



23 February 2010

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Ms Mahtab Grant  
Legal Services Board  
7<sup>th</sup> Floor, Victoria House  
Southampton Row  
London WC1B 4AD

Dear Ms Grant

### **Alternative Business Structures – approaches to licensing**

The ICAEW is pleased to respond to your request for comments on *Alternative Business Structures – approaches to licensing*.

In our previous paper<sup>1</sup> we identified the concept of Third Category regulators whose main business is not law. In this response we use this phrase again and also introduce the phrase Third Category professionals. These are practising members of the Third Category regulator who may already provide some unreserved legal services as part of their professional practice.

We are writing to you under separate cover in anticipation of the meeting you are calling for Third Category regulators. That Letter will address a number of concerns, some of which are highlighted elsewhere in this response and some which are not, hence the need for a separate letter to you

### **MAJOR POINTS**

The LSB wishes to open the market and achieve good outcomes which we welcome.

However the Consultation paper states that the Act contains “protections for lawyers and consumers” to which the paper intends to give “teeth”. The Act is more subtle than that as legal services are provided by professionals who are not lawyers.

We are concerned that the regulatory objectives set out in the Legal Services Act (LSA) which the LSB seeks to implement will not be served by regulating all providers of legal services as if they were law firms. We believe this to be a far wider and more extensive problem than has yet been recognised. Our Letter identifies:

- The contrasting regulatory impact of ABS formation on a firm of Third Category professionals and a firm of lawyers
- The distortions affecting Third Category regulators and their ability to enter the legal services market as a credible alternative to the SRA for legal services regulation

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<sup>1</sup> ICAEW Response to the Supplementary Consultation on proposed rules to be made under sections 30 and 51 of the Legal Services Act dated 27 October 2009

- Pressures on Third Category professionals to deregulate completely with attendant issues for diversity, satisfaction of the regulatory objectives, and transparency of the legal services market.

We have also highlighted these points where relevant in our response below in relation to the questions raised and look forward to debating them with you in more detail.

In the Consultation paper much reference is made to 'consumers'. However, 'consumers' are a very varied group of persons. They range from private individuals to large multinationals. Our view is that the arrangements proposed should take this into account, in much the same way that the FSA recognises the differences between different groups of consumers. The 'protections' needed by one group are likely to be greatly different to that needed by another, which in some cases may be very little. We have been advised that there is a dearth of available research in this area and have already offered our assistance to the LSB and the Consumer Panel.

Please contact me should you wish to discuss any of the points raised in this response.

Yours sincerely

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Past President

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## **RESPONSES TO SPECIFIC QUESTIONS/POINTS**

### **Question 1 – what is your view on basing the regulation of ABS on outcomes?**

1. The principle of regulation based on clear outcomes is welcomed. It must be based on all the regulatory objectives and where these objectives act against each other, further discussion is needed.
2. Further debate is required with Third Category regulators whose members already provide legal services (but whose main business is in a different area) to ensure outcomes
  - Are workable for this audience and without unintended consequences
  - Will not act as a barrier to the future creation of ABSs.

### **Question 2 - do you think our approach set out to the tests for external ownership is appropriate?**

3. The Institute is in broad agreement with the key proposals. However, the Act's requirements are very wide ranging, possibly more so than the FSA would require and they should be applied pragmatically. The key matter must be that non-authorised persons cannot interfere with the provision of legal services.
4. We are not clear why the LSB has put additional barriers in the way of LAs who may want to set a controlled interest or reduce the material interest percentage, and not allow LAs to set limits on the percentage of shares held or prohibit the flotation of licensed bodies on a recognised investment exchange. Any of these may create additional work for the LA and possibly the ABSs licensed by them but the Act does prohibit this and sets no additional requirements if a LA chooses to do so. Therefore we do not believe that the LSB should set additional requirements or prohibitions.
5. In some of our work we do require covenants from those who have a significant influence over an ABS. These are usually to the effect that the entity will not undertake any action that would conflict with the ABS's duties under the Act or the licensing rules. We would also place a similar requirement on the licensed body that it should report if that influence was exercised in an inappropriate manner.

### **Question 3 – Do you have views on how indemnity and compensation may work for ABS?**

6. We have written separately to the LSB on indemnity and compensation arrangements and refer to the comments in that letter<sup>2</sup>.

### **Question 4 – do you agree with our position on reserved and non reserved legal activities?**

7. To extend the scope of reserved legal services or to extend regulation to certain individuals who are not contemplated by the current arrangements without the participation of those involved and impacted by the changes would be contrary to BERR principles and the consumer interest. Our view is that there is much work to be done in making the current arrangements work before they are extended.
8. The question of reserved and non reserved legal services is complex and we are considering a follow up paper to the LSB on the point.

### **Question 5 – are the enforcement powers for LA's suitable?**

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<sup>2</sup> Letter from the ICAEW to the LSB (ref 20/10) dated 9 February 2010.

9. We have no comments to make. We believe our own enforcement powers to be adequate in relation to our own members (whether working in the practice of accountancy or elsewhere) and our member firms (including non-accountant partners, who accept our requirements as “affiliates” of the ICAEW). Additional enforcement powers are therefore not required for the protection of our members’ clients and third parties, though they may be for other LAs.

