

Regulatory restrictions on business ownership

**A review of the rules that prevent lawyers from owning or
being connected to other businesses**

October 2014

This paper will be of interest to:

Approved regulators and related disciplinary tribunals

The Judiciary of England and Wales

Providers of Legal Services

Legal Representative Bodies

Legal Advisory Organisations

Third Sector Organisations (representing the interests of consumers or providers of legal services)

Consumer Groups

Law Schools/universities

Law students (and prospective students)

Legal and regulatory Academics

Members of the Legal Profession

Accountancy Bodies

Potential new entrants to the ABS market

Government departments

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1. Executive summary

- 1.1. This report concludes the first of three thematic reviews that the Legal Services Board's (LSB) 2014/15 business plan said we would conduct. This thematic review considers the extent that regulation by legal services regulators unnecessarily prevents legal services providers from being connected with, investing in and owning a range of businesses.
- 1.2. In completing this review we considered the following issues:
 - Does statute require regulators to restrict legal services providers from being connected with other businesses?
 - Are regulatory restrictions to prevent legal services providers being connected with other businesses compatible with the regulatory objectives of the Legal Services Act 2007 (the Act) and would such restrictions be consistent with the better regulation principles?
 - Do the regulators have regulations that restrict legal services providers from being connected with other businesses, and, if so, what is the rationale for such restrictions?
 - If regulators do restrict legal services providers from being connected to other businesses can those restrictions be justified by any statutory requirements, are they compatible with the regulatory objectives and are they consistent with the better regulation principles?
- 1.3. The purpose of this document is to set out our understanding of the regulatory restrictions placed on legal services providers from owning an interest in or being connected with other businesses. We have sought to understand the rationale of any such restrictions and whether they can be justified against the regulators' statutory duties. Our conclusions will inform our engagement with regulators and our approach to any future rule change applications from the regulators.
- 1.4. There are at least ten pieces of primary legislation (including the Act) governing the regulation of legal services providers in England and Wales.¹ In the course of this work the LSB has reviewed all relevant statutes, secondary legislation and has considered whether there are any relevant judicial interpretations. **We have concluded that there is nothing currently in statute that requires a regulator to restrict legal services providers' ability to be connected with, invest in or own any other business.**
- 1.5. However, the Act does require regulators to act in a manner compatible with the eight regulatory objectives in it and to have regard to the better regulation principles. In order to act in manner compatible with the regulatory objectives it may be appropriate for a regulator to restrict those it regulates from being connected with other businesses. Any such restrictions should also be consistent with the better regulatory principles. The LSB can use its

¹ Primary legislation includes: The Ecclesiastical Licences Act 1533, the Public Notaries Act 1843, the Solicitors Act 1974, the Senior Courts Act 1981, the Administration of Justice Act 1985, the Copyright, Designs and Patent Act 1988, the Court and Legal Services Act 1990, the Trade Marks Act 1994, the Legal Services Act 2007 and the Crime and Courts Act 2013.

enforcement powers if, after investigation, it considers that a regulator's actions are having, or may have, an adverse impact on one or more of the regulatory objectives.

- 1.6. **Research shows that individual consumers do not know what is regulated; they assume that all legal services are regulated in some way.**² However, not all legal services are regulated. It may be the case that the risk of consumer confusion about what is and isn't regulated will be increased if connections between legal services providers and other businesses exist. But no research exists showing whether this is the case or not. It is possible for a disreputable business to refer a consumer from a regulated legal business to an unregulated business for a service without disclosing the change in regulatory protections. The individual may then be confused, particularly if the individual is vulnerable.
- 1.7. **The LSB considers that there may be some circumstances in which the regulatory objectives are served by the imposition of additional requirements on legal services providers that are connected to other businesses.** Where there is evidence that there is a high risk of consumer detriment, specific restrictions on the connections with other businesses may be justified in order to ensure that consumers' interests are protected and promoted. However, any such restrictions must be proportionate and targeted. In deciding whether to impose any restrictions, regulators must also balance the conflicting (and sometimes contradictory) implications of the other regulatory objectives.
- 1.8. **The LSB does not consider that there is any evidence to justify blanket restrictions on authorised persons being connected with, investing in or owning other businesses.** Our view is that it is possible for separate, reputable businesses to conduct their affairs in ways that support the regulatory objectives and do not lead to consumer detriment. In those cases, regulators should not restrict legitimate commercial activities. We consider that in such circumstances regulatory restrictions place legal services providers at a competitive disadvantage and reduce consumer choice. One of the significant issues in the market is the level of unmet legal need. Half of the public will have a legal problem in a three year period, yet only 20% will use a lawyer to solve that legal problem, 35% will not seek any advice and 13% will do nothing.³
- 1.9. Of the current legal services regulators, the Costs Lawyers Standards Board (CLSB), the Institute of Accountants in England and Wales (ICAEW) and ILEX Professional Standards (IPS) do not impose any restrictions on legal services providers to prevent them from being connected with, investing in or owning other businesses. The Bar Standards Board (BSB), the Council for Licensed Conveyancers (CLC) and the Intellectual Property Regulation Board

² Page 10, Vanilla Research (January 2013), Risk and the role of regulation, http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Vanilla%20Research%20Risk%20and%20Regulation%20final.pdf

³ BDRC continental (June 2012), Legal Services Benchmarking, <https://research.legalservicesboard.org.uk/wp-content/media/2012-Individual-consumers-legal-needs-report.pdf>

(IPReg) operate, or intend to operate, a notification process. Following notification these regulators may, depending on the risks posed to consumers, impose conditions, grant certain permissions or supervise the regulated entity differently.

- 1.10. **The Master of the Faculties and the Solicitors Regulation Authority (SRA) impose specific restrictions to prevent legal services providers from being connected with, investing in or owning other businesses.** The Master of the Faculties restricts notaries from being appointed representatives for regulated financial services companies but allows any other connection providing there is full disclosure to consumers. There are also other requirements to reduce consumer confusion. The SRA restricts those it regulates from being connected with certain types of separate business activities but allows them to provide others so long as there is disclosure to consumers and appropriate separation.
- 1.11. We have seen no evidence that the SRA has sought to assess whether these restrictions are consistent with the requirement to promote competition and to improve access to justice. The LSB also considers that because of the way the SRA's rules are framed and how they operate in practice they are unlikely to be consistent with the better regulation principles. This is because they do not appear to be proportionate, consistent or targeted. Our view is supported by the fact that the particular restriction has been waived by the SRA in a significant number of cases. For example, according to LSB analysis of information provided to it by the SRA, 17% of alternative business structure (ABS) licence holders as well as 4 (recognised body) law firms regulated by the SRA have been granted waivers from the separate business rule.
- 1.12. The SRA's recent policy statement acknowledges that existing requirements have not been considered against the requirements of the Act and suggests a willingness to look again at the operation of its current restrictions. It stated that: *the SRA will take the approach that the continuation of any existing regulatory intervention needs to be justified, rather than one of focusing on justifying its removal.*⁴ We welcome this perspective and are pleased that the SRA has acknowledged that the separate business rule is in need of review. We hope that this report assists with the SRA's and other regulators' endeavours.
- 1.13. We consider that those regulators that operate a 'notification and conditions' process are more likely to be operating in line with the better regulation principles than those with specific restrictions. However, any conditions imposed by regulators on legal services providers must be transparent, consistent and proportionate to the risk posed.
- 1.14. More generally, we consider that disclosure by providers when referring individuals to unregulated connected companies is likely to be the most

⁴ Page 10, Solicitors Regulation Authority (May 2014), *Approach to regulation and its reform*, http://www.legalservicesboard.org.uk/about_us/board_meetings/pdf/20140522_22_May_2014/14_29_The_SRA's_Approach_To_Regulation_AnxA.pdf

appropriate way to protect consumer interests and reduce the risk of consumer confusion.

- 1.15. **We expect regulators to review their current restrictions and processes against the regulatory objectives and consider what changes can be made.** We understand that SRA intends to review the separate business rule and we support this initiative.⁵
- 1.16. We also encourage other regulators, working collaboratively where appropriate, to review the issues raised by this paper. In particular, the need to consider the most appropriate regulatory approaches to deliver the outcome that consumers understand what is regulated and what is not. Research shows that consumers lack understanding in this area. This is relevant for all regulated legal services providers; however, it is amplified when services are provided by a firm connected to a regulated legal service provider.

