

Independent regulation of legal services

Crispin Passmore, Strategy Director

Regulatory Policy Institute, 26th April 2013

I will give you a short overview of independence in practice in the new regulatory environment for legal services.

Independent regulation of legal services

Why Independent?

It is important to remember why we focus on independence.

Independent regulation of legal services

Because otherwise vested interests...

And the answer, I think, is pretty stark.

Drivers of change in the legal sector

A lack of independence in regulation characterised by...

- Collapse of confidence in self-regulation
- Perceived anti competitive restrictions
- The ‘regulatory maze’
- Regulatory failure in complaints-handling
- Market developments

Result → Legal Services Act 2007.

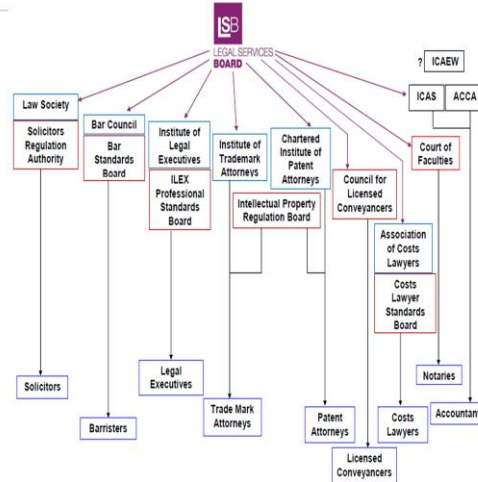
So some context...

- Legal services traditionally regulated by their own professional bodies, such as Law Society and Bar Council
- Since the 1980s Government has tried to introduce and encourage competition, encouraging new legal professional such as conveyancers and legal executives
- But by 2001 OFT was concluding that there were real barriers to competition in Legal and other professional markets
- David Clementi reviewed regulation of the legal sector in 2004 – challenging the artificial distinction between professions and business, saying to lawyers “If you don’t think that you are in business then you will not be for long.”
- Poor complaints handling over many years frustrated parliament and consumer groups alike
- And the complexity of so many different legal regulators with different standards and expectations confused everyone but the most determined
- It was clear that self regulation threatened innovation, undermined competition, and didn’t take advantage of technology as it relied on old and outdated modes of production
- The Legal Services Act 2007 had cross party support: reform was coming.

One result of LSA 2007 → Legal Services Board



- Oversight regulator for the sector
- **Independent** of both the profession and government
- Paid for by levy on lawyers
- Duties and enforcement powers
- Small – staff of 30, budget reduced from £5m to £4.5



So what happened to the regulatory maze and professional regulation?

Well.... it got more complicated!

- The Legal Services Board created by the Legal Services Act at the apex of the regulatory system – there to secure the regulatory objectives in line with the better regulation principles.

AND

- The professional bodies had to separate their representative and regulatory functions

A new ombudsman was mandated by statute to better handle complaints independent of the profession. And the restrictions on external investment in and ownership of law firms were to be dismantled.

The shift away from regulation that was perceived as protecting lawyers towards a clear focus on independence was set.

Priorities

First three years 2009-12

- Liberalising ownership through *alternative business structures*
- Establishing an independent Legal Ombudsman
- Separation of regulation within professional bodies

Current priorities 2012-15

- Improving and assuring performance of legal regulators
- Simplification of regulation to support growth and innovation
- Better consumer protection where needed

So how have the LSB tackled the task we were set?

We could have focused only on architecture, set-up and bedding in the new regime – especially in the first couple of years. But LSB aggressively pursued the task it had been given by Parliament – tackling all three priorities it set itself in tandem, ahead of schedule.

- Alternative business structures means letting law firms float on stock market, allowing foreign ownership of law firms, seeing private equity and venture capital come into the law, but also mutuals, such as the Co-Op and multi disciplinary approaches that combine legal services with accountancy, tax advice, business and management advice.
- The Legal Ombudsman opened its doors ahead of parliamentary expectation in 2010
- And the LSB insisted on steps towards separation of regulation from representative influence even before it had taken on its powers fully

As we moved into our second three year period, past the architectural reform, we avoided a steady state mentality: now we are focused on the heart and soul of the act and that demands independent regulation as a foundation.

- We have set out standards for the regulators to self assess against, and offered our own commentary on that self assessment.
- All accept that there is some way to go before regulation is satisfactory.
- And we are starting to tackle the costs and complexity that arises from the self regulatory history – but it is rooted in the culture of the sector as much as the legislation and rule book.

Back to independence – but independence from whom?



- Government?
- Parliament?
- Executive?
- Regulators?
- Courts and Judges?
- Professional bodies?
- Financial and legal business interests?
- Consumer and consumer bodies?

