ICAEW representation

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THE FUTURE OF LEGAL SERVICES

Memorandum of response, submitted by the Institute of Chartered Accountants in England & Wales, to the White Paper "The Future of Legal Services: Putting the Consumer First" issued by the Department for Constitutional Affairs in October 2005

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INTRODUCTION

1. The Institute of Chartered Accountants in England & Wales welcomes the opportunity to comment on the White Paper "The Future of Legal Services" published by the Secretary of State for Constitutional Affairs and Lord Chancellor in October 2005.

WHO WE ARE

2. The Institute of Chartered Accountants in England & Wales (the 'Institute') is the largest accountancy body in Europe, with more than 125,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.

3. The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department of Trade and Industry (DTI) through the Financial Reporting Council. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy.

SUMMARY AND MAIN POINTS

4. The Institute welcomes the publication of these proposals. We agree that the simplification of the structure of the regulation of legal services, and oversight by a body with clear public interest objectives, will be a valuable reform. However, the proposals could have unintended consequences in a number of areas, introducing unnecessary regulatory burdens and complexities for some providers of legal or other professional services. These could unnecessarily restrict the development of the market in a range of advisory and professional services including through the use of Alternative Business Structures (ABSs).

5. In particular, the Department will be aware that Chartered Accountants routinely provide advice and other services to their clients and employers, which come within the definition of legal services set out in Appendix C. This is most frequently given in the form of advice and assistance on a variety of business-related issues, extending to support in relation to legal rights and the performance of legal obligations in relation to tax law, company law and commercial requirements on businesses, but has also increased over the years in other areas. Indeed, the terms "Generally Accepted Accounting Principles" (GAAP) and "the True and Fair View" (True and Fair) under which company accounts must be prepared are both statutory terms, and so represent a legal obligation defining the greater part of the work that many accountants perform.

6. Members of the Institute of Chartered Accountants in England & Wales are themselves members of a regulated profession, and such services are undertaken under the over-sight of their professional body, which itself acts under the oversight of the Financial Reporting Council. The safeguards for the consumers of their services are robust, and the value placed on them has been demonstrated by the growth in this market. Any additional regulation of Chartered Accountants acting within their areas of competence, by another legal services front line regulator, is likely to be both unnecessarily burdensome and

restrict the development of this demand led, cost effective and consumer driven development in the provision of professional services. It would prejudice consumers, by distorting the market in favour of the provision of advisory services by lawyers and could result in an increase in the use of an inappropriately legalistic approach to the interpretation of technical accountancy terms such as GAAP and True and Fair.

7. These comments relate primarily to the services requested by the clients of Chartered Accountants, but in an increasingly complex world, there are a significant number of professions and other advisory businesses (many of them already regulated) where advice on compliance with legal obligations is integral to the service provided. These services would often be of greater value to consumers, were there a facility to provide a small legal department in-house to provide a one-stop-shop, including the services of fully trained lawyers practising in the specific area concerned. However, if the structure of such an entity resulted in the work of the whole firm having to be regulated as an ABS providing legal services (because the need to comply with the legal obligations suffuse the whole business) this could result in not only considerable over-regulation, but could also result in conflicting requirements from the various regulators. We do not consider that it would be overstating the case to assert that this could result in significant damage to the long term development of the UK economy, whose success has depended on a flexible and proportionate approach to business regulation and the supply of professional services.

8. The statutory environment within which "legal services" are provided and the work of the Legal Services Board (LSB) must take place against an objective public interest background, rather than giving (consciously or inadvertently) a market advantage to individuals or entities with a background in the traditional professions of the law, in preference to any equally strongly regulated trades or professions with rather different but equally good ethical standards or requirements for fitness and propriety, which will better suit the needs of some consumers. We are particularly concerned that if the White Paper proposals are implemented without further thought, the opportunity could be lost for further promoting the interests of consumers and the public interest, in the following areas:

    - The definition of "legal services"
    - The regulation of ABSs involving both lawyers and Chartered Accountants;
    - The development of the areas of legal or professional services that should be regulated and by whom; and
    - The development of Legal Professional Privilege, as an issue affecting competition between lawyers and other suppliers of advice on legal obligations and as an issue affecting the public interest in information being available to all those with an important public interest right to it.

    We consider these matters further below.

9. We are also particularly concerned that the White Paper makes no mention of the need for the LSB to work in conjunction with the Financial Reporting Council, the Financial Services Authority or any other regulator who may have responsibility for some of the activities performed by lawyers, or the activities of other participants in an ABS. The LSB should be required to cooperate with other regulators, and lead regulatory responsibility should be with the regulator responsible for the bulk of the services provided by any entity.

PROFESSIONAL SERVICES SUPPLIED BY ACCOUNTANTS

10. The regulation of accountants in the UK has undergone radical and continuing reform, resulting in a regulatory system and an accounting profession which we believe to be unparalleled on a global basis for integrity, market responsiveness and competence.

11. The majority of accountants in public practice provide a regular and routine service to their clients, involving a close knowledge of their clients' business and financial affairs with the regular preparation, review or audit of financial information and the routine provision of information and advice relating to, or arising from, that work. Chartered Accountants have been trained in the application of complex legal and technical requirements, but their primary training does not lead to their necessarily assuming an adversarial approach, and they tend to more frequently act in situations where the client is not in conflict. This can result in a very cost effective approach to the resolution of past failings, or emerging differences between clients and third parties, where an adversarial approach would be less helpful.

12. The provision of advice and assistance on a variety of business-related matters, extending to support in relation to legal matters, provided by Chartered Accountants has tended to grow out of these close client relationships. Business advice would be unhelpful if it did not include advice on rights and obligations under the law, where these are within the competence of the adviser. With their accumulated knowledge and trust for their Chartered Accountant, many clients prefer to depend on them for advice on general business matters, which can involve advice on legal considerations, although Chartered Accountants do not present themselves as solicitors or otherwise qualified as specialist legal advisers. We believe this to be a wholly positive development, where clients effectively have easy and cost effective access to professional services in connection with a range of business-related issues, in a regulated environment. The evolution of this steadily widening range of services provided by many Chartered Accountants has happened without much political or public attention, probably because of the few client or public interest problems associated with it. For these reasons, we believe that it is fundamental in the reform of the regulation of legal services that nothing should be done to prevent or deter the continued development of the provision of these services by Chartered Accountants, where this is in the public interest and that of their clients.