⁵ Paul Philip (4 September 2014), *speech to Westminster Legal Policy Forum keynote seminar: The future of legal services regulation*, <http://www.sra.org.uk/sra/news/events/conference-2014-09-04-westminster-legal-policy-forum.page>

2. Introduction

- 2.1. The LSB's business plan for 2014/15 committed us to a series of thematic reviews. The purpose of the reviews is to assess whether certain regulatory or statutory requirements imposed on lawyers are consistent with the regulatory objectives of the Act and the better regulation principles.⁶
- 2.2. The thematic reviews we have decided to undertake focus on regulatory requirements imposed on lawyers by their regulators that appear to be unnecessarily restrictive and to identify and share best practice by regulators. We undertook a prioritisation exercise to determine which thematic reviews would be completed during 2014/15. We concluded that we would look at:
 - The extent to which it may be possible to revise parts of schedule 13 to the Act to make the ownership tests for ABS more targeted and proportionate.
 - The extent to which restrictions on forms of practice are consistent with section 15 to the Act about when an entity needs to be authorised to provide reserved legal services to the public or a section of the public.
 - The extent to which regulation unnecessarily prevents legal services providers from being connected with, investing in and owning a range of businesses.
- 2.3. This report contains the results of the third thematic review listed above. We decided to undertake this review because we were concerned that some of the restrictions in place might not be evidence-based, proportionate or targeted. As a result, they might not be in consumers' interests if they prevent legal services providers offering services that consumers may require. They might also have an adverse effect on the regulatory objective of promoting competition by restricting lawyers' ability to compete with unregulated providers offering such services.
- 2.4. We considered that such arrangements may be putting existing legal businesses at a competitive disadvantage because they may lack the freedoms that are afforded to unregulated providers or those regulated by approved regulators with a more liberal approach. We also considered that such restrictions may hamper innovative and more efficient services offerings for consumers and so have a negative impact on access to justice.⁷ However, we determined that more work was necessary to understand the extent of such restrictions, the rationale for those restrictions, the impact of those restrictions (positive as well as negative) and to consider possible alternatives to the restriction of activities.

⁶ Page 15 - 18, LSB (April 2014), *Business Plan 2014/15*,

http://www.legalservicesboard.org.uk/news_publications/publications/pdf/20140408_LSB_2014_15_Business_Plan.pdf

⁷ Page 4-5, LSB (20 June 2011), LSB decision notice – licensing authority designation under Part 1 of Schedule 10 to the Legal Services Act (2007), http://www.legalservicesboard.org.uk/what_we_do/regulation/pdf/la_decision_notice_1.pdf

- 2.5. This report sets out our understanding of the issue under consideration and explores the reasons and potential rationale for imposing rules that stop lawyers from being involved with other commercial entities. We also look at whether and how legal services regulators impose such restrictions. The structure of the report is as follows:
- The report begins by explaining the issue and briefly covers some of the reasons why restrictions on ownership have been supported in the past.
 - We then consider whether restricting the businesses that lawyers can own or have an interest in is a statutory requirement or whether there is any relevant case law.
 - We then assess whether the Act's requirement for regulators to act in a way that is compatible with the regulatory objectives and to have regard to the better regulation principles justifies restricting the businesses lawyers can be involved in.
 - A brief summary of the current restrictions imposed on lawyers by legal services regulators is then provided.
 - We then consider whether the legal services regulators' approaches are likely to be compatible with the regulatory objectives and if they are consistent with the better regulation principles.
 - Finally we conclude and provide details of next steps.

3. Business ownership restrictions

- 3.1. This section covers what we mean by business ownership restrictions in the context of legal services providers. We consider some of the main arguments in favour of such restrictions being in place in the legal services market and the arguments against.
- 3.2. The LSB's use of the term business ownership restrictions refers to any restrictions placed on those that are authorised to provide reserved legal activities to stop them from owning or participating in businesses providing other services.
- 3.3. There are a number of arguments as to why it is considered desirable to restrict lawyers from owning or involving themselves in other entities that are not necessarily regulated by a legal services regulator. The most prevalent is that a consumer that has purchased legal services from a lawyer and then receives services from a firm which the same lawyer owns or is connected to (but which is not regulated by a legal services regulator) may not realise that these services are not regulated. In these circumstances the consumer may not have access to the legal ombudsman or other regulatory protections.
- 3.4. Confusion can arise because there are a number of services that may be considered by consumers to be legal services but are not required to be regulated by legal services regulators. This is because there are only a limited number of legal services that are regulated by statute. For example, (in most circumstances) if an individual were buying a property, the conveyance must be carried out by an individual or entity authorised by a legal services regulator to provide that service. However, were the same individual to purchase a will, they could choose a provider regulated by a legal services regulator or a completely unregulated provider. If the individual chooses the unregulated provider the individual will only have recourse to general consumer protections and not the protections offered by legal services regulation such as access to the legal ombudsman.
- 3.5. If a regulated lawyer were allowed to own or be connected with a firm offering services that are considered by the consumer to be legal services then the consumer may assume that the services provided by the separate entity are also regulated because of this connection. Those who argue in favour of restrictions consider that this confusion is amplified if the individual has a pre-existing relationship with the regulated lawyer or the regulated law firm where this individual works.⁸
- 3.6. There are a number of arguments that have been made against the imposition of restrictions on lawyers being connected or owning other

⁸ Legal Futures (20 February 2013), *Exclusive: SRA rejects LSB call for review of separate business rule*, <http://www.legalfutures.co.uk/latest-news/exclusive-sra-rejects-lsb-call-review-separate-business-rule>; The Guardian (6 April 2011), *Consumers warned over deregulation of legal services*, <http://www.theguardian.com/money/2011/apr/06/consumers-warned-deregulation-legal-services>; and, Page 16, Legal Ombudsman (March 2013), Report under section 120 of the Legal Services Act 2007: complaints outside the Legal Ombudsman jurisdiction, http://www.legalservicesboard.org.uk/about_us/board_meetings/pdf/paper_13_25_ceo_progress_report_apr_2013_anx_b.pdf

companies. The most forceful is that it is a restraint of trade.⁹ Other arguments include that such restrictions negatively impact consumers because lawyers are not permitted from partnering with other services providers to offer services in an integrated and more efficient manner. By offering complementary services through connected businesses the costs of marketing, client acquisition and other fixed costs can be shared between the legal services provider and the connected services provider. These savings can then be passed onto consumers.

- 3.7. It also argued that regulated legal providers are the only profession prevented from being connected with other businesses. For instance there is nothing to stop an accountant having an interest in a financial advice provider or a dentist from being connected to a cosmetic surgeon. Doctors are allowed to have financial interests in organisations providing healthcare services (including care homes and pharmacies). This interest must not affect the healthcare decisions made by the doctor and they are required to be open and honest with patients about any connections,¹⁰ but there are no restrictions. Co-location of pharmacies and general practitioner services can be beneficial to patients and make the provision of healthcare services in less populous areas possible.
- 3.8. The final, and most current argument, is that since the arrival of ABS licensing non-lawyers (whether individuals or firms) are able to own and / or manage firms providing regulated legal services as well as their own organisations. But, if there are restrictions on existing lawyers from owning or being connected to other firms then existing lawyers are at a competitive disadvantage in comparison. For example a wealth manager will be able to invest in a regulated law firm but a regulated law firm will not be able to invest in a wealth manager.
- 3.9. In this section we have set out what we mean by business ownership restrictions on lawyers and the main arguments in favour of such restrictions and those against. The next two sections cover whether such restrictions are required by existing statute or any requirements under the Act.

⁹ Law Society Gazette (May 2014), *PI lawyers start challenge to MoJ's whiplash plans*, <http://www.lawgazette.co.uk/practice/pi-lawyers-start-challenge-to-moj-s-whiplash-plans/5041221.article>

¹⁰ General Medical Council (2013), *Financial and commercial arrangements and conflicts of interest (2013)*, http://www.gmc-uk.org/guidance/ethical_guidance/21161.asp

4. Statutory basis

- 4.1. There are at least ten pieces of primary legislation (including the Act) that govern the regulation of lawyers in England and Wales.¹¹ There are also a number of pieces of secondary legislation and a number of court judgments. The LSB has reviewed this legislation to determine whether any specific requirements of statute require legal services regulators to restrict lawyers from having an interest or being connected to another business.¹²

*The Legal Services Act 2007*¹³

- 4.2. The Act applies to all approved regulators and licensing authorities overseen by the LSB.
- 4.3. The Act sets out the circumstances in which a person must be authorised by an approved regulator or licensing authority (a legal services regulator) in order to carry out a reserved legal activity (sections 14 to 19). It also defines what a reserved legal activity is (section 12 and schedule 2) and what a legal activity is (section 12). The Act is clear that if reserved legal services are being provided (as part of an entity's business) to the public or to a section of the public then the entity must be authorised by an approved regulator or licensing authority (unless they are exempt) (section 15).
- 4.4. The approved regulators and licensing authorities are able to make regulatory arrangements that those authorised to carry out reserved legal activities must follow (section 21 and section 83).
- 4.5. An approved regulator must, so far as is reasonably practicable, act in a way which it considers is compatible with the regulatory objectives and it must have regard to the better regulation principles (and any other principle that it considers represents best regulatory practice) (section 28).
- 4.6. There is nothing in the Act that explicitly restricts authorised persons from owning or having an interest in other businesses.

*The Solicitors Act 1974*¹⁴

- 4.7. The Solicitors Act (as amended) applies to solicitors regulated by the Solicitors Regulation Authority (SRA).
- 4.8. There are no specific requirements in the Solicitors Act that prevent a solicitor from owning an interest in or being connected with other businesses. There is no requirement on the SRA to make rules to restrict the businesses that

¹¹ Primary legislation includes: The Ecclesiastical Licences Act 1533, the Public Notaries Act 1843, the Solicitors Act 1974, the Senior Courts Act 1981, the Administration of Justice Act 1985, the Copyright, Designs and Patent Act 1988, the Court and Legal Services Act 1990, the Trade Marks Act 1994, the Legal Services Act 2007 and the Crime and Courts Act 2013.