**Question 6 – what do you think of our approach to access to justice?**

10. It stands to reason that any new ABS entering the market afresh will improve access to justice. Requiring entrants to explain how they will do it is unlikely to have any positive effect.
11. However we note the concern raised by Special Bodies that additional regulation could *reduce* access because the regulatory burden may mean Special Bodies leave the legal services market. This concern will apply equally to Third Category professionals who could encounter disproportionate regulation.
12. Our overall views follow the arguments set out in paragraph 221 of the Consultation paper. Firms will make commercial decisions on the services they wish to provide and the clients they wish to attract. Trying to set requirements for them to act differently is likely to be counterproductive. However, the ethical code that applies to the individuals/firms providing legal services should prevent any other forms of discrimination.
13. Nor can we see that there should be a requirement for LAs to make annual reports on this matter. If an LA was to set up, specifically to attract firms who only wanted to provide reserved legal services to ‘high net-worth’ individuals, that may be seen as not contributing to increasing access to justice, but it may well contribute to a competitive environment amongst firms, which is another objective of the Act. This should be an activity undertaken by the LSB, to see if there are groups in society who are facing barriers to accessing justice. Action to help could then be considered, but it would be strange.

**Question 7 –what are your views of our preference for a single appeals body?**

14. This raises specific and separate issues for Third Category regulators and professionals who already have appeal procedures that will cover professional services which also come within the ambit of legal services. These procedures allow for the parties to appear in person, be legally represented before a panel that includes lay members and matters are held in public.
15. A single appeals body should not be put in place without procedures for the avoidance of duplicate requirements. Any duplication should be identified and managed in the interests of justice and we are happy to work with the LSB and other interested parties.

**Question 8 –do you agree with our approach to special bodies?**

16. Yes, although we consider that the transitional period should be extended for a longer period so that the special bodies have time to consider their options once the ASB/LA landscape is clear. There is the option that the LSB becomes the LA for the special bodies and we believe that this should be considered in conjunction with the special bodies themselves.

**Question 9 – do you think our approach to HoLP and HoFA is suitable?**

17. Yes.

**Question 10 – do you think our approach to complaints handling is suitable?**

18. Overall the approach set out is suitable, but there could be major issues in firms which are multi-disciplinary practices as well as ABSs, and for Third Category professionals with existing complaints frameworks covering non-reserved legal services and non legal services.

19. The reserved legal element of work within a multi-disciplinary practices or a Third Category professional firm may be very small. Referring complaints about, for example audit matters, to the OLC would be counterproductive and time consuming, even if the complaint was apparently related to some legal issue within the audit. Instead we would suggest a process whereby the matter was initially referred to the particular LA to deal with. Only if the matter could not be resolved to the client's satisfaction and it was a matter that related to a reserved legal service would it need to be referred to the OLC. To put this matter into context, we receive less than 2,000 'complaints' a year and many of these are resolved by our conciliation processes.
20. The OLC will take all "service complaints" relating to ABS and refer them to the appropriate body where necessary. Clients of Third Category professionals would be surprised if certain complaints were referred onwards to the OLC, (even if on the same transaction), whereas others are not. We are not aware of any debate planned to harmonise arrangements and suggest this is commenced soon so there is clarity for consumers and regulators alike.

**Question 11 – what are your views on our proposed course of action to conduct research and depending on the results, will compel transparency of data or encourage it**

21. Our view is that anything that allows for the provision of legal services via different routes is likely to foster increased diversity and opportunity. Thus the creation of ABSs is likely to have a positive impact. Any information requirements that are placed on ABSs should also be placed on other providers of reserved legal services, but in respect of the provision of reserved legal services only. To do otherwise would be disproportionate for multidisciplinary practices where reserved legal services are a small part of their activities. Collecting such data has a cost and data at this level has to be supplied by individuals, who may regard the questions as intrusive.
22. We support research that assists in effective policymaking and delivery of desired outcomes. However, we are unclear what is meant by 'depending on the results, will compel transparency of data or encourage it'.
23. We are not sure that a diverse legal profession, as hopefully brought about by ABSs, will impact on small firms in the way suggested. Small firms will close if they cannot compete with larger firms on a cost basis or cannot offer niche services.

**Question 12 – do you agree with our approach to international issues?**

24. The Institute already operates on the international stage in the field of professional services. We would be happy to offer our assistance and experience to the LSB.

**Question 13- should LDPs, Recognised Bodies and other similar firms have transitional arrangements into the wider ABS framework in the way that we propose?**

25. We have no comments on this point.

**Question 14 – should ABS licences be issued for indefinite periods?**

26. We agree that licences should be issued for an indefinite period since there are mechanisms for the licence to be surrendered or withdrawn. We cannot see that the licensing fee can be anything other than reflective of the costs incurred by the LA. Continuity of the licence would also be dependent on the payment of an annual fee.

**Question 15 - do you agree with our approach to managing regulatory overlaps?**

27. In our meeting at the LSB in November 2009 we were advised that Third Category regulators would subscribe to a MoU dealing with (inter alia) specific issues of Third Category regulatory overlap.
28. We look forward to discussing the likely format of a draft and are happy to commence preparation of one if agreeable to the LSB.