



Summary of Decision

The following table is a high level summary of the decision of the Legal Services Board. It is not a formal part of the decision notice.

Purpose of notice
To grant an application from CILEx Regulation approving alterations to its regulatory arrangements in respect of the CILEx Regulation Compensation Arrangements (previously the CILEx Compensation Fund Rules.)
Alterations that are being approved by this decision
There are a series of alterations which are set out in more detail in the notice itself. However, the overall purpose of the changes are to transition the CILEx Regulation compensation fund to a largely insurance backed compensation scheme.

Decision notice

Issued by the Legal Services Board under Part 3 of Schedule 4 to the Legal Services Act 2007

CILEx Regulation's application for approval of changes to its regulatory arrangements in respect of the CILEx Compensation Fund Rules.

The Legal Services Board (**LSB**) has granted an application from CILEx Regulation which approves alterations to the regulatory arrangements in respect of the CILEx Compensation Fund Rules. The Chartered Institute of Legal Executives (**CILEx**) is an approved regulator and CILEx Regulation is the regulatory arm to which CILEx has delegated its regulatory functions.

This decision notice sets out the decision taken, including a brief description of the changes. The notes at the end of this notice explain the statutory basis for the decision. The chronology for the LSB's handling of this application is set out at the end of this decision notice.

Proposed changes

1. CILEx Regulation proposed a series of alterations for the overall purpose of transitioning the CILEx Regulation compensation fund to a largely insurance backed compensation scheme.
2. A summary of the specific changes are as follows:
 - Re-naming the rules as the CILEx Regulation Compensation Arrangements.
 - Introducing provisions to enable CILEx and CILEx Regulation to put arrangements in place to use an insurance policy to fund compensation claims made by clients of CILEx regulated entities.
 - Introducing eligibility requirements to limit access to the fund to consumers, a trustee of a trust with a net asset value of less than £2 million, and any other persons with income (including turnover after the deduction of tax) of less than £2 million per annum.
 - Limiting access to misappropriations and failures where there is some aspect of dishonesty a CILEx regulated entity has acted dishonestly in the course of providing Legal Services.
 - Introducing an aggregate limit of £2 million on the total value of claims which can be made in respect of one CILEx regulated entity.
 - Introducing an exceptional circumstances discretion to allow time limits for the receipt of claims under the scheme to be extended.
 - Listing the criteria that CILEx regulation may apply (and set out in separate, detailed guidance) in deciding whether to grant compensation on a discretionary basis. Such criteria includes reference to the making of grants on an interim basis.

- Introducing an additional requirement for claimants to pursue lost monies from third parties, as well as CILEx regulated entities before a claim is made on the fund.
- Introducing a provision allowing requirements for pursuing lost monies from CILEx regulated entities and third parties to be waived where an interim grant is being made or there is no reasonable prospect of recovering the monies in question, or where it would be unreasonable to expect an applicant to pursue one or all of the steps in question.
- To formally specify CILEx Regulation's ability to delegate part or all of its functions under the new rules to staff members or other persons.
- Improving clarity through a number of stylistic and drafting changes.

Key issues considered in the assessment of the application

3. The LSB broadly welcomes CILEx Regulation's approach in making these changes. We noted and welcomed CILEx Regulation's willingness to consider concerns received in consultation responses in preparing the final version of its application.
4. The LSB sought assurance on a number of issues in its assessment, which included:
 - Consumer protections, and
 - The availability of insurance

Consumer protections

5. The Legal Services Consumer Panel raised some concerns about the impact upon consumers in its response to the consultation about the proposed changes.
6. CILEx Regulation set out the following in its application:
 - CILEx Regulation holds the view that the revised proposals will have a positive impact upon consumer protection. It advised that, by comparison to seeking to grow a compensation fund with a low number of CILEx authorised entities, an insurance backed scheme would provide a greater level of consumer protection.
 - CILEx Regulation cited examples of where the proposals have clarified or enhanced consumer protection, including the provision of an exceptional circumstances criterion on the application of the time limit for making a claim.
 - CILEx Regulation also identified that it considered the introduction of an eligibility criteria, and an aggregate limit for claims per firm to be likely to have a neutral impact on consumer protection. Further, it considered that the risk of any negative impact on consumers was justified by the benefits of the proposals, which included the desire to ensure a sustainable entity based regime in the interests of competition in the legal services market.