13. Some Chartered Accountants and their clients have experienced barriers on the extent of professional services which can be provided, due to the definition of the reserved areas where solicitors or other regulated legal service providers have been granted a monopoly. A recent example of this is in the case of *Agassi v Robinson* [2005] EWCA Civ 1507 where a very cost effective and reliable means of conducting litigation through direct relationships between Chartered Accountants and barristers has effectively been made untenable, because the order relating to the tax adviser's costs could not be fully implemented under the current structure of the Licensed Access Scheme. For our further comments on this case, see paragraphs 24 to 28 below. We hope that the reform of the regulation of legal services will be implemented in a way which makes the further development of such arrangements easier, rather than increasing (however inadvertently) the barriers to continuing reform.

14. The branch of the legal profession with which the accountancy profession can most readily be compared is that of solicitors. Like solicitors, Chartered Accountants are

required to comply with a series of ethical principles upon which all other professional requirements depend. The suggested future principles for all those providing legal services have been summarised in the White Paper (paragraph 4.1) as:

- ***Independence:*** legal professionals should at all times maintain their duty to act with independence in the interests of justice.

- ***Integrity:*** legal professionals should act with integrity towards clients, the courts, and others, to maintain high standards of professional conduct and professional service, and not to bring the profession into disrepute.

- ***The duty to act in the best interests of the client:*** legal professionals should act in the best interests of the client, except where it would be unlawful to do so or where the interests of justice would be compromised.

- ***Client confidentiality:*** legal professionals should keep their clients' affairs confidential.

The fundamental ethical principles observed by Chartered Accountants are as follows:

- **Integrity:** A *member* should behave with integrity in all professional and business relationships. Integrity implies not merely honesty but fair dealing and truthfulness. A *member*'s advice and work must be uncorrupted by self-interest and not be influenced by the interests of other parties.

- **Objectivity:** A *member* should strive for objectivity in all professional and business judgements. Objectivity is the state of mind which has regard to all considerations relevant to the task in hand but no other.

- **Competence:** A *member* should undertake professional work only where he has the necessary competence required to carry out that work, supplemented where necessary by appropriate assistance or consultation.

- **Performance:** A *member* should carry out his professional work with due skill, care, diligence and expedition and with proper regard for the technical and professional standards expected of him as a *member*.

- **Courtesy:** A *member* should conduct himself with courtesy and consideration towards all with whom he comes into contact during the course of performing his work.

Some changes are currently being made to these principles, to co-ordinate them with those agreed through the International Federation of Accountants (IFAC), on a global basis. This will result in changes to the drafting and detail of the principles, but not to their general overall effect.

15. A comparison of these fundamental principles will reveal that they have many similarities, but a number of differences. These differences have grown out of the differing professional background and client relationships of the two professions, but those employed by Chartered Accountants are equally appropriate to the needs of

consumers, as is demonstrated by the growth in the market in their advice to clients on a wide range of business-related issues.

16. Chartered Accountants also have a different perspective on their obligations of confidentiality than lawyers. For example, the ethical guidance relating to confidentiality does not preclude the disclosure of information to the proper authorities in the public interest. In addition, Chartered Accountants do not come from a background where they are routinely subject to the rights and obligations of Legal Professional Privilege, though they recognise it and apply it, where it has been generated for a client, by their relationship with a lawyer. Chartered Accountants will generally approach the disclosure of information to third parties from the position of making a judgement dependant on a number of factors, including contractual terms and their legal obligations, as well as the public interest and the objective and legitimate interests of the intended recipient of the information. Chartered Accountants are not themselves entitled to benefit from the improper use of confidential information, any more than lawyers are permitted to do so.

17. We are convinced that this evolution in the market for these services provided by accountants is in the public interest and that of clients. Some of the proposals in the White Paper would appear to encourage such a growth, but only at the cost of some Chartered Accountants being subject to dual regulation by both accountancy and legal services regulators. Some could also lead to circumstances where Chartered Accountants are inappropriately judged by the ethical standards of the legal profession rather than their own. Neither of these possible developments would be in the public interest nor in the interests of consumers.

KEY ISSUES IN THE REGULATION OF LEGAL SERVICES

The Definition of Legal Services

18. As noted above, the definition of legal services is extremely wide, including within its scope many of the services that will be provided by other professionals acting well within their own competence, and providing services that it would not be appropriate for a lawyer to provide. This definition could be misleading to many consumers and others, in that it tends to indicate that these services are only, or should only be, provided by a specialist legal professional. It has already, apparently, led to the conclusion that they should be under the oversight of a legal front line regulator, when provided by an ABS firm, bringing a consequent likelihood of inappropriate and duplicated regulation. We therefore suggest that the definition of “legal services” be amended to include only:

- The reserved areas of legal practice and
- Services provided by those holding themselves out to be legal practitioners.

The Regulation of ABS Firms

19. We are concerned that the proposals relating to the regulation of ABS firms, set out in Chapter Six of the White Paper could needlessly distort the development of the market in legal and other professional services, restricting the way in which such services can be provided without improving the levels of protection of consumers or the public interest. We give examples of the ways in which this could occur, below.

20. We see no reason why it should be suggested that the FLRs should be restricted to bodies which already regulate the existing reserved areas for lawyers (as suggested in the first

bullet of Section 6.2). It is not appropriate to put a bar on the development of the FLRs in a way that could prevent additional regulators of reserved legal services to emerge, in a flexible market. Nor do we think it appropriate that a legal practice FLR should have overall responsibility for an ABS which practices predominantly in another regulated area. We suggest that regulators in other fields, such as other professional bodies or the FSA, should be entitled to license ABSs, where authorised by the LSB, and have overall responsibility for the protection of the consumers of the services of that entity, as lead regulator.

