused by LSB initiatives.”

Assessment

12. We think that it is too early to say whether the BSB and Bar Council have achieved full compliance at this stage, given that new arrangements and processes are still to bed in, although the agreement of an increase in BSB resources in-year for 2012 and in its ongoing baseline in June is a promising sign. It is therefore recommended that the Board assess The Bar Council and BSB as **potentially compliant** provided that:
- the committee, governance and finance manual changes have the anticipated effect
 - the Service Level Agreements continue to develop in order to ensure more effective operation
 - the return of any monies to the Bar Council for section 51 purposes can only happen after the BSB has properly assured itself that it has what it needs for regulatory purposes.
13. The BSB’s comments about its budget arrangements could suggest that some of its necessary regulatory activities might not be undertaken because they do not fit into the “envelope” set by the Bar Council. While we recognise the need for adequate financial controls, there is a risk that the Bar Council’s financial constraints on the BSB mean that the BSB is compelled to undertake its business planning based on what it can afford to do within the Bar Council’s envelope. This is as opposed to planning its business based on what it should be doing to ensure that it is an effective regulator, working in line with the

regulatory objectives and ensuring the right outcomes for consumers of legal services.

14. There is a related risk that the BSB lacks all necessary resource to undertake its regulatory functions, in particular those that may arise in the year which may not have been anticipated. However, while there is nothing to suggest that any approaches to the Bar Council for additional resource have been declined, it is noted that the BSB has raised resource constraints as a reason for seeking slower timetables on some work the LSB expects to see happen. Resource will therefore be a key part of our regulatory standards work with the BSB and this specific point will be kept under review as part of that work.
15. We would not expect to see any changes arising from the decision about the Bar Council's Chief Executive when made to impact on IGR arrangements and would expect the BSB to refer to the LSB should it have any concerns about the arrangements.

CLSB and ACL

Background

16. CLSB and ACL were not compliant last year but were in the process of establishing a new regulatory function which had not been assessed against our IGRs. We therefore asked CLSB to complete a full assessment of compliance based on the Schedule to the IGRs.

Summary of response

17. CLSB and ACL certified that they were compliant with the IGRs. They also confirmed that they had set out fully under the four IGRs principles that provisions are in place which evidence independence and that no undue influence has been exerted by ACL on CLSB during the period October 2011 to May 2012, or indeed before.
18. CLSB and ACL provided a comprehensive assessment of compliance with the Schedule, which included evidence and supporting material.
19. Of note in the CLSB's response were the following points:
 - CLSB board members were appointed on one and two year terms. When those on one year terms came up for renewal they were only appointed for a further year meaning that the end of their new terms coincides with the end of those on two year terms. While ideally this would not have been the case, CLSB has confirmed that upon renewal of terms in 2013, the lengths will be reviewed and staggered. CLSB will consider Board composition at

its October 2012 meeting in order to ensure it has the right balance of skills, experience and continuity going into 2013

- The response did not seem to recognise that LSB concurrence was needed for any Board level dismissals. However, CLSB has confirmed that it took this as read.

Assessment

20. We had no concerns about the response and recommend that the Board assesses CLSB and ACL as **compliant**.
21. Areas that we will note in the assessment letter include the terms of appointment and dismissal points raised above, as well as also noting positively the speed with which the response was returned.

The Intellectual Property Regulation Board (IPReg), Chartered Institute of Patent Attorneys (CIPA) and Institute of Trade Mark Attorneys (ITMA)

Background

22. Last year's LSB assessment highlighted the recently established approved regulator forum and the revised delegation agreements as areas where we would seek an update on in 2012.

Summary of response

23. IPReg, CIPA and ITMA certified that they were compliant with the IGRs.
24. IPReg reported that in its view, the new forum was working very well and has provided a forum to consider matters such as the 2012 budget, business plan, financial reports and policy matters relating to IPReg's licensing authority application.
25. A new general delegation agreement and a delegation agreement for IPReg's ABS work have been agreed. As part of the new arrangements ITMA and CIPA observers will be invited to attend the IPReg Board as observers.
26. IPReg provided a full assessment of how oversight by the Institutes is in line with the principles of the IGRs, providing examples for each of the IGRs principles of governance, appointments, strategy and resources and oversight. It did not consider there to be any risks to continued compliance with these principles.
27. CIPA and ITMA commended the work of IPReg so far on ABS. They also agreed with the assessment that the new approved regulator forum had improved liaison and understanding between the regulator and the professional

body. However, thought that this needed to be developed further and a joint sub-committee should be considered.

Assessment

28. We had no concerns about the response and recommend that the Board assesses IPReg, CIPA and ITMA as **compliant**.
29. The assessment letter will welcome the improvements that have been made this year. We also intend to note that while we welcome collaborative working between the regulator and the professional body, we would caution about the risk of affecting compliance with the IGRs should it ever come to exercise decision making powers. We may seek an update on the operation of any sub-committees next year, should any have been established.

Institute for Legal Executives Professional Standards (IPS) and the Chartered Institute for Legal Executives (CILEx)

Background

30. We did not identify any areas of concern in IPS' IGRs assessment last year.

Summary of response

31. At the time of preparing this paper, CILEx had not counter-signed the response as it wished to consider it at its 6 July meeting. We will therefore report orally at the Board meeting on any additional comments received from CILEx. We expect IPS and CILEx to certify compliance with the IGRs.
32. IPS provided a full assessment of how oversight by CILEx is in line with the principles of the IGRs, providing examples for each of the IGRs principles of governance, appointments, strategy and resources and oversight. It did not consider there to be any risks to continued compliance with these principles.