¹² The LSB is aware of ongoing work by the Ministry of Justice to establish greater independence between those who produce medical reports in relation to personal injury claims and law firms and others involved in such claims. This may involve changes in statute to restrict the extent that lawyers can own or be connected with such businesses. However, given that this work by the Ministry of Justice has yet to result in changes to statute we have not considered it as part of this report.

¹³ Legal Services Act 2007: <http://www.legislation.gov.uk/ukpga/2007/29/contents>

¹⁴ Solicitors Act 1974: <http://www.legislation.gov.uk/ukpga/1974/47/contents>

solicitors can be involved in although it has the discretion to do so. In general the use of the term “*may*” for many areas of regulation affords the SRA some level of discretion about what rules and restrictions it chooses to impose on solicitors. This is made more obvious as the legislation uses “*shall*” in relation to the provisions on client money.

- 4.9. The Solicitors Act allows the SRA to make rules for regulating any matter of professional practice, conduct, fitness to practise and discipline of solicitors. It also allows it to investigate whether these rules have been complied with (section 31). It “*may*” make rules about professional indemnity insurance (section 37), compensation grants (section 36) and accountants’ reports (section 34). The Solicitors Act states that the SRA “*shall*” make rules in relation to the operation of client accounts and the keeping of client money (section 32). The Solicitors Act extends these rules to include the employees of solicitors (section 34). It also allows the SRA to either make, or to make an application to the Solicitors Disciplinary Tribunal (SDT) for it to make, an order to prevent non-solicitor employees or consultants from working in solicitors firms, except where they have the SRA’s permission to do so, if they have been involved in wrongdoing (section 43).
- 4.10. There are specific requirements for solicitors that wish to practise as a sole practitioner. They must have an endorsement on their practising certificate and follow any relevant rules made by the SRA. These rules must prescribe when a solicitor can be regarded as suitable to practise as a sole solicitor (section 1). It is also allowed to impose conditions on practising certificates requiring solicitors to take or to not take specific steps specified by the SRA (section 120 and section 13A). These requirements are currently in the process of being amended through the use of a section 69 order under the Act. This will lead to the situation where a sole practitioner will be subject to the same type of authorisation as other SRA regulated entities.

The Administration of Justice Act 1985 (AJA)¹⁵

- 4.11. The AJA applies to solicitors and licensed conveyancers. For solicitors it is primarily concerned with the regulation of SRA regulated entities. For licensed conveyancers it covers most aspects of their regulation.
- 4.12. The AJA does not have any provisions requiring the SRA to make rules restricting the right of solicitors or those involved in recognised bodies or legal services bodies from having an interest in or being connected to another business. The AJA does not contain any provisions requiring the CLC to restrict licensed conveyancers or licensed conveyancer bodies from having an interest or being connected to another business.
- 4.13. The relevant sections of the AJA (in terms of this document) were inserted by the Act. The AJA allows the SRA to regulate legal services bodies and recognised bodies (or incorporated practices in the language of the AJA). Recognised bodies are SRA regulated entities in which all of the owners and

¹⁵ Administration of Justice Act 1985: <http://www.legislation.gov.uk/ukpga/1985/61/contents>

managers are authorised persons. Legal services bodies (often referred to as Legal Disciplinary Practices or LDPs) are entities regulated by the SRA which have up to 25% non-lawyer ownership and / or management. The AJA allows the SRA to make rules about the management and control of recognised bodies and legal services bodies and to make rules about which bodies may be authorised and their ongoing compliance requirements (section 9).

- 4.14. The AJA states that when the SRA makes rules about recognised bodies and legal services bodies it “*must*” make rules that require that they do not provide any services other than solicitor services or other relevant legal services (however the SRA “*may*” also make rules containing exceptions to this requirement). Solicitor services are defined as professional services such as those that are provided by individuals practising as solicitors or lawyers of other jurisdictions. Relevant legal services include the activities of other authorised persons (such as barristers) and those employed in recognised bodies. The SRA is allowed by rules to define what services are not to be treated as solicitor services or relevant legal services (section 9).
- 4.15. The result of this is that any activity carried out by the SRA regulated entity that is a “*solicitor service*” may be regulated by the SRA, unless the SRA chooses to introduce exceptions to what is and what is not considered a “*solicitor service*.” The corollary of this is twofold. Firstly, the SRA need not regulate the services provided by recognised bodies that are not the sort of services normally provided by solicitors. Secondly, these requirements do not extend to bodies that are owned or are in some other way connected to the SRA regulated body.
- 4.16. The AJA provides the legislative framework for the CLC and for the regulation of licensed conveyancers. The AJA gives the CLC the power to make rules about the regulation of licensed conveyancers (section 20, 21 and 22) and prescribe the training requirements for licensed conveyancers (section 13). The CLC is also able to make rules regulating those working with licensed conveyancers to provide conveyancing services to the public (section 20).
- 4.17. The AJA allows the CLC to make rules regarding the management and control of licensed conveyancing bodies and prescribe the requirements for an applicant to be recognised as a licensing conveyancing body. This includes rules related to the provision of conveyancing services and relevant legal services. Relevant legal services is defined as including services such as those carried out by authorised persons (such as solicitors and barristers) and is not limited to the reserved legal activities in the Act (section 32A). Akin to the Solicitors Act, in the AJA the term “*may*” is used for many areas of regulation. This gives the CLC a level of discretion about whether to make rules regarding licensed conveyancers. This is made more obvious as the legislation uses “*shall*” in relation to the provisions requiring rules on client money.
- 4.18. The AJA does give the CLC the power to make rules about the regulation of the sort of services offered by authorised persons regardless of whether they are reserved legal activities or not. However, the AJA does not require the CLC to make such rules.

Copyright Designs and Patents Act 1988 (CDPA)¹⁶

- 4.19. This legislation includes provisions related to the regulation of patent attorneys. The legislation allows the keeper of the register of patent attorneys (IPReg by delegation from the Chartered Institute of Patent Attorneys (CIPA)) to make rules for the regulation of the practice, conduct and discipline of patent attorneys (section 275A). The CDPA does not contain any provisions requiring IPReg, as keeper of the register, to restrict patent attorneys from having an interest in or being connected to another business. No other provision is directly targeted at restricting patent attorneys from being connected with other business activities.

The Courts and Legal Services Act 1990 (CLSA)¹⁷

- 4.20. This legislation includes provisions related to the regulation of notaries by the Master of the Faculties. Section 54 gives the Master of the Faculties the power to make rules for the regulation of the practice, conduct and discipline of public notaries. The CLSA does not contain any provisions requiring the Master of the Faculties to restrict public notaries from having an interest in or being connected to another business. No other provision is directly targeted at restricting notaries from being connected with other business activities.

Trade Marks Act 1994 (TMA)¹⁸

- 4.21. This legislation includes provisions related to the regulation of trade mark attorneys. The legislation allows the keeper of the register of registered trade mark attorneys (IPReg by delegation from Institute of Trade Mark Attorneys (ITMA)) to make rules for the regulation of practice, conduct and discipline of trade mark attorneys when they are carrying out trade mark agency work (section 83A). Trade mark agency work is defined as applying and obtaining registered trademarks in the UK or overseas and conducting proceedings in relation to trade marks. This includes reserved legal activities as well as the unreserved legal activity of applying for a registered trade mark. The TMA does not contain any provisions requiring IPReg, as keeper of the register, to restrict trade mark attorneys from having an interest or being connected to another business. No other provision is directly targeted at restricting trade mark attorneys from being connected with other business activities.

Other relevant statutes and court judgments

- 4.22. A review of other relevant statutes, including, the Crime and Courts Act 2013, the Senior Courts Act 1981, the Public Notaries Act 1843 and the Ecclesiastical Licences Act 1533, and court judgments did not uncover any provisions related to restrictions being placed on authorised persons in relation to having an interest or being connected to another business.

¹⁶ Copyright, Designs and Patents Act 1988: <http://www.legislation.gov.uk/ukpga/1988/48/contents>

¹⁷ Courts and Legal Services Act 1990: <http://www.legislation.gov.uk/ukpga/1990/41/contents>

¹⁸ Trade Marks Act 1994: <http://www.legislation.gov.uk/ukpga/1994/26/contents>

Conclusion

- 4.23. In conclusion, there are no provisions in statute restricting the rights of authorised persons to have an interest in or be connected to other businesses.
- 4.24. Existing statute does place requirements on the SRA to regulate the activities carried out by the entities it regulates if they are the sort of activities usually provided by solicitors and other authorised persons. However, that does not preclude unregulated bodies providing the sort of services usually provided by solicitors and other authorised persons, providing such services are not reserved legal activities.
- 4.25. There is nothing in statute that restricts legal services providers regulated by the SRA from having an interest in or being connected to a business providing unregulated services that may be considered the sort of services usually provided by solicitors or other authorised persons.
- 4.26. The Act requires that legal services regulators, when discharging their regulatory functions (whether related to the reserved legal activities or otherwise), act in a way that is compatible with the regulatory objectives. It also requires them to have regard to the better regulation principles and to what they consider to be best regulatory practice. This means that legal services regulators may, in order to fulfil these duties, impose restrictions on the services provided by authorised persons and the organisations that they may be connected with, invest in or own. However, such restrictions must be justified with reference to the regulatory objectives and the better regulation principles. The next section of the paper considers whether placing restrictions on the connections that an authorised persons can have is compatible with the regulatory objectives and / or consistent with the better regulation principles.