21. We agree with the conclusions reached by the Department, that there should be no overall requirement for majority lawyer control in all ABS firms. The development of legal service departments, for example, in major retailers, (the "Tesco-law" model) could provide a very welcome extension to the provision of legal services in a cost effective form, where it is appropriately regulated. However, where a relatively small proportion of the overall services provided by an entity consist of legal services, then it is unrealistic to provide an FLR should be able to direct an ABS firm to alter its management or ownership arrangements (Section 6.2, first bullet of second tranche). Instead, we suggest that an ABS firm should be required to provide reserved legal services under discrete management (including under the oversight of the Head of Legal Practice (HoLP)) and the FLR could be able to require that the ABS divest itself of the legal services practice, if necessary. As a lawyer, the HoLP would be responsible to a legal services regulator for compliance with the appropriate standards in the reserved services provided.

22. We are particularly concerned at the suggestion that **all** of the services supplied by an ABS firm subject to the regulatory control of an existing legal services FLR, whether or not they are reserved legal services and regardless of other regulatory control over such services (Section 6.2, last paragraph). This could result in advice given by Chartered Accountants in the course of accountancy practice being judged according to the fundamental principles of lawyers, rather than their own, which would be completely inappropriate and could represent a complete bar to the development of ABSs involving both lawyers and Chartered Accountants. Where ABS firms are already regulated for any or all of their services, a lead regulator should be appointed, which should be that one which regulates the bulk of the services provided. Any additional FLR required for the regulation of services reserved to lawyers should be obliged to act in cooperation with that lead regulator.

The Development of Regulated Areas

General

23. There are a number of areas where we agree that the provision of legal and other professional services should be regulated. However, this does not necessarily mean that they should be regulated as if lawyers are the only people who can be appropriate to the provision of such services. Provision should be made to allow reserved services to be regulated as flexibly and by as wide a range of regulators as is consistent with the protection of consumers and the preservation of the public interest. In addition, the provision of legal and other professional services should not necessarily be judged according to the fundamental principles appropriate to lawyers, if they already have in place ethical principles or rules of conduct more appropriate to their way of working and regulatory background and which are equally suitable to the needs of consumers and the public interest.

Litigation Services - Licensed Access Scheme

24. We support the development of provisions to make access to the Courts more efficient and more cost effective. However we are concerned that the recent decision in the case of *Agassi v Robinson* indicates that there are serious problems with the Licensed Access Scheme, previously known as BarDirect. The Judgement in this case includes the following statement:

> 'The [Licensed Access Scheme] was certainly both a new and a better way of providing advocacy services, because it enabled the barrister to receive instruction direct from a skilled professional who understood the very technical issues of tax law that arose in the case more efficiently and at less cost than would be involved if the client had to instruct a solicitor as well. And the Lord Chancellor must have been satisfied when he approved this rule change that these new arrangements were appropriate in the interests of the proper and efficient administration of justice.' [paragraph 16 of the Judgement]

25. In the context of providing instructions to the barrister 'more efficiently and at less cost' the Court of Appeal noted that:

> 'fees charged by a firm of solicitors for the work done in respect of these two appeals might have been three times as high as [those of the skilled professional]'

26. However although the Court of Appeal ruled that Agassi should be entitled to recover his legal costs, in practice only a proportion of his actual 'legal' costs could be recovered because the person instructing the barrister was not a solicitor and because of the interaction between the Solicitors Act 1974 and the Courts and Legal Services Act 1990.

27. The argument put forward by the Respondent and the Law Society, who were interveners in the Agassi case, was that to allow the full costs to be recovered would allow any litigant to recover the costs of 'an unqualified and unregulated person' who assisted in their particular litigation. The professional concerned in this specific case was a highly qualified and regulated member of the Chartered Institute of Taxation (CIoT). An extension of the ability to recover costs to professionals engaged under the Licensed Access Scheme would lead only to the recovery of costs of professionals licensed by the Bar Council, not unqualified or unregulated persons.

28. The outcome of this case, and the implications for the future of the Licensed Access Scheme, are clearly diametrically opposed to the principal aim of the reform of legal services set out in the Foreword to the White Paper, namely:

> 'Consumers need, and deserve, legal services that are efficient, effective, and economic. They want to have choice, and they want to have confidence in a transparent and accountable industry.'

We strongly recommend that the workings of the Licensed Access Scheme should be reviewed, and amended, in the context of the objectives set out in the White Paper and in the light of the decision in the *Agassi v Robinson* case.

Probate, Will Writing and Estate Management

29. The preparation of probate papers for gain is a reserved area of practice for solicitors, for historical reasons. The related areas of will writing and estate administration remain unregulated, even though they could provide equal or even more serious opportunities to subvert the intentions of testators or prejudice the interests of beneficiaries. Also, the loosening of the regulatory monopoly through the Courts and Legal Services Act 1990 has not worked well, not yet resulting in the licensing of a single additional probate practitioner. Rather than continuing with the unsatisfactory status quo, we suggest that all these areas of practice should be regulated, but the consumer should be able to choose any of a range of suitably regulated service providers. So, for example, firms of Chartered Accountants should be able to provide these services (which have a high degree of accounting and tax related content) under the oversight of their professional body. We also see no reason why banks and other financial services institutions should not be able to supply them under the regulation of the Financial Services Authority. Each of the regulators should apply their normal principles and standards to the granting of licences to supply these services and their regulation of them. This would provide for a much wider and more flexible supply of these services, without significantly weakening the regulatory protection.

Trust and Company Service Provision

30. The provision of trust and company services will be required to be licensed and monitored under the provisions of the third EU Money Laundering Directive, which needs to be implemented by the Autumn of 2007. In addition, we are aware that the Law Commission are concerned that some professional trustees draft trust deeds in a way that protects themselves against the consequences of their own negligence, frustrating the intentions of settlors and the interests of beneficiaries. We understand the need to minimise the gold plating of EU Directives, and the need to keep regulatory burdens to the lowest level consistent with the protection of the public. However, it is apparent that the licensing and monitoring of trust and company service providers is already going to be put in place for anti-money laundering purposes. If, at any future time, it is decided that regulation of trust and company service providers is also needed for consumer protection purposes, then by far the most cost effective way would be to introduce provision for it at the same time as the implementation of the Directive. As with probate, will writing and estate administration, this should include the possibility for such providers to be regulated by the FSA, by an accountancy professional body, by a legal services FLR or by another appropriate body.

