

**APPLICATION MADE BY THE SOLICITORS REGULATION AUTHORITY BOARD  
TO THE LEGAL SERVICES BOARD UNDER PART 3 OF SCHEDULE 4 TO THE  
LEGAL SERVICES ACT FOR THE APPROVAL OF:**

- **SRA Amendments to Regulatory Arrangements (Accountants' Reports) Rules [2014]**

**A PROPOSED ALTERATIONS**

1. The proposed alterations will:
  - (a) Introduce an exemption from the requirement for all firms to obtain an accountant's report for the small group of firms where the requirement can no longer be justified by the limited risks posed to client money, in that they receive and hold 100% of their client money from Legal Aid Agency work.
  - (b) retain the existing requirement on all other firms to obtain an accountant's report within six months of the end of the accounting period to which the report relates but only require qualified reports to be delivered to the SRA within the same timeframe.
  - (c) Update the format of the accountant's report to remove unnecessary information fields.
2. If approved, the changes will come into effect on 31 October 2014.

**B NATURE AND EFFECT OF THE SRA's CURRENT ARRANGEMENTS**

3. The Accounts Rules impose a general obligation on all firms holding client money to obtain and deliver to the SRA an accountant's report .
4. Around 9,000 firms hold client money and need to comply with the requirement annually. In 2013, of the 8,622 reports received, 60% were qualified and therefore risk-assessed to determine if further action was necessary. No further action was taken in respect of those reports which were not qualified, as they did not identify any breaches of the Accounts Rules or risks to clients' funds.
5. Accountants are required to complete and sign their report in the form published by the SRA. Feedback has suggested that the current form, which has not been reviewed for some time, contains unnecessary information fields, which are time-consuming to complete.

**C. NATURE AND EFFECT OF THE PROPOSED AMENDMENTS TO THE CURRENT ARRANGEMENTS**

6. The proposed amendments would have the following effect:
- (a) approximately 150 firms which receive and hold 100% of their client money from Legal Aid Agency work, would no longer be required to obtain an accountant's report;
  - (b) only those firms whose accountant's reports are qualified would be required to deliver a copy to the SRA; and
  - (c) the form of accountant's reports would be streamlined by the removal of unnecessary information fields.
7. A copy of the SRA Amendments to Regulatory Arrangements (Accountants' Reports) Rules [2014] is attached at annex 1.

**D. RATIONALE FOR THE PROPOSED AMENDMENTS**

8. The SRA Board's recent policy statement "[Approach to regulation and its reform](#)" sets out a clear framework and rationale for a programme of reform. The statement outlines an immediate programme of work designed to:
- remove unnecessary regulatory barriers and restrictions and enable increased competition, innovation and growth to better serve the consumers of legal services;
  - reduce unnecessary regulatory burdens and cost on regulated firms;
  - ensure that regulation is properly targeted and proportionate for all solicitors and regulated businesses, particularly small businesses.
9. Having considered the feedback to a consultation exercise earlier in the year, the Board has concluded that the current arrangements requiring firms to obtain an accountant's report provide an important element of independent oversight, however it has also concluded that the requirement on all firms holding client money to deliver an accountant's report to the SRA is not sufficiently proportionate or targeted.
10. The proposed amendments represent the first phase of a programme of work which will culminate in a review of the Accounts Rules to be implemented through rule changes in April 2016. Details of phases two and three are set out below:

*Phase two – April 2015*

- Amend the Accounts Rules to reflect revised criteria for the circumstances in which accountant's reports need to be qualified
- Issue a fully revised format for the accountant's report
- Amend the overseas provisions of the Accounts Rules where necessary

- Consider whether there are further categories of firms we can exclude from the requirement to obtain an accountant's report

*Phase three – April 2016*

- Conduct a full review of the Accounts Rules to be implemented through rule changes in April 2016
11. Consumer confidence in the legal services market is underpinned by an expectation that client money will be safeguarded. This protection is primarily delivered through an obligation to comply with the SRA Accounts Rules 2011 (the Rules), which set out detailed requirements for the handling of client money. The current proposals do not change the substantive detail of those Rules. In fact, these proposals signal the start of a longer-term programme of work to review them in their entirety to ensure they are fit for purpose.
  12. The rationale for our changing approach to regulation is the need to focus on provisions which are both targeted and proportionate, recognising that regulation which goes further can create unjustifiable costs for legal firms which are then passed onto consumers and may impact on wider access to justice.