5. Regulatory objectives and better regulation principles

The regulatory objectives

- 5.1. The LSB, the Office of Legal Complaints and all of the approved regulators must all act, so far as is reasonably practicable, in a manner compatible with the eight regulatory objectives of the Act. Approved regulators are given the freedom to act in a way that they consider most appropriate for the purpose of meeting those objectives. However, the LSB can use its enforcement powers if it considers that an act or omission by an approved regulator has had or might have an adverse impact on the regulatory objectives and it is appropriate to take action.
- 5.2. The regulatory objectives are:
- protecting and promoting the public interest;
 - supporting the constitutional principle of the rule of law;
 - improving access to justice;
 - protecting and promoting the interests of consumers;
 - promoting competition in the provision of services in the legal sector;
 - encouraging an independent, strong, diverse and effective legal profession;
 - increasing public understanding of the citizens' legal rights and duties; and
 - promoting and maintaining adherence to the professional principles of independence and integrity; proper standards of work; observing the best interests of the client; the duty to the court; and maintaining client confidentiality.
- 5.3. The LSB has set out what it considers the regulatory objectives mean and how we consider they apply to the LSB and the approved regulators.¹⁹ None of the approved regulators have attempted a similar exercise, although more recently the SRA has touched on how it views the regulatory objectives in a paper on its approach to regulation and reform.²⁰
- 5.4. To assist the LSB in this thematic review we have undertaken an assessment of the possible impact on the regulatory objectives of placing wide-ranging restrictions on legal services providers being connected with, investing in or owning a range of businesses. We used the regulatory objectives definitions in our published paper and we considered each regulatory objective independently before reaching an overall conclusion.

¹⁹ LSB (2010), *The Regulatory Objectives*,

http://www.legalservicesboard.org.uk/news_publications/publications/pdf/regulatory_objectives.pdf

²⁰ Solicitors Regulation Authority (May 2014), *Approach to regulation and its reform*,

http://www.legalservicesboard.org.uk/about_us/board_meetings/pdf/20140522_22_May_2014/14_29_The_SRA's_Approach_To_Regulation_Anx_A.pdf

5.5. Below is a summary table of our assessment of the impact of regulatory restrictions on business ownership on each of the regulatory objectives. A detailed explanation of the rationale and conclusions of our assessment is available on later pages.

Regulatory objective	Impact on the regulatory objectives	Why?
RO1: Protecting and promoting the public interest	+ / -	It may be in the public interest to reduce the risk of consumer confusion on scope of regulation. But we do not consider that disproportionate restrictions are in the public interest.
RO2: Supporting the constitutional principle of the rule of law	Negligible	Not relevant, Although any relevant rules must be intelligible, clear and predictable.
RO3: Improving access to justice	+ / -	Restrictions on business ownership may lead to increased costs and prevent firms from innovating to provide better services to consumers. Although confusion regarding access to redress may impact consumer confidence.
RO4: Protecting and promoting the interests of consumers	+	Restriction on business ownership may reduce risk of consumer confusion about regulatory scope. However, any restrictions need to be proportionate and targeted at the risks posed to consumers.
RO5: Promoting competition in the provision of services in the legal sector	-	A restriction on business ownership places lawyers at a competitive disadvantage and it damages competition. However, It may be appropriate to restrict some elements of competition but these must be evidence-based and proportionate.
RO6: Encouraging an independent, strong, diverse and effective legal profession	Negligible	Not relevant. However, preventing lawyers from legitimate enterprise may lead them to stop providing reserved legal activities.
RO7: Increasing public understanding of citizens legal rights and duties	Negligible	Not relevant. However, restrictions may reduce consumer confusion.
RO8: Promoting and maintaining adherence to the professional principles ²¹	+ / -	Lawyers being connected to other businesses may lead to the perception that the professional principles are not being upheld. However, there is no evidence that restrictions prevent lawyers from acting unethically.
Overall	-	Regulators, in general, should not restrict connections between legal services businesses and other reputable commercial activities. However, there may be circumstances when restrictions on the types of business a law firm can be associated with are necessary. But any restrictions must be proportionate and targeted on the risk involved.

²¹ The professional principles are those defined by section 1 (3) of the Act as requiring authorised persons to act with independence and integrity; maintain proper standards of work; act in the best interests of their clients; comply with their duty to the court to act with independence in the interests of justice; and, maintain client confidentiality.

RO1 Protecting and promoting the public interest

- 5.6. We consider that business ownership restrictions could protect and promote the public interest when applied proportionately. This is because they may reduce the risk to the public of being confused about whether a service provided by a firm connected to an authorised person is regulated or not.
- 5.7. However, business ownership restrictions will prevent the people to which they apply from carrying out business activities that others have the right to offer. This creates an uneven playing field. It is therefore unlikely that the public interest will be served by the imposition of disproportionate and untargeted regulatory rules that restrict investment and ownership of legitimate enterprises by authorised persons.
- 5.8. The Act and related statutes do not require legal regulators to restrict authorised persons from investing in, owning or having an interest in other businesses. Parliament has had a number of opportunities to extend the scope of legal services regulation to include other activities. It has not done so. It has given regulators the discretion to impose these types of restrictions. But it has also placed requirements on them to have regard to the better regulation principles; this means that any restrictions need to be proportionate, targeted and applied consistently.
- 5.9. Our view is that, while it may be in the public interest to reduce public confusion about whether services are regulated or not, this needs to be balanced against the regulatory objectives of promoting competition and improving access to justice (see below). In any event, we do not consider that it is in the public interest to impose disproportionate and/or untargeted restrictions on the entities that authorised persons may be connected with.

RO2 Supporting the constitutional principle of the rule of law

- 5.10. The LSB does not consider that business ownership restrictions are particularly relevant to this regulatory objective. This is because its aims are more about overarching issues of independence and protection from the state.
- 5.11. However, the LSB's interpretation of the rule of law highlights that regulation should be *intelligible, clear and predictable*.²² Complex regulatory arrangements that restrict ownership of certain businesses by authorised persons create uncertainty for them. The fact that the SRA has issued a large number of waivers from its separate business rule (see paragraphs 7.10 and 7.11) calls into question whether the rationale for its rule is intelligible, clear and predictable.

²² LSB (2010), *The Regulatory Objectives*,
http://www.legalservicesboard.org.uk/news_publications/publications/pdf/regulatory_objectives.pdf

RO3 Improving access to justice

- 5.12. In our judgement, access to justice could be improved by business ownership restrictions. This is because they may reduce possible confusion about when practitioners and activities are covered by legal services regulation and when they are not. Those using regulated services will be able to seek redress for poor service from the legal ombudsman and may be able to seek compensation. This may enhance confidence in using legal services, with a consequential benefit to access to justice. Those not using regulated services will have to pursue redress using existing consumer protection laws which could reduce consumer confidence and undermine access to justice.
- 5.13. However, it also possible that restrictions on business ownership may prevent groups of firms being connected to an authorised person and offering a range of services through different firms (some regulated by a legal services regulator and some not). Such groups may be able to share costs of client acquisition, marketing and other costs. This may enable firms to reduce the costs of their services and so encourage those that would not otherwise seek legal advice to do so. This is a growth opportunity for firms and the resolution of legal problems in a more cost effective manner for business is likely to have a positive impact on economic growth. Regulators will soon be under an obligation to have regard to the need to promote economic growth.²³ Regulations that hamper growth will need to be reconsidered in the light of such an obligation.
- 5.14. Our research shows that half of the public will have a legal problem in a three year period, yet only 20% will use a lawyer to solve that legal problem, 35% will not seek any advice and 13% will do nothing.²⁴ 62% of SMEs handle their legal problems on their own or with friends and family and only 18% of legal problems faced by SMEs resulted in the use of a solicitor.²⁵ This suggests that there is a significant latent demand for legal services. Many consumers cited cost concerns as a reason for not seeking professional advice.²⁶ A reduction in operating costs may enable firms to reduce their charges and so provide legal services to those with legal needs that are not currently using such services.
- 5.15. Based on our assessment we consider that disproportionate and untargeted restrictions placed on the businesses that authorised persons can be connected with, invest in or own may have a negative impact on access to justice. It may lead to increased costs and prevent firms from innovating to provide a better, integrated - or unbundled - service. There is limited evidence

²³ Department for Business Innovation and Skills (January 2014), *Draft guidance: non-economic regulators: duty to have regard to growth*, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/274552/14-554-growth-duty-draft-guidance.pdf

²⁴ BDRC continental (June 2012), *Legal Services Benchmarking*, <https://research.legalservicesboard.org.uk/wp-content/media/2012-Individual-consumers-legal-needs-report.pdf>

²⁵ Pleasence and Balmer (April 2013), *In need of advice? Findings of a small business legal needs benchmarking survey*, <https://research.legalservicesboard.org.uk/wp-content/media/In-Need-of-Advice-report.pdf>

²⁶ Optimisa research (April 2013), *Consumer use of legal services*, <https://research.legalservicesboard.org.uk/wp-content/media/Understanding-Consumers-Final-Report.pdf>

that such restrictions will improve quality.²⁷ However, it is true that in the event of a poor outcome, the options for redress for users of regulated providers of legal services are simpler to use and more comprehensive.