Legal Professional Privilege

31. The question of privilege was looked at in the context of previous reviews by the Office of Fair Trading and the Department of Constitutional Affairs but has not been included in the current review of the regulation of legal services. We recognise the sensitivity of the issue, but we believe that the way should be left open for an early review of LPP including its operation in both advisory and litigation services. We believe that the number of different regulated trades and professions that are qualified and capable of providing ‘legal advice’ calls into question whether the clients of solicitors and barristers should have LPP in relation to advice given, but no others.

32. We are mindful of the remarks of Lord Carswell in the case of *Three Rivers District Council and others v Governor and Company of the Bank of England* namely:

> 'One can add the experience of lawyers who have advised on taxation matters. This applies in particular to inheritance tax planning, where the focus is on the disposition of assets and litigation is not in prospect. It is essential that the legal adviser has a complete picture of financial matters, some of which may be highly confidential, especially when dealing with family businesses. Many clients seeking such advice would be very dismayed to think that the information they have made available to their lawyers might not remain confidential.'

The advice described in the above quote is exactly the same sort of advice that a Chartered Accountant would give to his own client in relation to inheritance tax. It is equally confidential but it is difficult to discern a policy reason why LPP should apply if that advice is given by a solicitor but not if the advice is given by someone equally qualified to give the advice but who happens to be a Chartered Accountant.

33. In recent years, Government Departments and other authorities have increasingly been granted powers to obtain information from a wide range of professional service providers, in order to assist them in carrying out their duties effectively in an increasingly complex environment. This has included requirements for pro-active disclosure of information, which can often be required of any professional adviser with the exception of legal professionals, due to the availability of LPP. Recent examples include the money laundering suspicion reporting requirements under Section 330 of the Proceeds of Crime Act 2002 and the introduction of the Disclosure of Tax Avoidance Schemes (DOTAS) in the Finance Act 2004. The first of these is currently in the course of amendment, under Home Office proposals for the extension of the exemption from reporting suspicions formed in "privileged circumstances" to auditors, accountants and tax advisers, where they are providing services equivalent to those that might be provided by a legal professional. The second was sidestepped by introducing what many consider to be an unsatisfactory legal 'patch' whereby lawyers are taken out of the DOTAS regime if they feel LPP prevents them from complying. In those cases the onus for disclosure is transferred to the client on the basis that the client is only required to report the transactions they have undertaken and not the underlying advice. This does not resolve the competitive inequality between the legal and accountancy professions.

34. We suggest that the LSB will be an appropriate body to consider future emerging issues in this area, where judgements are needed as to the appropriate balance between the public interest information needs of Government agencies and the public interest needs in preserving client confidentiality (including LPP) and an effective market in legal and other professional services. Such judgements will be best made in discussion with the Government agencies involved and other regulators of those providing professional and other advisory services.

RESPONSES TO PARTICULAR PROPOSALS IN WHITE PAPER

In this section of our response, we give our comments on the specific Government proposals, as set out in the White Paper.

Chapter 4: A new regulatory framework

4.1 The 7 objectives and 4 principles for the regulation of legal services will be

set out in legislation. All partners in the regulatory framework – the Legal Services Board, the Office for Legal Complaints and the Front Line Regulators – will have to deliver these.
Changes to the objectives and principles will be made by secondary legislation subject to the approval of Parliament.

We support the drafting of legislation on the basis of its objectives, which we believe helps to clarify the intentions of Parliament and the way in which the legislation should be implemented. We also broadly support the seven objectives, as listed in paragraph 3.1 of the Paper, but consider that the LSB should have an over-riding obligation to carry out its functions in the public interest. The more narrowly defined consumer interest objective is of course vitally important, but only covers a narrower sub-set of the more general public interest imperative.

We agree that FLRs should have fundamental ethical principles which apply to the provision of services by those they regulate, and that these should be appropriate, adequate and agreed with the LSB. However, we do not think it necessary or appropriate for these to be laid down in statute. We think that these principles may appropriately develop over time, and that a statute based system could prevent timely changes to deal with new situations.

The LSB should also be required to act in cooperation with any other regulatory authorities concerned with the regulation of those providing legal or other professional services.

There should be a requirement for any significant and substantive proposed changes in the objectives to be subject to public consultation, as well as the approval of Parliament.

4.2 Legislation will require all partners in the regulatory framework to adopt best practice in carrying out their functions.

We agree that all organisations with a role in the regulatory framework should adopt the principles of good regulation (and their successors) of the Better Regulation Executive, in carrying out their functions. We suggest that the phrase "best practice" is avoided as being too subject to change and potentially over prescriptive.

4.3 Legislation will require all partners in the regulatory framework to adopt a risk-based approach to regulation.

Overall we support a risk based approach to regulation, and we are strong in our support for cost effective and flexible regulation which imposes as few burdens as possible, while achieving its objectives. However, we do have some concerns that the implementation of the recommendation to set "standards/rules which are applied to a whole set of regulated firms/organisations on the basis of assessments of the risks posed to society by the activities of firms of that type". We fear that this may lead to some regulators enforcing standards in an uneven or arbitrary way, according to current perceived risks, with insufficient attention to the need for every entity covered by the requirements to comply with them. The most counter-productive of regulations are those that are complied with by the conscientious, but not by those who are prepared to ignore them in the knowledge that they are unlikely to be enforced, thus giving a clear market advantage to the latter.

Chapter 5: Simplifying regulation

5.1 Legislation will establish a new Legal Services Board (LSB), with regulatory power vested in it. The LSB will authorise Front Line Regulators (FLRs) that satisfy it that they are competent to regulate. The LSB will be able to modify or remove the authorisation if an FLR fails, and to carry out regulatory functions in those circumstances.

We broadly agree with these proposals, subject to our comments in paragraphs 19 to 22**,** on the types of organisations that should be permitted to operate as the Front Line Regulators of ABSs, and their oversight.

We do not believe that it would be appropriate for the LSB to directly regulate law firms or ABSs, as well as having oversight of FLRs. This was a model used under the Financial Services Act 1986. It lead to issues, including questions over the equivalence of rule books, that led to the need for reform resulting in the Financial Services and Markets Act 2000.