**Supporting the constitutional principle of the rule of law**

13. These proposals will have a neutral impact on the constitutional principle of the rule of law.

**Improving access to justice**

14. These measures are these measures are designed as part of an overall package of reforms to reduce unnecessary burdens for legal services providers and their clients. Research<sup>1</sup> has shown that both individual consumers and small businesses currently struggle to access affordable legal services. We accept that these measures are only one part of the process and that we will need to go further in seeking to affect the market to increase competitiveness. However, decreasing the regulatory burden whilst increasing access to justice for consumers is not a question of taking only one step. Instead, it will take a series of incremental reforms across a range of areas and this policy change needs to be seen in that context

**Protecting and promoting the interests of consumers**

15. It is important to acknowledge that the protection of consumers' interests goes beyond an objective of simply safeguarding their money. Their interests are protected more broadly by being able to access affordable legal services which deliver appropriate outcomes with competence and integrity. Such access is secured not only by making services available and affordable, but also through establishing consumer confidence in the wider legal system and legal services providers.

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<sup>1</sup> See 2013 'Small business legal needs survey'  
<https://research.legalservicesboard.org.uk/reports/consumers-unmet-legal-needs>

16. It has been suggested that the removal of a blanket requirement to deliver accountants' reports will result in a reduction in consumer protection and consumer confidence because it will remove a deterrent to non-compliance with the Rules. We consider the amendment to our proposals to require the delivery of qualified reports will effectively mitigate this risk.

### **Encouraging an independent, strong, diverse and effective legal profession**

17. BME solicitors continue to be disproportionately over-represented in sole practices and the smallest firms<sup>2</sup>. It is therefore important to consider the impact of these proposals on smaller firms.
18. It is probable that many firms would have continued to commission an accountant's report were the original proposals removing this requirement have gone ahead. Under the revised proposals, these firms will only have to deliver qualified reports to us and a section of firms will be exempt from the requirement altogether. We consider this to be a targeted and proportionate response to the risks posed. Further, in our response to consultation, we have signalled a clear long-term strategy to more clearly define the criteria for qualification, which will give firms greater certainty as to the areas we will focus upon.
19. We therefore believe that proceeding with this proposal will help implement recommendation 20 of the Independent Comparative Case Review (ICC) report commissioned by the SRA and published in March 2014:
- (a) Publish proposals to reduce the regulatory burden for small firms and to improve our engagement with, and regulation of, them.
  - (b) Pursue a programme of regulatory reform to ensure our regulation is more targeted and proportionate.

### **Increasing public understanding of the citizen's legal rights and duties**

20. These proposals will have a neutral impact on public understanding of the citizen's legal rights and duties

### **Promoting and maintaining adherence to the professional principles**

21. The proposals do not reduce or dilute the obligation to comply with the SRA Accounts Rules or with the broader requirements in the Code of Conduct and Handbook to safeguard clients' monies and protect their interests.

## **F. STATEMENT IN RESPECT OF THE BETTER REGULATION PRINCIPLES**

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<sup>2</sup> 50.5% of BME solicitors work in sole practices or firms with 2 to 4 partners compared to 28.7% of White European solicitors and 30% of BME solicitors work in firms with 26 or more partners compared with 42.6% of White European solicitors <https://research.legalservicesboard.org.uk/wp-content/media/Review-of-published-evidence-on-the-equality-of-pay-in-legal-services-Final.pdf>

22. These measures support the better regulation principles of being targeted and proportionate. They remove a blanket requirement to deliver accountants' reports, which applies to all firms regardless of the risk they pose, and put in place a more targeted requirement for reports to be obtained and delivered to us only where necessary.

#### **G. STATEMENT IN RELATION TO DESIRED OUTCOMES**

23. The changes with respect to accountants' reports are being made in accordance with the programme of reform set out in the SRA Board's recent policy statement "[Approach to regulation and its reform](#)".

#### **H. STATEMENT IN RELATION TO IMPACT ON OTHER APPROVED REGULATORS**

24. We have not identified any adverse impact on people regulated by other approved regulators.

#### **I. IMPLEMENTATION TIMETABLE**

25. If approved, the changes will come into effect on 31 October 2014.

#### **J. STAKEHOLDER ENGAGEMENT**

26. In May 2014 the SRA consulted on proposals to remove the mandatory requirement to deliver an accountant's report to introduce an obligation for COFAs to sign a declaration that they were satisfied that their firms were managing their client account in accordance with the Accounts Rules.
27. The consultation elicited a large number of responses and led to the opportunity to engage with stakeholders at meetings and events during the consultation period. A copy of the summary of consultation responses and SRA conclusions is attached as an annex to the Board paper.
28. Stakeholder feedback was carefully considered by the Board and the proposals were substantially amended to reflect it.

#### **ANNEXES**

- Annex 1:** SRA Amendments to Regulatory Arrangements (Accountants' Reports) Rules [2014] (attached separately)
- Annex 2:** SRA Board paper (attached separately)

**SRA CONTACT FOR MATTERS RELATING TO THIS APPLICATION**

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Date: 25 September 2014.