Availability of insurance

7. The LSB sought assurance on the availability of insurance in its assessment. The proposed amendments to the rules make payment of a grant subject to the sum being paid by the insurers. The LSB sought clarity from CILEx Regulation about whether any mechanisms have been put in place to mitigate the risk of a dispute occurring between the insurer and CILEx Regulation about a claim, and for resolving such a dispute should it occur.
8. CILEx Regulation set out the following in its response:
 - CILEx Regulation acknowledged there was a remote risk that a dispute could arise between CILEx Regulation and the insurer about awarding a claim. It was identified the rules had been drafted to provide transparency about this risk, however CILEx Regulation advised it could not envisage a scenario where this would occur. CILEx Regulation further advised that its insurance broker is not aware the selected insurance provider has ever refused to pay a claim, despite insuring this and other compensation funds for many years.
 - To mitigate the risk of a dispute occurring, CILEx Regulation confirmed that it had engaged with the insurance provider to ensure that the potential scenarios for claims are understood. CILEx Regulation also stated that it worked with its insurance broker to ensure the wording of the contract, as far as possible, minimises the likelihood of a dispute. CILEx Regulation also stated that its insurance broker had advised that as the wording of the policy was fully agreed by the insurer, the risk of a dispute was reduced.
 - In response to the LSB's query about resolving disputes that may arise, CILEx Regulation advised that the processes in place within the insurance industry to resolve complaints are considered appropriate. In light of this, CILEx Regulation stated that its broker had confirmed that it would not be necessary to include any mediation provisions within the policy.
9. In assessing the application, the LSB also raised some drafting queries which CILEx Regulation was able to resolve.

Decision

10. The LSB has considered CILEx Regulation's application against the criteria in paragraph 25(3) of Schedule 4 to the Legal Services Act 2007 (the Act) and has decided to grant the application.
11. The annex to this decision notice contains the specific amendments to CILEx Regulation's regulatory arrangements as approved by the LSB.

Chronology

- The LSB confirmed receipt of an application from CILEx Regulation on 20 July 2017.
- An extension notice was issued for the application on 16 August, extending the decision period to 7 September 2017

LSB decision notice 18 August 2017

- This decision notice is effective from 18 August 2017.
- The decision notice will be published on our website within the next two business days of the date of this notice.

Neil Buckley, Chief Executive of the Legal Services Board
18 August 2017

Notes:

1. The LSB is required by Part 3 of Schedule 4 to the Act to review and grant or refuse applications by approved regulators to make alterations to their regulatory arrangements.
2. Paragraph 25(3) of Schedule 4 to the Act explains that the LSB may refuse an application setting out a proposed change to the regulatory arrangements only if it is satisfied that
 - (a) granting the application would be prejudicial to the regulatory objectives
 - (b) granting the application would be contrary to any provision made by or by virtue of this Act or any other enactment or would result in any of the designation requirements ceasing to be satisfied in relation to the approved regulator
 - (c) granting the application would be contrary to the public interest
 - (d) the alteration would enable the approved regulator to authorise persons to carry on activities which are reserved legal activities in relation to which it is not a relevant approved regulator
 - (e) the alteration would enable the approved regulator to license persons under Part 5 [of the Act] to carry on activities which are reserved legal activities in relation to which it is not a licensing authority, or
 - (f) the alteration has been or is likely to be made otherwise than in accordance with the procedures (whether statutory or otherwise) which apply in relation to the making of the alteration.
3. The designation requirements referred to in paragraph 2(b) above are set out in paragraph 25(4) of Schedule 4 to the Act and are
 - (a) a requirement that the approved regulator has appropriate internal governance arrangements in place
 - (b) a requirement that the applicant is competent, and has sufficient resources to perform the role of approved regulator in relation to the reserved legal activities in respect of which it is designated, and
 - (c) the requirements set out in paragraphs 13(2)(c) to (e) of Schedule 4, namely that the regulatory arrangements are appropriate, comply with the requirements in respect of resolution of regulatory conflict (imposed by sections 52 and 54 of the Act) and comply with the requirements in relation to the handling of complaints (imposed by sections 112 and 145 of the Act).
4. In accordance with paragraphs 20(1) and 23(3) of Schedule 4 to the Act, the LSB has made rules¹ about the manner and form in which applications to alter regulatory arrangements must be made. Amongst other things, the rules highlight the applicant's obligations under section 28 of the Act to have regard to the Better Regulation Principles. They also require applicants to provide information about each proposed change and details of the consultation undertaken.
5. If the LSB is not satisfied that one or more of the criteria for refusal are met, then it must approve the application in whole, or the parts of it that can be approved.