Assessment

33. We had no concerns or comments to make about the response and recommend that the Board assesses CILEx and IPS as **compliant**, subject to any comments from CILEx, which will be reported at the Board meeting.

Next year and beyond

34. We have now completed three years of IGR dual self-certificates for most of the AARs. Since 2010 we have seen good (if not quite complete) progress among each of the AARs and established a process which is on the whole readily accepted by them, as evidenced by the prompt response from the AARs this year.

35. Dual self-certification has been a valuable process that engages both the professional body and the regulator, causing them to think carefully about whether the arrangements that have been put in place deliver independence in practice.
36. Using a template that covers all elements of the IGRs for the first (and possibly second) assessment is a good approach and should continue for new AARs. It is particularly suited to ensuring that appropriate governance arrangements are in place, and also to some degree for identifying the most egregious transgressions of the principle of independent regulation.
37. It is worth noting that we would expect new AARs to be compliant with the IGRs at the point of designation, given that under Schedule 4, section 13 (2)(a) of the Act, if a designation order were made in relation to a body, the applicant would have “appropriate internal governance arrangements in place at the time the order takes effect.” However, it may be that we need to give further consideration to an appropriate approach for any regulator of special bodies.
38. Our particular interest in independence is because of its role in underpinning regulation that is risk based and consumer focused, rather than profession dominated. Thus independence is as much about independence from the *regulated community* as it is about independence from the *professional body*. Just as important is that there is a perception of independence held by both consumers and the profession. A more targeted approach to ensuring independent regulation, linked to our increasing knowledge about the regulatory effectiveness of each regulator will allow us to ensure that the dual self-certificate process is directly linked to our strategic priorities² and that regulation is in the public interest.
39. Dual self-certification therefore should continue but – as with this year – it should be focused on those areas (either relevant to all or some AARs or individual issues) that pose a risk or barrier to this wider independence. As part of this move to better target our approach to independence, the LSB, the regulators and the professional bodies will need to better define the role of the regulator and the professional bodies, perhaps through linking roles to permitted purposes under Section 51 of the Act. Defining what we mean by the proper roles of regulators and professional bodies would also help ward off any accusations of overstepping our remit.
40. A more targeted approach could include consideration of issues, including:

² Our strategic priorities for 2012-15, as set out in our *Strategic Plan 2012-15 and Business Plan 2012/13* are: assuring and improving the performance of approved regulators, helping consumers choose and use legal services with confidence and helping the changing legal sector to flourish by delivering appropriate regulation to address risks.

- Is the Board of the regulator operating within its terms of reference (and in particular, not stepping into professional matters)? Conversely, is the professional body straying into regulatory matters?
- How effective are the Chairman and/or Chief Executive? Are they credible as exemplars of independent regulation ?
- Should there be a set of core Board competencies that we expect to see met? How can we be assured of the quality and capacity of the Board?
- Should there be a mandatory requirement for the Boards of the regulators to have a lay Chair?
- What is the composition of the committees of the Board and how does this relate to their functions?
- How best can we assure ourselves of the effectiveness of the regulatory board in its oversight of the regulator's *staff*? And of the Approved Regulator in its oversight of the regulatory *board* ?
- Does the regulator have people (notably the senior management team) who are able to deliver effective regulation?
- Does the regulator have freedom to set and spend its agreed budget in whichever way it considers necessary to deliver its regulatory functions?
- In terms of timing, should we link the self-certification process to the timetable for gaining approval for practising certificate fees?
- What other factors might affect independence – e.g. financial influence of/reliance on a significant player(s) in the regulated community?
- How do regulators ensure and measure public confidence in them and their independence? What about the confidence of those they regulate?
- Are there signs of co-ordination between the regulatory body and the professional body on policy, for example joint or similar responses to consultations?
- What evidence is there of consumer engagement to indicate a focus on consumers, rather than the profession?

41. In practice, it may be that approaches to these issues may be better expressed as indicative behaviours to an outcome specified by the Board, rather than as an expanded set of rules.
42. It is envisaged that gathering the evidence to inform our assessment would be a year-round process, based on a variety of sources, such as speeches, media monitoring, colleague input and the evidence that we collect as part of our regulatory standards work. It may be that in certain instances, we would have enough information from our wider work to form our own conclusion about a regulator's independence.
43. Given this broader perspective, we will need to consider how far independence per se remains a discrete focus or whether it will instead evolve into an important underlying contextual concern in our assessments of regulatory performance.
44. We will develop our thinking over the coming months with a view to bringing a more detailed proposal to the Board in winter 2012/13. In particular, we will

need to focus on how we communicate and consult upon a new approach. At this stage we invite the Board to comment on issues noted above and offer any other matters that we should take into account.

45. A new and more dynamic approach to ensuring independent regulation is most likely to be a forward looking activity starting with next year's round of self assessment and being developed and embedded into regulators over the subsequent year(s) rather than be a one off assessment of the previous year.

Next steps

46. The Board is asked to agree the assessment of each AAR's compliance with the IGRs. Subject to the Board's agreement, we intend to issue our assessment letters within the next week.
47. The Board is also asked to consider and provide comments on proposals for next year and beyond, before considering a more detailed proposal later in 2012. We do not envisage publicising a new approach to the IGRs until after SRA has achieved compliance, expected in January 2013.