However...

*Independence does not
mean an accountability free
zone...*

So who do we want regulators to be independent from? Which vested interests?

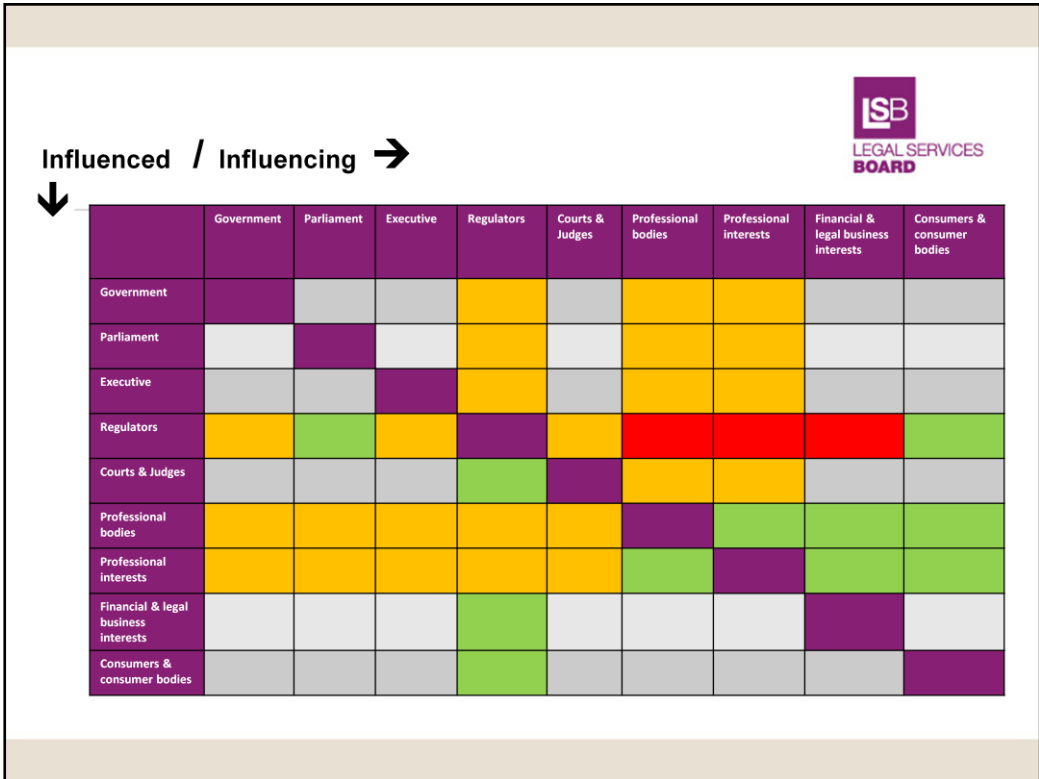
Is it the same in every sector of the economy?

Well in law, perhaps we have to add in courts and judges, issues related to the rule of law and administration of justice in the public interest?

Are these significantly different to the usual concerns (in other markets) about independence from producer, consumer and government interests?

It seems to me that the possibility of undue influence between all stakeholders is dynamic, subtle and never quite pinned down, and more about undue influence than loaded words like capture.

But we can try to understand it and spot risks in practice as well as theorise.



So a simple attempt to identify and map where the risk is greatest.

Remembering that influence and independence works in each direction we can try and map who influences who – and from that spot where we see risk of inappropriate influence or a threat to independence.

Of course, none of the actors on this stage exist free from influence or are pure of thought. We could carry on filling in the boxes, each coming to a different view as to where risk lies.

But the LSB takes the view that the reddest risks arise from the influence of business, lawyers and representative bodies on their regulators.

So we focus on these most of all, while trying not to lose sight of other risks.

The biggest risk to independent regulation...

Threat to regulators' independence from inappropriate professional interest

Why it matters...

- Competition and open market issues
- Public interest
- Proper administration of justice
- Rule of law
- Others?

Why are these risks the ones we see as most serious?

Well, it keeps taking us back to the problems of self regulation:

- Resistance to removal of barriers to entry
- Focus on titles rather than risk
- A hierarchy of ethics and goodness with lawyers at the top non lawyers further down and, probably regulators relegated to the second division.
- A confusion as to what is in the public interest

As an aside, I am always surprised how often the public interest as put forward by some parts of the legal profession appears, amazingly, to coincide with the professions particular interests.

All of this matters – not just for the integrity of the legal market but for regulation in other sectors, the economy and society. It is hard to envisage effective regulation of the economy without the rule of law and proper administration of justice; and that requires a functioning legal market – though that is a long way from equating the rule of law with the rule of lawyers!