¹ Rules for Rule Change Applications – Version 2 (November 2010)

CILEx REGULATION COMPENSATION ARRANGEMENTS FUND RULES

Introduction

1. (1) These are the CILEx Regulation Compensation ArrangementsFund Rules.
- (2) These rules are made by CILEx under ~~articles 3 and 4 of~~ the Legal Services Act 2007 (Chartered Institute of Legal Executives) (Modification of Functions) Order 2014.
- (3) These rules came into force on 5th January, 2015 and were subject to changes on [insert date of new changes coming into force].
- (4) Responsibility for the application and administration of these Rules and of the Fund is delegated by CILEx to CILEx Regulation.

Interpretation

2. In these Rules, unless otherwise provided:

Applicant: means a person applying for a Discretionary Grant;
Authorised Entity: means a partnership (including a limited liability partnership), company or sole principal authorised by CILEx under the Legal Services Act 2007 to:
(a) carry on an activity which is a Reserved Legal Activity ~~reserved legal activity~~; or
(b) provide immigration advice or immigration services;

and where the context permits, references to acts or omissions by such a body shall include the acts or omissions of such a body's principals (including the partners in a partnership, the members in an LLP or the directors in a company) and employees;

CILEx: means the Chartered Institute of Legal Executives;
CILEx Regulation: means Cilex Regulation Ltd;
Compensation means a contract of insurance taken out pursuant to rule 3(2)(a);
Insurance Contract

Consumer: means an individual acting for purposes which are wholly or mainly outside of that individual's trade, business, craft or profession;

Discretionary Grant: means a ~~D~~iscretionary ~~G~~rant made ~~by CILEx~~ under Rule ~~5-6~~(1)(a) or (b) out of the Fund or with a view to

<u>Eligible Person:</u>	<u>payment being made by virtue of a Compensation Insurance Contract;</u>
<u>the Fund:</u>	<u>has the meaning given in rule 6(5);</u> <u>means the CILEx Compensation Fund as described in rule 4;</u>
<u>Legal Services</u>	<u>do not include:</u> i) <u>practising as an employee of an employer other than a sole principal or entity regulated by CILEx Regulation; or</u> ii) <u>discharging the functions of any of the following offices or appointments:</u> <u>a) judicial office;</u> <u>b) Under Sheriffs;</u> <u>c) members and clerks of such tribunals, committees, panels and boards as the CILEx Regulation Board may from time to time designate but including those subject to the Tribunals and Inquiries Act 1992, the Competition Commission, Legal Services Commission Review Panels and Parole Boards;</u> <u>d) Justices' Clerks; or</u> <u>e) Superintendent Registrars and Deputy Superintendent Registrars of Births, Marriages and Deaths and Registrars of Local Crematoria.</u>
<u>Person</u>	<u>includes a body of persons corporate or unincorporated;</u>
<u>Qualifying Insurance:</u>	<u>has the meaning given in Rule 1(2) of the CILEx Professional Indemnity Insurance Rules;</u>
<u>Regulated Legal Activity</u> regulated legal activity:	means:
<u>Reserved Legal Activity</u> reserved legal activity:	(a) a <u>Reserved Legal Activity</u> reserved legal activity; or (b) immigration advice or immigration services; and has the same meaning as in the Legal Services Act 2007.

Compensation Arrangements ~~The Fund~~

3. (1) CILEx shall establish and maintain compensation arrangements in accordance with these rules.
- (2) For the purposes of rule 3(1), compensation arrangements shall include arrangements for the funding of discretionary grants under rule 6 by one or more of the following:
 - (a) insurance provided by an authorised insurer (within the meaning of section 64

(4) of the Legal Services Act 2007);
(b) the Fund.