RO4 Protecting and promoting the interests of consumers

- 5.16. It is often suggested that restricting authorised persons from being connected with, investing in or owning a range of businesses is likely to reduce the risk of members of the public being confused about whether a firm offering legal services is regulated or not. This is a compelling argument since preventing connections between authorised persons and unregulated legal services providers helps to prevent the boundaries between regulated and unregulated providers being blurred. This blurring of the boundaries is likely to be amplified if a referral arrangement exists between the two connected companies.
- 5.17. Research suggests that consumers think that all legal services are regulated. Focus groups commissioned by the Legal Services Consumer Panel found that regardless of age, location or legal services experience there was little or no detailed knowledge of the specific protections offered to legal services consumers. Most participants assumed that there was some regulation and that it applied to all providers.²⁸ These findings are supported by research by the SRA that found that consumers were surprised to find out that some legal services were regulated and others were not.²⁹
- 5.18. A logical response to such consumer confusion might be to regulate all activities that consumers think are currently regulated, not simply to restrict the ability of legal services providers to be connected with other businesses. However, Parliament has declined to regulate all legal activities. Alternatively an intervention to improve consumer awareness of the scope of regulation may be desirable. Enhanced disclosure by regulated providers may have a positive impact in such a scenario.
- 5.19. We also consider that it is important to ask whether the restrictions are likely to improve value for money for consumers. It is likely that restricting the businesses that authorised persons can be connected with may drive up their costs and reduce their opportunities for innovation and efficiencies. We have also shown previously in this paper that a significant amount of latent demand exists in the legal services market and that consumers do not consider that they are well served at current prices. This suggests that there is a value for money issue in the sector. However, the extent to which ending business ownership restrictions will deliver better value for money for consumers is not something we have sought to evaluate.

²⁷ Page 9, IFF (2011), Understanding the consumer experience of will writing services, <https://research.legalservicesboard.org.uk/wp-content/media/Will-writing-experiences-2011.pdf>

²⁸ Page 10, Vanilla Research (January 2013), Risk and the role of regulation, http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/Vanilla%20Research%20Risk%20and%20Regulation%20final.pdf

²⁹ Page 25, GFK (February 2011), *Consumer attitudes towards the purchase of legal services*, <http://www.sra.org.uk/sra/how-we-work/consumer-research/summaries/purchase-of-legal-services.page>

- 5.20. On balance, we consider that restricting involvement in other businesses by authorised persons could help to protect the interests of consumers. This is because consumers do not understand what is regulated and what is not. However, any restrictions need to be proportionate and targeted at the risks posed to consumers.

RO5 Promoting competition in the provision of services

- 5.21. We consider that restricting authorised persons from being connected with, investing in or owning a range of businesses could have a negative impact on competition since restricting investment and collaboration may restrict some aspects of what would otherwise be legitimate competition. In some circumstances, it may be appropriate for some aspects of competition to be restricted in order to protect consumers. We would expect such restrictions to be evidence-based and proportionate. We consider that restrictions may have exclusionary side effects on legitimate business structures that would otherwise have the potential to bring significant consumer benefits through diverse delivery methods, new investment and new ways of running firms with better links to clients through association with other services.
- 5.22. There is also a risk that regulations that restrict the ability of legal services providers from being connected with, investing in or owning other businesses have the potential to drive legal services providers away from the provision of reserved legal activities, in order to avoid regulation altogether. This would reduce competition in the market for reserved legal activities.
- 5.23. Specifically we consider that restricting authorised persons from being connected with, investing in or owning a range of businesses places authorised persons at a competitive disadvantage to firms that are providing only unregulated legal services. This may lead to negative outcomes for those competing with such firms and for consumers. However, this has to be balanced with the consumer protection issues discussed above.

RO6 Encouraging an independent, strong and effective legal profession

- 5.24. The LSB does not consider that business ownership restrictions are particularly relevant to this regulatory objective. However, as we have discussed when considering the impact of restrictions on access to justice, such restrictions may have an impact on the ability of authorised persons to innovate and remain profitable.
- 5.25. It may be the case that a legal services provider will only be economically viable if connected to another business offering different services. For instance, information provided by the regulator of notaries to the LSB shows that nearly a quarter of notaries have an annual fee income of under £5000 from their notarial practice. If notaries were restricted from being connected to other businesses and earning more income it is not clear whether they would elect to continue to provide notarial services. This could damage the strength of the profession. The same argument can be made for other providers of legal services.

RO7 Increasing public understanding of the citizen's rights and duties

5.26. The LSB does not consider that business ownership restrictions are particularly relevant to this regulatory objective. But as we showed when considering the objective of protecting and promoting the interests of consumers, the evidence suggests that consumers are currently unsure about what legal services are regulated and what are not. Most consumers assume that all services are regulated. Restrictions may go some way to preventing further confusion or misapprehension, although whether this equates to increasing the public's understanding of their rights and duties is questionable.

RO8 Promoting and maintaining adherence to the professional principles

5.27. This objective is arguably the most debated regulatory objective in relation to placing restrictions on authorised persons preventing them from being connected with, investing in or owning other businesses. Many argue that ownership of other businesses will compromise an authorised person's ability to act with independence and integrity. This is because they may have an economic incentive to refer the client to firms in which the authorised person has an interest and this may not be in the best interest of the client.

5.28. However, such incentives exist regardless of whether there are restrictions on authorised persons being connected with, investing in or owning a range of businesses. If there are restrictions, authorised persons could simply offer the same services from inside the legal services body or have a referral arrangement in place with an external party. There is also a body of thought that argues that, in terms of ethics, lawyers may not be superior to non-lawyers.³⁰ Therefore we do not consider that there is a clear case that restrictions on business ownership protect consumers by restricting the ability of an authorised person to act unethically.

5.29. More positively we consider that strong incentives exist that help to ensure that, regardless of the structure of the legal services business, whether it is connected with other companies or has referral arrangements in place, it benefits by acting ethically. Research shows that the most important factor when choosing a legal services provider is reputation. Nearly 30% choose on this basis and reputation was a factor for 56% of users of legal services. 22% of consumers found their legal provider following the recommendation of a family member or friend.³¹

5.30. We do consider that the involvement, and use, of connected companies by authorised persons may give the impression that the professional principles are not being adhered to. However, it seems unlikely that blanket restrictions will tackle the reasons for such perceptions. For instance, evidence from the Legal Services Consumer Panel tracker survey has shown that less than 50%

³⁰Moorhead (March 2014), *Precarious Professionalism -- Some Empirical and Behavioural Perspectives on Lawyers*. HLS Program on the Legal Profession Research Paper No. 2014-17. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2407370

³¹ Page 34, BDRC continental (June 2012), *Legal Services Benchmarking*, <https://research.legalservicesboard.org.uk/wp-content/media/2012-Individual-consumers-legal-needs-report.pdf>

of people trust lawyers³² and the LSB's SME research found that only 13% of SMEs surveyed considered that lawyers provide a cost effective means to resolve legal issues.³³ Joint research into referral fees suggested that consumers were happy for referral arrangements to remain provided that lawyers were transparent about them and their existence was disclosed.³⁴

- 5.31. We therefore consider that a connection between authorised persons and other businesses may lead to the perception that the professional principles are not being upheld. However, there is no evidence that restrictions prevent lawyers from acting unethically and in any event we do not consider that blanket restrictions are a way of limiting unethical behaviour or of reducing the perception of such behaviour. We consider that more targeted regulatory intervention may be more effective.

Conclusion

- 5.32. Based on this assessment, we consider that regulators need to balance the competing (and sometimes contradictory) implications of the regulatory objectives when considering what, if any, restrictions need to be imposed on authorised persons being connected with, investing in or owning other businesses. Our view is that it is possible for separate, reputable businesses to conduct their affairs in ways that support the regulatory objectives and do not lead to consumer detriment. In those cases, which may well be the majority, regulators should not restrict legitimate commercial activities. However, there may be circumstances in which the regulatory objectives are furthered by imposing restrictions on the types of business a law firm can be associated with; it may be that these restrictions need to be relatively onerous if there evidence that there is a high risk of consumer detriment. But any restrictions must be proportionate and targeted.

The better regulation principles and best regulatory practice

- 5.33. The legal services regulators are required, when discharging their regulatory functions (whether related to the reserved legal activities or otherwise), to have regard to the better regulation principles and to what they consider to be best regulatory practice. Although legal services regulators may, in order to fulfil their wider duties, impose restrictions on the services provided by authorised persons and the organisations that they can have an interest in or be connected with, such restrictions must be consistent with the requirements of better regulation.

³² Optimisa research (April 2013), Consumer use of legal services, <https://research.legalservicesboard.org.uk/wp-content/media/Understanding-Consumers-Final-Report.pdf>

³³ Pleasence and Balmer (April 2013), In need of advice? Findings of a small business legal needs benchmarking survey, <https://research.legalservicesboard.org.uk/wp-content/media/In-Need-of-Advice-report.pdf>

³⁴ Vanilla Research (March 2010), Referral Arrangements Research, http://www.legalservicesconsumerpanel.org.uk/publications/research_and_reports/documents/VanillaResearch_ConsumerResearch_ReferralArrangements.pdf

5.34. The better regulation principles³⁵ are that regulatory activities should be:

- Transparent – regulations should be simple and user-friendly. Policy objectives need to be clearly defined and effectively communicated to all parties.
- Accountable – regulators must be able to justify decisions and be subject to public scrutiny.
- Proportionate – regulators should only intervene when necessary, any remedies should be appropriate to the risk posed, and costs must be identified and minimised.
- Consistent – rules and standards must be joined up and implemented fairly. In addition, regulation should be predictable in order to give stability and certainty to those regulated.
- Targeted only at cases in which action is needed – regulation should be focused on the problem, and minimise side effects.