The biggest risk to independent regulation...

Front line regulators are not wholly independent of professional interest

- Regulators' Boards dominated by lawyers
- Predominantly lawyers from that sector of legal market (solicitor, barrister, legal executive etc) involved at Board and exec levels
- Cultural ties and norms are those of the specific part of legal market
- Rule books are rooted in sector history and passported by legislation as 'good enough'
- Some lack of regulatory and economic understanding at regulators
- Still accountable to their master Approved Regulator/professional body
- Prevailing focus still on individual professional rather than entity behaviour

So how do the risks manifest themselves?

That the Legal Services Act did not fully separate regulation from representation and professional bodies has had an undoubted impact.

You can see that the profession still has a significant role in many aspects of regulation.

And the Legal Services Act passported all the old self regulation models into the new regime, treating them as if they have been approved by the LSB - meeting the standards and requirements of the modernised regime.

That was, in my view, a mistake; a missed opportunity to deliver properly independent regulation.

When we add together these issues, especially the impact on the culture of the regulators, I worry how independent regulation actually is.

LSB independence also an issue?

LSB independent of Government and Professional bodies/regulators

- LSB is an NDPB, not a statutory body or non-ministerial department
- Government proposes legislation, appoints Chairman and Board
- Select Committees may undertake pre-appointment scrutiny next time
- Almost half LSB Board is lawyers
- Professional bodies' relationships with Government & Parliament
- CEO is Accounting Officer and so could be challenged by MoJ Perm Sec

But some worry that the LSB itself is not independent.

Are we too close to Government? Are we too close to consumer interests?

Certainly some of our front line regulators and their professional bodies think so. And they are not afraid of telling Government so – you may spot an irony in the legal profession that asserts its independence so strongly quietly asking Government to reign in an independent regulator!

But I would ask if the sorts of issues on this slide are evidence of a lack of independence or part of proper public scrutiny and accountability?

Checks and balances that mitigate risk...

- Lay Chair and lay majority of LSB Board
- Nolan compliant appointment of LSB Chair and Board
- Lord Chief Justice approval of appointment of LSB Chair and Board

- Professional bodies have to separate regulation from representation
- Lay majority on regulators' boards, possibility of lay Chairs
- Decision about regulation made in line with better regulation principles
- Regulators share regulatory objectives
- LSB at apex of regulatory structure with significant duties and powers

We try to mitigate the biggest risks.

- So the LSB is appointed and structured to minimise political or professional interference
- And the structure - the LSB role at the head or apex of the system – tries to minimise undue professional influence of independent regulation.

The key to me is how the LSB acts and the standards it sets and demands from the regulators – that is what will help secure their independence of thought – but they have to want to be free!

Legal services regulatory objectives

Why it matters...

- Protecting and promoting the public interest
- Supporting the constitutional principle of the rule of law
- Improving access to justice
- Protecting and promoting the interests of consumers
- Promoting competition in the provision of services
- Encouraging an independent, strong, diverse and effective legal profession
- Increasing public understanding of the citizen's legal rights and duties
- Promoting and maintaining adherence to the professional principles

And the regulatory objectives – set out in Section One of the Legal Services Act – are applied equally to the LSB and the front line regulators.

This shared endeavour should ensure that oversight and front line regulators do not pull in different directions.

So the LSB set out what it thinks these mean in practice; while no other regulator has matched that.

Current risks

Front line regulators independent of professions and professional bodies	however...	LSB not worried about independence from Government
<ul style="list-style-type: none"> - Capture by special interests - Loaded Board make up - Culture - Structural complexity - Legislative overlap 		<ul style="list-style-type: none"> - Referral fees - Damage based agreements - QASA - ABS authorisation - Will writing - Board appointments - Government has not tried to interfere

Given all of that, where do we think we are in securing independent regulation?

Structurally the act fudges these issues, keeping complexity and building in real risks of undue professional influence.

And culturally the legal regulators remain rooted in history, rooted in their part of the profession.

But the LSB isn't captured by Government.

- We make decisions that Government disagrees with
- Government took a different view to LSB on referral fees
- And is not bound to follow our recommendation on the regulation of will writing
- We deliver our statutory functions not government policy
- And when the regulators or professional bodies run to Government to complain about our regulatory activity, Government does not interfere.

Should we be worried about a threat to our independence?

- **Yes...** It's incredibly difficult, almost like running through treacle, to deliver a changed legal market
- **No...** running through treacle is something we've gotten very good at doing.

So push me into an answer – am I worried about independence or not?
Well 'yes', and 'no'.