The Fund

- ~~4.3~~(1) CILEx must establish and maintain the CILEx Compensation Fund (the Fund) which is to be applied to the payment of Discretionary Grants and for the other purposes provided for under these Rules.
- (2) Every Authorised Entity must make contributions to the Fund. CILEx~~X~~ may from time to time prescribe the rate and amount of, and payment arrangements for, those contributions which may include provision for different payments to be made by different descriptions of Authorised Entity.
- (3) Any contribution which is not paid in accordance with ~~paragraph rule 4~~(2) may be recovered by CILEx as a debt.

Management of the Fund

- ~~5.4~~ (1) The Fund ~~shall is to be~~ held, managed, administered and distributed by CILEx Regulation, which may in particular:
- (a) make discretionary grants from the Fund in accordance with rule 6~~hold and distribute any monies raised for the purposes of the Fund;~~
 - (b) invest the Fund in any investments in which trustees may invest under section 3 of the Trustee Act 2000 (general power of investment) as restricted by sections 4 and 5 of that Act;
 - (c) insure in relation to the Fund, and pay premiums in respect of such insurance from the Fund, for such purposes and on such terms as it considers appropriate (including for the avoidance of doubt in respect of a Compensation Insurance Contract);
 - (d) borrow for the purposes of the Fund, pay interest on any money so borrowed, repay any money so borrowed and use investments or other property which form part of the Fund as security for such borrowing; and
 - (e) use the Fund to pay any ~~other~~ costs, charges or expenses properly incurred by CILEx in establishing and administering the Fund (which may include such liabilities incurred by persons appointed to manage and administer the Fund on behalf of CILEx).
- (2) The payments which may be made under ~~paragraph rule 5~~(1)(e) include any expenditure, including the payment of any award of costs or damages, incurred by CILEx, CILEx Regulation, their employees or agents as a result of proceedings against any of them for any good faith act or omission in the exercise or purported exercise of powers under these Rules.

- (3) [For the avoidance of doubt, CILEx Regulation may delegate part or all of its functions under these rules to staff members or other persons appointed for this purpose. Any such delegation must be in writing.](#)

Discretionary Grants

- ~~6.5.~~ (1) ~~The Fund may be used by~~ CILEx Regulation ~~may to~~ make Discretionary Grants to [Eligible p](#)Persons ~~who are clients of Authorised Entities~~ to
- (a) [compensate \(in whole or in part\) for losses suffered as a direct consequence of a dishonest misappropriation or a dishonest failure to account by an Authorised Entity in the course of providing to that person Legal Services of a type which that entity was authorised by CILEx Regulation to provide](#) ~~replace money which an Authorised Entity has misappropriated or for which an Authorised Entity has otherwise failed to account~~; or
 - (b) compensate [\(in whole or in part\)](#) a person in respect of the civil liability of an Authorised Entity which, contrary to the CILEx Professional Indemnity Insurance Rules, does not have in place a policy of qualifying insurance against which a claim in respect of that civil liability can be made.
- (2) A grant may not be made [in excess of funds available under these compensation arrangements or in](#) respect of any loss:
- (a) arising solely by reason of the professional negligence of an Authorised Entity;
 - (b) which is a personal debt or trading debt or liability of an Authorised Entity;
 - (c) arising from practice by the Authorised Entity outside of England and Wales;
 - (d) which is a claim for interest under a contract between the Applicant and an Authorised Entity; ~~or~~
 - (e) which did not arise from the provision of legal services performance or purported performance by an Authorised Entity of a regulated legal activity that it is authorised by CILEx to undertake;
 - [\(f\) arising from the provision of services by an individual \(including authorised individuals\) other than through a sole principal or entity authorised by CILEx; or](#)
 - [\(g\) where the other requirements for making a Discretionary Grant under these rules have not been satisfied, including in particular as regards the Applicant suffering loss and hardship \(rule 7\(2\)\) and where other remedies may be available \(rule 8\).](#)