5.35. Overleaf is a summary table of our assessment as to whether the imposition of restrictions on authorised persons to stop them from being connected with, investing in or owning other businesses is consistent with the better regulation principles. Full explanation of our rationale for each assessment is on the following pages.

³⁵ Better Regulation Task Force (2003), *Principles of Good Regulation*, <http://webarchive.nationalarchives.gov.uk/20100407162704/http://archive.cabinetoffice.gov.uk/brc/upload/assets/www.brc.gov.uk/principlesleaflet.pdf>

Better regulation principle	Observations in relation to regulatory restrictions on business ownership
Transparent	A clear rule restricting ownership of connected businesses by lawyers may be transparent (as would no restrictions). However, administratively complex implementation, more complex restrictions or exemptions are likely to lack transparency.
Accountable	To be accountable, any restrictions on business ownership must be operated consistently with published and clearly explained policy.
Proportionate	A specific and general prohibition on connections between lawyers and other businesses is unlikely to be a proportionate response to the issue of consumer confusion about the scope of regulation. A more proportionate response will be targeted at areas of highest risk and, possibly, complemented with disclosure and requirements to differentiate the separate business (whether through branding or another means).
Consistent	Regulators should work together to apply a consistent approach to connections between regulated legal businesses and other businesses. Regulators should apply a consistent approach in relation to their own decisions. The policies and regulatory decisions regarding any exceptions, waivers or exclusions should be evidence-based and transparent.
Targeted	Regulations should be targeted at the regulatory problem. We consider that the regulatory problem is consumer confusion about the scope of regulation. This could be addressed through targeted referral restrictions, marketing requirements or other disclosure requirements.
Overall	We consider that an approach that imposes restrictions on business ownership for only the areas highest risk complemented with disclosure requirements will be more proportionate and more accurately targeted at the problem of consumer confusion about the scope of regulation. However, restriction requirements based on exemptions may be inconsistent with the better regulation principles of transparency and consistency. This is because they may lack simplicity and predictability.

Transparent

- 5.36. Transparent regulation is simple and user friendly. A requirement that no authorised person can have an interest in or be connected with another business can be said to be simple and user friendly. However, while the requirement may be transparent, how the rule is implemented may lack transparency. For instance its application may be administratively complicated or selective through the use of waivers.
- 5.37. Placing no restrictions on the organisations that an authorised person can be connected with is also simple and user friendly.
- 5.38. Regulation that sits in the middle and imposes restrictions in relation to some activities and not others is much less simple.

Accountable

- 5.39. The better regulation principle of accountability concerns regulators' ability to justify decisions and subject them to public scrutiny. Largely this relates to policy decisions taken by regulators and scrutiny of regulators' performance. However, it does have some relevance to the matter being considered. In relation to restrictions on the connections that authorised persons may have, any restrictions that are operated inconsistently or without published and clearly explained policy is likely to be inconsistent with this better regulation principle.

Proportionate

- 5.40. To act in a manner consistent with the better regulation principle of proportionality policy solutions need to be proportionate to the risk and justify the compliance cost imposed. Outright prohibitions are the strongest regulatory response to a regulatory risk. Therefore restrictions on authorised persons being connected with, investing in or owning other businesses can only be justified if there is sufficient risk.
- 5.41. We have concluded earlier in this paper that a risk of consumer confusion about the scope of regulation does exist from authorised persons being connected with other businesses. However, we do not consider that the most prohibitive regulatory tool is the most appropriate response to this risk. A more proportionate response may be a disclosure regime or a more targeted approach, such as preventing less sophisticated consumers from being referred to connected businesses but not prohibiting the connection.

Consistent

- 5.42. Currently the existence of a number of different regulators with a number of different approaches to the issue of authorised persons being connected with, investing in or owning other businesses will inevitably lead to inconsistencies. These inconsistencies are likely to exacerbate consumer confusion about the scope of regulation of authorised persons and any connected organisations.
- 5.43. More concerning is if individual regulators lack consistency regarding their rules on connections with certain businesses but not others. Exceptions and exclusions within rulebooks, or by decisions taken by regulators, reduce the predictability of regulatory frameworks. It also leads to the possibility that regulations are not implemented fairly. Regulators that allow or prevent connections between authorised persons and other businesses on a case-by-case damage the predictability and fairness of the regulatory regime.
- 5.44. To have regard to the better regulation principle of consistency regulators should work together to apply a common approach to connections between regulated legal businesses and other businesses. Regulators should apply a consistent approach in relation to their own decisions. The policies and regulatory decisions regarding any exceptions, waivers or exclusions should be evidence-based and transparent.

Targeted

- 5.45. To deliver targeted regulation regulators must avoid a scattergun approach. They must clearly define the regulatory problem they are seeking to address and, where possible, only introduce regulations that target that problem. Regulators should also regularly review their regulatory framework to test whether their arrangements are still necessary and effective. If not they should be modified or reworked.
- 5.46. In relation to rules that restrict authorised persons from being connected with, investing in or owning other businesses, we consider that such rules are unlikely to target the policy problem. We have concluded that the policy problem is consumer confusion on regulatory scope of services provided by

those connected to authorised persons. However, to address this issue does not necessarily require a specific restriction on connections. The policy problem could be addressed through restrictions on referral from authorised person to connected organisations, marketing restrictions or consumer disclosure requirements.

Conclusion

- 5.47. The imposition of restrictions on authorised persons to stop them from being connected with, investing in or owning other businesses does not appear to be in line with many of the principles of good regulation. It is unlikely to be proportionate or targeted on the regulatory problem. This is because the policy problem identified is related to consumer confusion. We consider that there are a number of approaches other than prohibition that are more likely to reduce the likelihood of consumer confusion about whether a service connected to an authorised person is regulated or not. A blanket approach restricting the investment decisions of authorised persons is therefore unlikely to be proportionate or targeted and so not consistent with a number of the principles of good regulation.
- 5.48. If a regulator imposes regulations that restrict authorised persons from being connected with some businesses but not others this is also likely to be inconsistent with the better regulation principles of transparency and consistency. This is because it is likely to lack simplicity and predictability.

6. Current regulatory approaches

- 6.1. This section summarises the current regulatory approaches of the regulators to the issue of authorised persons being connected with, investing in or owning other businesses.
- 6.2. We have collected this information by reviewing each regulator’s regulatory arrangements and checking our understanding with each one before publication. We received responses from all regulators to the ‘fact checking’ exercise with the exception of the Intellectual Property Regulation Board and the Master of Faculties.
- 6.3. A summary table of the arrangements in place is shown below:

Regulator	Specific restrictions (do the rules restrict a lawyer from being connected with certain businesses?)	General restrictions (are lawyers restricted from providing unregulated services?)	Notification or conditions (do regulators require notification of connections and/or does permission have to be granted?)	Additional rules on consumer disclosure
BSB	No	Yes (for individuals providing unreserved legal services)	Yes (for entities and for risk assessment use only and for individuals to comply with association rules)	No
CLC	No	No	Yes (a permission may require ring fencing of a separate business)	No
CLSB	No	No	No	No
ICAEW	No	No	No	No
IPReg	No	No	Yes (may impose conditions)	No
IPS	No	No	No	No
Master of the Faculties	Yes (notaries cannot be appointed representatives)	No	No	Yes (and also requirements regarding business names)
SRA	Yes (connections are not allowed with businesses providing some specific services)	No	No	Yes for permitted connections (and requirements to ensure separation)

Bar Standards Board (BSB)

- 6.4. The BSB is responsible for regulating practising barristers, registered European lawyers and it is also able to regulate registered foreign lawyers on a temporary basis (this does occur that regularly). It is a “qualifying regulator” and is therefore able to regulate immigration and asylum advice. Practising barristers can be classed as self-employed (within chambers or as a sole practitioner) or employed (in an authorised or non-authorised body). Being employed in an authorised body includes any entity authorised by another regulator, and includes being a ‘manager’ (i.e. partner, director etc) within that entity. Barristers specialise in providing advocacy services but can also provide a number of other reserved legal activities, including litigation, probate and conveyancing. Very often they provide legal advice and opinion. The BSB also has a role in regulating non-practising barristers now known

as unregistered barristers. It does not currently regulate entities (although it has applied to the LSB to be granted the right to do so) and it is not a licensing authority for ABS (although it has plans to apply to be designated as a licensing authority).