5.2 Legislation will require existing regulatory bodies to satisfy the LSB of the appropriateness of their governance arrangements.

This provision should apply not only to existing regulatory bodies but also to future ones.

5.3 Legislation will require the Legal Services Board to establish and maintain a Consumer Panel.

We agree with this proposal. A Practitioner Panel should also be maintained, which should include representation from ABSs involving a majority of non-lawyers.

We suggest that the membership of the Consumer Panel should extend to representatives of large scale consumers of legal services, such as the Confederation of British Industry and the Institute of Directors, as well as the representatives of small businesses and individuals who are currently included (See also our suggestions under 5.6 below, on the powers to appoint and maintain a Consumer Panel).

5.4 Legislation will set the size of the Board of the LSB at 9 to 12 members. It will be possible to change this by secondary legislation, subject to Parliamentary approval.

We have no comment to make on this proposal. However, as noted elsewhere in the White Paper, a majority of the members should be non-lawyers, and so should the Chair.

5.5 Legislation will provide for the Secretary of State to appoint the Chair of the LSB. The Secretary of State will appoint the members of the LSB, following consultation with the Chair. All appointments will be in accordance with the rules of the Commissioner for Public Appointments.

We have no detailed comment to make on this proposal, but the Department will need consider carefully the possibility that the granting of these powers to the Secretary of State might lead to a perception that the LSB is not independent of Government.

5.6 The LSB should seek to be added to the list of organisations with 'stop now' powers under the Enterprise Act.

Legislation will provide for the powers of the LSB to be amended by secondary legislation, subject to the approval of Parliament.

We agree that the LSB should be added to the list of organisations with 'stop now' powers under the Enterprise Act.

Legislation should provide that amendments to the powers of the LSB by secondary legislation, subject to public consultation as well as the approval of Parliament.

Legislation will provide the LSB with the following powers to carry out regulation:

Authorisation of Front Line Regulators (FLRs)
• to authorise FLRs if it is satisfied that they will regulate in the consumer interest.

Controls over FLRs
• to require Front Line Regulators to provide it with information (subject to privacy/confidence) to carry out its duties
• to issue regulatory guidance to FLRs
• to approve fees to be raised by FLRs
• to set requirements for indemnity insurance arrangements of FLRs and practitioners
• to set compensation fund requirements.

Sanctions over FLRs
• to set regulatory targets for FLRs and to monitor compliance
• to impose financial penalties on FLRs for failing to meet targets or achieve compliance
• to direct an FLR to take a specific regulatory action
• to strike down or amend rules of an FLR.

In most cases the LSB will want to work alongside the FLR in areas of weakness to improve them. However, where an FLR continues to fail, the LSB will be able to:
• remove the authorisation of the FLR in a particular area or areas of regulation and either identify an alternative FLR or carry out their regulatory functions itself.

Ultimately, the LSB would be able to recommend secondary legislation to remove the authorisation of an FLR entirely. Following consideration of any wider public interest issues, the Secretary of State would be expected to carry through the LSB's recommendation in such a case.

In general, we agree that the LSB should be granted these powers, and that they appear to be necessary and sufficient for their functions, in relation to the regulation of the provision of legal services by lawyers and law firms.

However, we have considerable concerns that these powers do not include any powers to cooperate with any other regulatory authority. Nor do such powers or requirements appear to be mentioned elsewhere in the White Paper. In the case of Alternative Business Structures (ABSs), firms will sometimes have a lead regulator (such as this Institute for firms of Chartered Accountants or the FSA for banks) which have responsibility for the

regulation of the firm as a whole, and which should not be required to give precedence to the LSB as the regulator of the legal services which may represent a small proportion of the services provided as a whole. See our comments in paragraphs 19 to 22 above, for our further thoughts on these matters.

Powers in relation to the operation of the compensation schemes run by FLRs should be proportionate, and should be limited to payments to individuals and small businesses. This is the model used by the Financial Services Authority under the Financial Services and Markets Act 2000. We suggest that payments should not be required to be made by FLR compensation schemes in excess of £20,000, in line with that proposed for awards made by the OLC.

Legislation will provide the LSB with powers in relation to the new Office for Legal Complaints, in relation to alternative business structures and to enable it to obtain advice and information:

Powers in relation to the Office for Legal Complaints
• to appoint the Chair of the OLC, subject to the approval of the Secretary of State
• to appoint the OLC Board
• to set and monitor performance targets for the OLC
• to approve the budget of the OLC
• to remove the Chair of the OLC, subject to the approval of the Secretary of State, for example in cases of poor performance, misconduct, or bringing the OLC into disrepute
• to remove members of the OLC Board, for example in cases of poor performance or misconduct, or bringing the OLC into disrepute.

We consider that the OLC should also be subject to a requirement to cooperate with any other office or ombudsman with responsibility for consideration of complaints against ABS firms.

If the current very wide definition of "legal services" is retained, then the OLC should not have any responsibility for dealing with complaints where there is a more appropriate professional or regulatory complaints handling system.

Controls over alternative business structures
• to authorise FLRs to license (or in the absence of an ABS regulator to license itself) ABS firms which meet the required standards
• to exclude a person from holding a position in an ABS firm
• to set and modify the safeguards for ABSs (e.g. a fit and proper test, nominated Head of Legal Practice and Head of Finance and Administration)

We agree that the LSB should have powers to control the provision of reserved legal services through the operation of ABS firms, but we consider that these should be subject to cooperation with other regulatory authorities to which the ABS firm may be subject. The lead regulator for an ABS firm should be that (if any) appropriate to the majority of the services provided. Our further comments on these matters are set out in paragraphs 19 to 22.

Powers in relation to advice
• to appoint and maintain a Consumer Panel

• to request advice from the Consumer Panel
• to require any person or organisation to provide it with information in connection with its functions

The power to require any person or organisation to provide the LSB with information in connection with its functions should be subject to a requirement for the LSB to be proportionate in its requests and a right of appeal to an independent tribunal and to the Courts, by the person or organisation from which information is required. Without these safeguards such a power could be oppressive on the regulated population or third parties.