- (3) Discretionary Grants may be made:
- (a) on an interim basis;
 - (b) subject to payment being received from an insurer pursuant to a Compensation Insurance Contract.
- (4) CILEx Regulation shall publish guidance as to the criteria to be applied in deciding whether to make a Discretionary Grant. Such guidance may include:
- (a) the circumstances in which it might be appropriate for the time limits for making an application under these rules to be extended;
 - (b) a requirement for decision makers to take account of the affordability of each application in the context of maintaining the Fund in appropriate cases;
 - (c) guidance on when and how to distribute monies on a pro rata or nominal basis;
 - (d) a requirement for decision makers to take account of the terms of any relevant Compensation Insurance Contract;
 - (e) guidance on making use of interim grants;
 - (f) guidance on acts or omissions on the part of an Applicant which may result in a claim being refused or reduced, including where the conduct of the Applicant has contributed to the loss and where the Applicant has not provided full cooperation during the course of the application;
 - (g) guidance on assessing eligibility under these rules, including the need to take a broad approach in the context of calculating assets and income and to take account of assets held or income received by any parent undertaking;
 - (h) guidance on making use of interim grants in circumstances where there is a significant risk that the aggregate limit set for grants per Authorised Entity under rule 9(2) will be met and the period of time after which final grants should ordinarily be made.
- (5) For the purposes of rule 6(1), a person is eligible if that person is a client or former client of the Authorised Entity and is:
- (a) a Consumer; or
 - (b) a trustee of a trust with a net asset value of less than £2 million; or
 - (c) any other person who has annual income in the last accounting year (including annual turnover after the deduction of tax) of less than £2 million.
- (6) Any Discretionary Grant is to be made in the absolute discretion of CILEx Regulation and no person has a legally enforceable right to any grant.

Applications

- ~~7.6.~~ (1) An application for a Discretionary Grant must be made:

- (a) in the form CILEx Regulation may from time to time prescribe; and
 - (b) ~~made promptly and in any event, save for exceptional circumstances,~~ not more than one year after the Applicant first knew, or with reasonable diligence should have known, about the misappropriation, failure to account or events giving rise to a civil liability (as the case may be).
- (2) An Applicant must provide evidence to satisfy CILEx Regulation that, in consequence of the misappropriation, failure to account or events giving rise to a civil liability (as the case may be), the Applicant has suffered or is likely to suffer loss and hardship.
- (3) The Applicant has the burden of proving a claim and must provide CILEx Regulation with such documents or other information as it may require in respect of that claim (though for the avoidance of doubt satisfaction of such requirements does not give a person a legally enforceable right to any grant).
- (4) Failure to provide documents or other information or to co-operate with CILEx Regulation may be taken into account when determining the merits of an application.

Other Remedies and Subrogation

- ~~8.7.~~ (1) A Discretionary Grant may be refused in respect of all or any part of a loss that is:
- (a) an insured risk; or
 - (b) capable of being made good by any other means.
- (2) Before deciding whether to make a Discretionary Grant and subject to exercising its discretion under rule 8(4) below, CILEx Regulation ~~may~~ shall require an Applicant to:
- (a) pursue any civil remedy against: ~~the Authorised Entity who is the subject of the application;~~
 - (i) the Authorised Entity who is the subject of the application;
 - (ii) any third party who possesses or controls the money that the Applicant seeks to recover;
 - (b) commence insolvency proceedings against that Authorised Entity;
 - (c) make a formal complaint to the Police or other agency against that Authorised Entity; and/or
 - (d) assist in the taking of any action against that Authorised Entity.
- (3) If a Discretionary Grant is made, the Fund is subrogated to any rights or remedies of the recipient in relation to the subject-matter of the Discretionary

~~Grants are to be subrogated to CILEx~~ and, if required by CILEx Regulation (whether before or after the making of the grant) the Applicant must:

- (a) prove in any insolvency or winding-up of the Authorised Entity;
- (b) sue for recovery of the loss or other property in the name of the Applicant but on behalf of CILEx; and
- (c) comply with any other reasonable requirement for the purpose of giving effect to CILEx's rights.

(4) CILEx Regulation may waive the requirement for an Applicant to pursue one or more of the steps set out in rule 8(2) above if:

- (a) a Discretionary Grant is being made on an interim basis;
- (b) there is no reasonable prospect of such steps assisting in the recovery of the Applicant's losses; or
- (c) it would otherwise be unreasonable to require the Applicant to do so.

Grant Limits

9. 8. (1) A Discretionary Grant ~~may~~ shall not exceed £500,000.

(2) Discretionary Grants made in respect of one Authorised Entity shall not exceed a total of £2 million.

Refusal of an Application

10. 9. If an application for a Discretionary Grant is refused, whether in whole or part, CILEx Regulation must inform the Applicant in writing of its decision and the reasons for that decision.