- 6.5. The BSB does not restrict the right of barristers to be connected with, invest in or own other businesses. However, as the BSB currently focuses on regulating individuals it does regulate the legal services (whether or not reserved legal activities) provided by practising barristers regardless of what entity it provides them from. It also restricts them from providing legal services from unauthorised bodies (although there are also a limited number of exemptions to this).³⁶ The BSB defines legal services as including representation, advice and the drafting or settling any statement of case, witness statement, affidavit or other legal document. It excludes a number of other aspects from this definition such as sitting as a judge, lecturing and providing free advice.³⁷
- 6.6. The BSB's rules allow a barrister to be connected with another business, providing they do not do anything that the BSB restricts them from doing and they notify the BSB of the association. However, for that practising barrister to personally offer legal services (as defined by the BSB) to the public from such a business, the business must also be authorised to provide reserved legal services.³⁸ The BSB's rules do not restrict a practising barrister from having an ownership stake in a business providing unregulated legal services.
- 6.7. The entity rules currently being considered by the LSB do not include rules that prevent a BSB authorised entity supplying non-reserved legal activities from a separate business. However, all entities will be required to inform the BSB if they propose to operate a separate business so this information can be built into their overall risk profile.³⁹

Council for Licensed Conveyancers (CLC)

- 6.8. The CLC was established by the Administration of Justice Act 1985 to regulate licensed conveyancers and in 2008 gained the right to regulate probate activities. The CLC was designated as the first licensing authority for ABS.
- 6.9. The CLC does not place any restrictions on the sort of businesses that licensed conveyancers or licensed conveyancer firms can be connected with, invest in or own. As part of its licensing framework for recognised bodies and for ABS (paragraph 11 and 8.34 respectively) it will endorse licences with all

³⁶ Page 101, BSB Handbook, 1st Edition – January 2014, Part 3, B7: *Scope of practice as an employed barrister (non-authorised body)* https://www.barstandardsboard.org.uk/media/1553795/bsb_handbook_jan_2014.pdf

³⁷ Page 267, BSB Handbook, 1st Edition – January 2014, Part 6: *Definitions* https://www.barstandardsboard.org.uk/media/1553795/bsb_handbook_jan_2014.pdf

³⁸ Page 101, BSB Handbook, 1st Edition – January 2014, *ibid*

³⁹ Page 24, BSB (June 2014), Amendments to the new BSB Handbook: Entity Regulation, for approval by the Legal Services Board,

http://www.legalservicesboard.org.uk/Projects/statutory_decision_making/pdf/2014/20140626_1_BSB_Change_Of_Regulatory_Arrangements_Under_Schedule_4_Entity_Regulation_Application.pdf

the reserved legal activities the applicant can carry out and grant permissions to the same applicant to carry out non-reserved legal activities.⁴⁰

- 6.10. In relation to ABS (at paragraph 8.39 of the framework) if a non-reserved service is permitted then the CLC will either adopt a co-regulatory approach (if an appropriate regulator exists) or it may require the applicant to ring fence the services for which it has authorisations and permissions.⁴¹
- 6.11. The CLC's approach is effectively a permissions based regime. This is because it will grant permissions for non-reserved legal activities to be carried out by licensed conveyancers and be regulated by the CLC. In the event that permissions are not appropriate, the CLC may require the creation of a separate business to carry out such non-reserved activity. The activities of the separate business will not be regulated by the CLC.

Costs Lawyer Standards Board (CLSB)

- 6.12. The CLSB regulates costs lawyers. Costs lawyers are allowed to exercise a right of audience, conduct litigation and administer oaths. A cost lawyers' principal activity is the drawing up of bills of costs. The CLSB does not currently regulate entities (but has consulted on introducing a framework to do so) and is not a licensing authority.
- 6.13. The CLSB does not restrict the right of costs lawyers to be connected with, invest in or own other businesses. The entity regulation framework that has been consulted on by the CLSB does not propose to introduce any restrictions.

Institute of Chartered Accountants in England and Wales (ICAEW)

- 6.14. The ICAEW is the newest regulator of legal services providers. It was designated as an approved regulator and licensing authority for probate activities during 2014. It intends to authorise individuals and firms to provide probate activities. Primarily these will be ICAEW regulated accountants and their firms. Once authorised these will be known as authorised individuals and accredited probate firms.
- 6.15. The ICAEW's regulatory arrangements do not restrict the right of accredited probate firms or authorised individuals to be connected with, invest in or own other businesses.

Intellectual Property Regulation Board (IPReg)

- 6.16. IPReg was established in 2010 by two membership bodies, the Chartered Institute of Patent Attorneys (CIPA) and the Institute of Trade Mark Attorneys (ITMA) to carry out delegated regulatory functions. As a consequence, IPReg

⁴⁰ Page 2, CLC, *CLC Recognised Body Recognition Framework*, https://www.clc-uk.org/pdf_files/regulatory_arrangements/frameworks/6_Recognised_Body_Recognition_Framework.pdf and Page 22, CLC, *Licensing Alternative Business Structures – The Licensed Body (ABS) Licensing Framework*, https://www.clc-uk.org/pdf_files/regulatory_arrangements/frameworks/3_Licensed_Body_ABS_Licensing_Framework.pdf

⁴¹ Page 22, CLC, *Licensing Alternative Business Structures – The Licensed Body (ABS) Licensing Framework*, https://www.clc-uk.org/pdf_files/regulatory_arrangements/frameworks/3_Licensed_Body_ABS_Licensing_Framework.pdf

currently regulates patent attorneys and registered trade mark attorneys. It also regulates entities that provide the services of patent attorneys and trade mark attorneys. IPReg is currently going through the process of being designated as a licensing authority for ABS.

- 6.17. IPReg does not restrict the right of registered trade mark attorneys or patent attorneys to be connected with, invest in or own other businesses. However as part of its conditions of registration it may impose conditions on entities that are seeking registration as an IPReg regulated entity.
- 6.18. A condition may seek to limit the risk to clients, third parties or the public arising from a business agreement or association which the body has or is likely to enter into. This provision allows IPReg to impose additional requirements on applicants that have connections with other businesses that IPReg feels pose a risk to consumers or the public interest.⁴²

ILEX Professional Standard (IPS)

- 6.19. IPS is responsible for regulating Fellows and associate prosecutors of the Chartered Institute of Legal Executives (CILEx). IPS is allowed to authorise Fellows to carry out the reserved legal activities of the exercise right of audience, the conduct of litigation and the administration of oaths. IPS is also “qualifying regulator” and is therefore able to regulate immigration and asylum advice. It also runs a specific regulatory scheme for associate prosecutors at the CPS to allow them to conduct litigation and exercise rights of audience. At the time of writing CILEx is currently going through the process of being designated to regulate persons offering reserved instrument activities (conveyancing) and probate activities. It is also introducing a scheme to regulate entities owned and managed by persons authorised to deliver the reserved or regulated activities. It is not a licensing authority (but it has plans to become one in future).
- 6.20. The IPS does not restrict the right of CILEx fellows to be connected with, invest in or own other businesses. The entity regulation framework currently being introduced does not introduce any restrictions on the entity, or the managers or owners of such entities, from being connected with investing in or owning other businesses.

The Master of the Faculties

- 6.21. The Master of the Faculties regulates notaries who can provide of notarial activities, probate activities, reserved instrument activities (conveyancing) and the administration of oaths. Many notaries are also solicitors and work in SRA regulated firms. When doing so, only the notarial activities carried out by the notary is regulated by the Master of the Faculties. The Master of the Faculties does not regulate entities and is not a licensing authority.

⁴² Page 6, IPReg, Patent Attorney and Trade Mark Attorney Registered Bodies Regulations, <http://ipreg.org.uk/wp-content/files/2012/09/Registered-bodies-regs.pdf>

- 6.22. Generally the Master of the Faculties does not restrict the right of notaries to be connected with, invest in or own other businesses. However, rule 17 of the code of conduct does impose a number of specific requirements if a notary chooses to be connected with other businesses.⁴³
- 6.23. These require that the word notary or other common terms for notary services must not be used in the connected business' name. They also require that the word notary or any other words designated or indicating a notarial or legal practice be used in connection with the notary's involvement with that business. If a client is referred from the notary's practice to the connected business, the notary must inform the client in writing that the connected business is not regulated by the Master of the Faculties and so the client does not benefit from the regulatory protections that affords. Finally, if there are shared premises or shared staff between the connected company and notary's practice, all customers of the connected business must be given the same level of disclosure regarding regulation as if they were a client referred to the business by the notary. These requirements do not apply to notaries working in other bodies authorised to carry out reserved legal activities.
- 6.24. Rule 20 of the code of conduct for notaries also prevents a notary from being an appointed representative of a regulated financial services firm.⁴⁴

The Solicitors Regulation Authority (SRA)

- 6.25. The SRA regulates solicitors, other types of lawyer (for example registered foreign lawyers), firms offering legal services in England and Wales and the managers and employees of those firms. It was established formally by the Law Society of England and Wales in January 2007. The SRA is able to regulate all of the reserved legal activities defined by the Act, except for notarial activities, and is a licensing authority for ABS. It is a "qualifying regulator" and is therefore able to regulate immigration and asylum advice.
- 6.26. Chapter 12 of the SRA's code of conduct concerns whether solicitors can be connected with, invest in or own other businesses. The rule is known as the separate business rule.⁴⁵ The effect of the rule is that firms regulated by the SRA cannot own (or be owned by), actively participate in or be connected with a separate business that offers services that the SRA defines as prohibited separate business activities. The SRA's definition of prohibited separate business activities includes;
- work on any matter that could come before a court (whether or not proceedings are started);
 - instructing counsel;

⁴³Page 8, Master of the Faculties, *Notaries Practice Rules 2014*, <http://www.facultyoffice.org.uk/wp-content/uploads/2014/09/Notaries-Practice-Rules-2014.pdf>