The power to request advice from the Consumer Panel will not compensate for an apparent lack of any requirement for the LSB to carry out public consultations in appropriate circumstances. We agree that there need be no requirement for public consultation for minor rules changes of the LSB or FLRs, but more fundamental changes (such as those requiring legislative change) should be subject to a requirement for public consultation.

It should also be recognised that although the consumer and related organisations, listed in Appendix A, represent consumer groups whose interest it is vital to protect, they are not the only ones. Commercial concerns of all sizes are also significant consumers of legal services, and if they cannot obtain them in a suitably open but appropriately regulated market, the future economic success of the United Kingdom will be affected in proportion to the relative importance of those entities. We suggest that the CBI and the IoD should also be represented on the Consumer Panel, and that the LSB should be alert to the need for the inclusion of representation from other discrete interest groups, such as the voluntary sector.

The LSB should also be required to consult with, and obtain advice from, other regulatory authorities, where this is appropriate. It would also be appropriate to require a Practitioner Panel (including representation from non-legal ASBs).

5.7 Legislation will require the LSB to consult formally with the Consumer Panel, the Secretary of State for Constitutional Affairs, the Office of Fair Trading and the higher judiciary when it is considering taking the following action:
• making a recommendation to the Secretary of State to authorise new FLRs, or to remove the authorisation of existing FLRs, in whole or in part
• making a recommendation to the Secretary of State that unregulated activities should be brought under the scope of its regulatory control
• carrying out specific regulatory functions itself
• reviewing or setting the targets or funding of, or the sanctions available to, the Office for Legal Complaints
• issuing a directive to alter any of the rules of a FLR.

We suggest that some or all of these functions should also be subject to public consultation, and consultation with the persons subject to regulation by the relevant FLR and their competitors and clients.

5.8 Legislation will require the LSB to publish an annual report, to be laid before Parliament. The LSB will have a duty to provide a report on relevant issues to the Secretary of State for Constitutional Affairs as requested.

We agree with these proposals.

Legislation will provide the Secretary of State with powers to:
• bring forward secondary legislation on the advice of the LSB to widen the scope of regulation
• bring forward secondary legislation on the advice of the LSB to authorise new FLRs, or to alter or remove the existing authorisation of an FLR
• remove the Chair or members of the LSB (in the latter case, having consulted the Chair) in specific limited situations (e.g. misconduct)
• direct the LSB to take action to implement international agreements
• bring forward secondary legislation to amend the powers of the LSB
• initiate value for money scrutinies or major reviews of regulation from time to time, e.g. where there has been criticism from a Parliamentary committee
• consider and resolve any approach from the OFT where it has raised competition concerns with the LSB and is not satisfied with the LSB's response.

We agree with these proposals, but they should be applied subject to the Secretary of State being satisfied that the LSB has taken into account the results of any public consultation it has undertaken, in making its recommendations. They should also specifically include powers aimed at future reductions in unnecessary burdens, such as a power to narrow or otherwise change the scope of regulation, as well as widening it.

5.10 Legislation will provide for the OFT to:
• have an ongoing duty to scrutinise regulating provisions of all authorised FLRs, and
• to report to the LSB on competition issues relating to professional rules prior to authorisation of any new FLR.
The LSB will be under a statutory obligation to respond to any OFT report published, and to take appropriate action.

We agree with these proposals.

Legislation will give the Secretary of State the power to resolve issues, following the taking of advice from the Competition Commission, in the event of a disagreement between the OFT and the LSB.

We agree with this proposal.

Chapter 6: Confidence and choice – new ways of delivering for consumers

6.1 Legislation will provide for a flexible and robust licensing scheme for alternative business structures. This will allow lawyers and non-lawyers to work together to provide legal and certain associated services. External investment will be permitted.

We agree with these proposals, subject to our comments on the regulation of ABSs, set out in paragraphs 19 to 22.

6.2 Legislation will provide for the modification of Front Line Regulators' powers by secondary legislation proposed by the Secretary of State for Constitutional Affairs following a proposal from the LSB.

We agree with these proposals, subject to a requirement for public consultation for significant changes.

6.4 Legislation will require Front Line regulators of ABSs to ensure that firms identify a Head of Legal Practice and a Head of Finance and Administration.

We agree with these proposals, but it should be clear that the oversight by a legal services FLR, of the Head of Finance and Administration of the ABS firm as a whole, should relate only to the impact of these functions on the provision of reserved legal services.

6.5 There will be no requirement for an overall majority of lawyers in all ABS firms. The LSB will decide whether the services provided by some ABS firms require a certain level of lawyer control.

We agree that the LSB should have decision making powers over the level of lawyer control over particular categories of services provided by ABS firms, but these should not apply outside the reserved areas. Nor should they be employed within the reserved areas without discussion with the other regulators of ABS firms, and public consultation. In considering this matter, the LSB will need to have particular regard to the need to preserve level competitive conditions between differently structured and regulated ABS firms.

6.6 External investment in ABS firms will be permitted, and will be based on a fitness to own test, covering:
• honesty, integrity and reputation
• competence and capability, and
• financial soundness.

We agree with these proposals. However, we believe that judgements on these matters should be carried out by the LSB subject to discussions with other regulators to which the ABS firms may be subject. Ultimately, these matters should be judged by the lead regulator of any entity, in the interests of consumers and the public interest.

If it is intended that an ABS firm will be able to become directly listed on a public stock market, the implications of these proposals will have to be thought through carefully, and alternative protections may need to be introduced. If this is not intended, we believe this to be an unwarranted restriction on competitive conditions.

6.7 The LSB will determine the extent of external investment in ABS firms according to the type of business and acting in line with its regulatory objectives.

We broadly agree with these proposals. However, we believe that judgements on these matters should be carried out by the LSB subject to discussions with other regulators to which the ABS firms may be subject. Ultimately, these matters should be judged by the lead regulator of any entity, in the interests of consumers and the public interest.

6.8 Legislation will provide for consumers to complain to the new Office for Legal Complaints.
ABS regulators will pass cases of misconduct to the relevant disciplinary body.
ABS regulators will be able to require the removal of a director or partner in an ABS firm and to prohibit them from holding any position of control in an ABS

firm, either for a fixed period, or indefinitely.
ABS regulators will be able to alter or remove an ABS firm's licence to offer services.

We agree with these proposals. In particular, we have no problem with the OLC being an appropriate initial recipient of complaints in relation to any legal or professional service, though it may need to act particularly sensitively to avoid unfair treatment in relation to complaints relating to services provided under ethical and regulatory requirements other than those of the legal profession.

6.9 The LSB will provide clear rules relating to the prevention of conflicts of interest in respect of services provided by ABS firms.

We agree with these proposals. However, we believe that the relevant rules on these matters should be carried out by the LSB subject to discussions with other regulators to which the ABS firms may be subject. To the extent that these do not relate to the reserved areas of legal services, the lead regulator of the ABS firm should take responsibility for these matters.

6.10 ABS regulators must not permit ABS firms to provide any service likely to be incompatible with the principles of the legal profession.

We agree broadly with this proposal. However, it should be clear that ABS firms which are predominantly members of other professions should have the higher requirement for compliance with the fundamental ethical requirements of their own profession, where these are adequate, appropriate and well enforced. This should not be allowed to stand in the way of their acting as an ABS, where this is in the interests of their clients and the public interest.

6.11 Legislation will require the LSB to monitor the provision of legal services across different sectors and geographically, and use the results of that work to inform its regulatory decisions. This will include the authorisation of, and imposition of any conditions upon, ABS regulators.

We agree with this proposal. However, if the current very broad definition of legal services is retained, this should take into account the fact that some services will be equally appropriate to the competence of alternative regulators. In any case, the LBS should be required to carry out these functions in cooperation with other appropriate regulators and the OFT.

6.14 The Not for Profit sector will fall within the regulatory scope of the LSB and the ABS licensing scheme. The LSB and Front Line Regulators will have the power to waive or alter ABS licensing requirements in specific cases where it is in the public interest.

We agree with this proposal.

Chapter 7: Protecting consumers if new problems occur

7.2 The LSB will have a statutory duty to determine whether a legal service should be regulated.

We broadly agree with this proposal. However, the fact that a legal or other professional service should be regulated does not necessarily mean that it should be regulated under the oversight of the LBS – for example, see our comments above, in paragraph 23 and subsequent paragraphs.

Legislation will require the LSB to investigate aspects of the market if requested to do so by its Consumer Panel, the Office of Fair Trading, or the Secretary of State for Constitutional Affairs.

We agree with this proposal.

7.4 Legislation will give the LSB the power to:
• investigate the prospect of market intervention
• make a report to the Secretary of State
• propose that additional activities are brought under its regulatory control by means of secondary legislation.

We agree with this proposal, subject to consultation with any other regulatory authorities which may be concerned with the matter, the OFT and public consultation where appropriate.

Legislation will require the LSB to consult in advance the Consumer Panel, the Secretary of State for Constitutional Affairs, the Office of Fair Trading and the higher judiciary.

Public consultation should also be required, where appropriate.

The LSB will have the power to:
• authorise appropriate regulator(s) for any newly reserved activity, or, as a last resort, regulate the activity directly itself
• make a charge to the sector for any costs involved in new regulation.
Legislation will enable new areas to be brought within the regulatory net by secondary legislation, subject to the approval of Parliament.

We agree with this proposal, subject to consultation with any other regulatory authorities which may be concerned with the matter, and public consultation where appropriate.

7.6 Legislation will enable the LSB to:
• investigate, including taking advice from the Office of Fair Trading, the prospect of removing a service from its statutory oversight
• make a recommendation to the Secretary of State to propose that a service should be removed from the statutory oversight of the LSB. This would be given effect by Regulatory Reform Order or primary legislation, subject to the approval of Parliament.

We agree with these proposals.

7.7 Legislation will provide for those legal services that currently may only be provided by certain qualified members of the legal profession to form the core activities over which the LSB will have regulatory control.
Legislation will provide that where the LSB proposes to the Secretary of State that additional activities should be brought within or out of its regulatory

control, those activities must fall within the definition of legal services.

We agree with this proposal. However, these provisions of the legislation should be written in a way which allows for evolution of the understanding of the extent and definition of core legal services, the appropriate persons to provide those services over time and how they should be regulated.

Chapter 8: Complaints – what happens if things go wrong?

8.2 Legislation will establish the new Office for Legal Complaints with clearly defined powers. It will deal with all consumer complaints about legal service providers who are members of bodies or organisations regulated by the LSB.
The OLC will be independent from Government and providers of legal services. It will be accountable to the LSB and will be funded by the sector.
The OLC will investigate all complaints and refer any issues of misconduct to the FLR concerned, monitoring the decisions. The LSB will oversee their disciplinary arrangements.

We agree with these proposals. However, the OLC, LSB and FLRs should be required to agree and operate Memoranda of Understanding with other regulators and complaints and disciplinary bodies to which the providers of legal and other professional services may be subject, to prevent the possibility of those providers being subject to over-lapping or inconsistent requirements and enforcement provisions. There should be no implication in the structure of the OLC that ABSs must necessarily be lawyer dominated, nor any competitive advantage given to such ABSs.

The White Paper does not currently include any provisions to deal with the possibility of double jeopardy or the duplication of investigations for regulated persons operating within ABSs. These will need to be given careful consideration in the drafting of the proposed legislation and its implementation.

8.3 Legislation will set the size of the OLC Board at 7 to 9 members. It will be possible to change this by secondary legislation, subject to the approval of Parliament.
To meet the needs of the different consumers, the members of the OLC will between them have experience of:
• consumer affairs
• the provision of legal services
• complaints handling
• the wider advice sector
• civil or criminal proceedings and the working of the courts
• legal education and training
• the maintenance of the professional standards of persons who provide legal services
• the needs of diverse consumers within society.

There should also be a requirement for a majority of the members of the OLC to consist of non-lawyers, to ensure that the public interest and the interest of consumers is maintained and seen to be maintained.

The OLC Board will appoint arbiters who will make decisions on individual complaints. To command consumer confidence, legislation will provide that:

• all appointments to the Board of the OLC will be made by the LSB on merit, in accordance with the rules of the Commissioner for Public Appointments
• the Chair will be a non-lawyer and will be appointed by the LSB with the approval of the Secretary of State for Constitutional Affairs
• the Board of the OLC will consist of a majority of non-lawyers
• the LSB will be able to remove the Chair of the OLC with the agreement of the Secretary of State in cases of poor performance or conduct, or of bringing the OLC into disrepute
• the LSB will be able to remove members of the Board in the same circumstances.

We agree with these proposals.

8.4 Legislation will provide the OLC with the following power, which will apply to those regulated by the LSB (including ABS firms):
• the power to require evidence
• the power to dismiss cases
• the power to enforce decisions
• the power to make decisions in all the circumstances of a complaint.
To ensure that the OLC's powers remain adequate, it will be possible to amend them by secondary legislation, subject to the approval of Parliament.

We agree with these proposals. Consideration should also be given to whether the OLC should be given the power to require evidence from complainants and third parties (subject to controls to prevent such powers being used oppressively).

8.6 Legislation will enable the OLC to make a report to the LSB where it is concerned that an FLR is not properly carrying out its duties in relation to discipline. It will then be for the LSB to take action with the FLR as necessary.

We agree with this proposal.

8.8 The OLC will consider how best to make information available to consumers about the complaints records of providers.

We agree with this proposal.

8.9 The LSB will ensure that the OLC agrees protocols with the FLRs regarding sharing of information.

We agree with these proposals. Protocols should also be agreed with the other regulators of ABSs.

8.10 Legislation will require the OLC to monitor and prepare reports on trends in complaints handling and outcomes.

We agree with these proposals.

Legislation will require the OLC to produce an annual report, to include details of its performance.

We agree with this proposal.

8.11 Legislation will provide for an upper limit of £20,000 for awards by the OLC. It will be possible to amend this by secondary legislation, subject to the approval of Parliament.

We broadly agree with these proposals, which should be operated subject to a requirement for amendments to be subject to public consultation.

We agree that £20,000 is an appropriate limit, in relation to monetary awards in compensation for poor service or distress. We also agree that it would be an appropriate limit on amounts that can be claimed from a compensation scheme, in cases where it cannot be recovered from the service provider concerned. However, we consider that the OLC should also have the power to enforce reasonable contractual terms on legal service providers, or monetary compensation for non-compliance, whether or not these exceed £20,000 in value.

There will also be a need to provide for a right of appeal, against decisions made by the OLC, including to the Courts.

8.12 Legislation will provide that:
• each tribunal should review its powers and provide an annual report to the LSB
• the LSB or the relevant tribunal will be able to recommend to the Secretary of State variations of its powers and procedures
• the Secretary of State will be able to amend the powers or procedures of tribunals by secondary legislation, subject to Parliamentary approval.

We agree that questions of professional misconduct should be referred to the disciplinary tribunal (or similar body) of the professional body concerned, and that these tribunals should be under the regulatory oversight of the LSB, in respect of the reserved areas and other legal services provided by specialist legal professionals.

Chapter 9: Cost and funding of the new arrangements

9.1 The costs of the LSB will be met by the providers of legal services. The costs of the OLC should be met by providers through a general levy and the polluter pays principle.
The LSB will determine the precise balance. The OLC and the FLRs will determine how the general levy will be allocated among them.

We agree with these proposals, however, they should be operated subject to a requirement for consultation of the regulated population and the FLRs, including the regulators of ABSs.

PARTIAL REGULATORY IMPACT ASSESSMENT

The Partial Regulatory Impact Assessment (PRIA) presented in Appendix D of the paper is seriously flawed, in that it has been drawn up in a way that presupposes that "legal services" as defined in the White Paper will be provided only by members of the legal professions. No consideration has been given to the impact of the proposals on members of other advisory trades or professions or (more importantly) their clients.

In paragraph 2.32, the OFT report on competition in the professions is quoted as identifying a number of professional rules set by legal services self-regulating bodies which were potentially unduly restrictive to effective competition. In a regulatory reform intended to put the interests of consumers first, it is inappropriate to omit consideration of the relative costs and benefits of regulation of ABSs by non-legal services regulating bodies, in a climate where legal services regulating bodies have been found to have been starting from a low base, in their consideration of the interests of consumers and the public interest.

The Summary of Options considered in the PRIA, in section 4, is incomplete, it that it does not consider the (we believe considerably more beneficial) option of permitting non-legal regulatory bodies to have oversight of the overall provision of services by ABSs. This is driven home by the fact that there is no inclusion in the list given in paragraph 4.3 of other trades and professions that supply unreserved services which come within the overall definition of "legal services" used in the White Paper. These can either be provided on an unregulated basis (equivalent to the unregulated legal services provided by will writers and so on) or can be provided on the basis of an existing robust regulatory structure.

The Small Firms Impact Test set out in section 9 demonstrates some of the weaknesses of the PRIA, by devoting seven paragraphs to the impact on small legal practices, against two paragraphs to the impacts on small business consumers of legal or professional services. We also note that no consideration at all has been given to the impact of the proposals on small professional services firms, such as accountants, whose business may be affected by the setting up by legal practices of ABS firms providing accountancy services, which will compete more directly with them without the accountancy practices having an appropriately structured and regulated opportunity for provision of equivalent competitive services through their own ABSs. However, it is more important to consider the interests of the consumers of legal services than their suppliers. Most small businesses have an existing relationship with a professional firm of accountants, with whom they are familiar and with whom they have an existing relationship of trust. It would almost certainly be easier and more cost effective for them to seek legal and other professional services through a ABS led by their accountant, than to have to seek them through a ABS led by a legal practice and regulated as such.

Similarly, the Competition Assessment set out in section 10 of the RIA is flawed, in that it considers competition implications only within the legal professions, and not valid and appropriate competition between the legal professions and their regulated and non-regulated potential competitors. This is unhelpful to the interests of the consumers of legal services, as widely defined in the White Paper.

CONCLUSIONS

We would be pleased to provide further backing for the views we express in this response, and in particular to explain why the changes we propose would further the objectives of the reform, to seriously put consumers first.

FJB
20 January 2006