⁴⁴Page 10, Master of the Faculties, *Notaries Practice Rules 2014*, <http://www.facultyoffice.org.uk/wp-content/uploads/2014/09/Notaries-Practice-Rules-2014.pdf>

⁴⁵SRA Handbook, Version 10, 1 July 2014, Chapter 12: Separate businesses
<http://www.sra.org.uk/solicitors/handbook/code/part5/content.page>

- immigration advice (even when regulated by the Office of the Immigration Services Commissioner);
- drafting wills;
- acting as a nominee, trustee or executor;
- providing legal advice as a main service; and
- the definition also refers to other reserved legal activities like advocacy, conveyancing and probate.⁴⁶

6.27. SRA regulated entities are allowed to own (or be owned by), actively participate in or be connected with a separate business that conducts permitted separate business activities. But only if the entity has safeguards in place to ensure that clients are not misled about the extent to which the services provided by the permitted separate business are regulated. The permitted separate business must be reputable and not be presented as being regulated by the SRA. The following services are permitted separate business services:

- alternative dispute resolution;
- financial services (including wholly owned nominee companies providing services solely to a financial services company);
- estate agency;
- management consultancy;
- company secretarial services;
- acting as a parliamentary agent;
- practising as a lawyer in another jurisdiction;
- acting as bailiff;
- acting as a nominee, trustee or executor outside England and Wales;
- providing legal advice as a subsidiary part of the main service of the separate business; and
- any other business provided services that are not a prohibited separate business activity.⁴⁷

6.28. Entities regulated by the SRA are only allowed to be connected with a business that is an appointed representative of a regulated financial services firm if the financial services firm is an independent financial adviser. Generally solicitors are not allowed to provide legal services to external clients unless they are providing them from a body authorised to do so by the SRA or

⁴⁶ The LSB has abridged the definition. The full definition can be found here: http://www.sra.org.uk/solicitors/handbook/glossary#prohibited_separate_business_activities

⁴⁷ The LSB has abridged the definition. The full definition can be found here: http://www.sra.org.uk/solicitors/handbook/glossary#permitted_separate_business

another approved regulator.⁴⁸ Although there are a number of specific exceptions to this requirement (for instance in relation to in-house work, pro-bono and work for associations amongst other things). The SRA is in the process of reviewing the provisions relating to in-house practice.

- 6.29. The effect is that SRA entities are allowed to own (or be owned by), actively participate in or be connected with a separate business if it does not conduct prohibited separate business activities.

Conclusion

- 6.30. Other than the SRA and the Master of the Faculties, none of the approved regulators impose specific restrictions that prevent authorised persons being connected with, investing in or owning other businesses. The BSB, when it is regulating individual practising barristers has rules that impose general restrictions to some degree.⁴⁹ The BSB when regulating entities, the CLC and IPReg operate a notification and conditions style framework and, once notified, they may impose additional restrictions or alter their supervision approach. Only the SRA and the Master of the Faculties have rules requiring specific disclosures to be made relating to the authorised person's involvement in other businesses. Those regulators that operate a notification or conditions regime may impose additional disclosure requirements as a condition of approval.

⁴⁸SRA Handbook, Version 10, 1 July 2014, *Practising Framework Rules*, <http://www.sra.org.uk/solicitors/handbook/practising/part2/content.page>

⁴⁹ See paragraph 6.4.

7. Assessment

- 7.1. The preceding sections of this paper have shown that regulators are not required by statute to restrict authorised persons from being connected with, investing in or owning other businesses. However, regulators can impose such restrictions to fulfil their duties to act in a manner compatible with the regulatory objectives. Such interventions must be consistent with the better regulation principles.
- 7.2. We have assessed the imposition of such restrictions against the regulatory objectives and the better regulation principles. We have concluded that regulators need to balance the competing (and sometimes contradictory) implications of the regulatory objectives when considering what, if any, restrictions need to be imposed. We do not consider that general, blanket restrictions will be consistent with the better regulation principles.
- 7.3. Our review of the regulatory arrangements of the approved regulators has found that only the CLSB, ICAEW and IPS do not impose any restrictions to prevent authorised persons from being connected with, investing in or owning other businesses. The paper will now consider the specific arrangements in place by the regulators and whether they are likely to be compatible with the regulatory objectives and consistent with the better regulation principles.

Specific restrictions

- 7.4. The Master of the Faculties has a very specific restriction in its rules. It restricts notaries from being appointed representatives for regulated financial services firms but allows connections with any other businesses. We understand that this is because appointed representatives can be financial advisers who are only able to offer a restricted range of products from a single or small number of financial services providers. The independence (and perception of independence) of a notary is very important. The Master of the Faculties considers that this type of association compromises that independence. However, these rules no longer reflect the operation of the financial adviser market. Following the FSA's Retail Distribution Review (RDR) there are now two categories of financial adviser: restricted advisers and independent advisers. The FCA regulates the use of such terms. Advisers that are restricted or independent can be appointed representatives and a great many independent advisers are now in fact appointed representatives.⁵⁰
- 7.5. We consider that the Master of the Faculties rules as currently drafted may now be more restrictive than necessary. This is because appointed representatives can now offer independent financial advice but the rule, aimed at ensuring notaries only provide independent financial advice, prevents notaries from providing independent financial advice from such an

⁵⁰ Page 10, FSA (June 2012), Finalised guidance 12/15: Retail distribution review: Independent and restricted advice, <http://www.fca.org.uk/your-fca/documents/finalised-guidance/fsa-fg1215>

entity. The Master of the Faculties' restrictions have a clear rationale, however it has not incorporated the changes in the financial services market and so may wish to consider whether they remain proportionate for the outcome it is seeking to achieve.

- 7.6. The SRA's separate business rule is the most restrictive of all the regulators. The SRA argues that the separate business rule is needed:
- to ensure that members of the public are not confused or misled into believing that a business connected to an SRA regulated entity or individual is regulated by the SRA or another approved regulator when it is not;
 - to ensure that the protections afforded to the clients of practising lawyers are in place in relation to certain mainstream legal services; and,
 - to prevent a solicitor severing part of a case or matter in such a way that the client loses statutory protections.⁵¹
- 7.7. Our analysis against the regulatory objectives recognises that there is an issue regarding consumer confusion and that regulatory intervention may be necessary to reduce it. The SRA imposes disclosure and structural separation requirements on SRA regulated entities that have connections with permitted separate businesses. We have made no assessment of the effectiveness of such disclosures. However, it may be that such an intervention is a more proportionate requirement, in terms of protecting and promoting the consumer interest, than restrictions on connections with some but not all business activities. Therefore it is possible that the first reason for imposing the rule could be achieved in a more proportionate way than is currently the case.
- 7.8. The second objective is more contested and this is due to the definitions used in relation to permitted and prohibited separate business activities and what is a 'mainstream legal service'. The SRA handbook does not define what it means by mainstream legal services. However since the objective of the rule is to maintain regulatory protection for such services we can assume that mainstream legal services includes the services that appear in the list of prohibited separate business activities.
- 7.9. The rationale for the different activities being included in the list of prohibited separate business activities is unclear. For instance the SRA interprets the rule as including services that involve being notified of, and assessing, a claim against an insurance policy (so called first notification of loss)⁵² and also the provision of tax advice by accountants.⁵³ It is not clear whether authorised persons or potential applicants would interpret such services as mainstream legal services.

⁵¹ SRA handbook, version in force 31/03/2009 to 5/10/2011, *Rule 21: Separate businesses*, <http://www.sra.org.uk/solicitors/change-tracker/code-of-conduct/rule21.page#TOA-Rule-21-02>

⁵² We understand this is the case due to the second condition that the ABS AA Law Ltd must comply with to be granted a waiver to the separate business rule. See: <http://www.sra.org.uk/solicitors/firm-based-authorisation/abs-register/606959.page>

⁵³ We understand this is the case due to the conditions that the ABS Pricewaterhousecoopers Legal LLP must comply with to be granted a waiver to the separate business rule. See: <http://www.sra.org.uk/solicitors/firm-based-authorisation/abs-register/442833.page>

- 7.10. The SRA is able to issue waivers in relation to the separate business rule. Information provided to the LSB in January 2013 stated that it issued two waivers of the separate business to recognised bodies in 2011 and another two in 2012. The SRA does not publish details of how many recognised bodies have been granted waivers to the separate business rule so we do not know how many there are. The SRA also does not publish the names of recognised bodies that have been granted a waiver to the separate business rule.
- 7.11. In relation to ABS, the SRA is required to keep a register of licences issued by it. On this register the SRA records whether it has granted a waiver and what SRA rules the ABS licence holder has a waiver from. LSB analysis in August 2014 showed that of the 326 licences the SRA has issued it has granted 63 waivers. Of these 63 waivers, 57 included a waiver from the separate business rule. Therefore around 17% of ABS licence holders are allowed to be connected to businesses offering prohibited separate business activities. When it grants these waivers the SRA can place conditions on the applicants. Very often the conditions imposed in relation to waivers of the separate business rule include additional disclosure requirements.
- 7.12. The existence of so many waivers, particularly for new entrants, exposes the arbitrary nature of having a list of activities that legal services providers can be connected with and a list with which they cannot. The SRA appears to accept that certain legal services providers are capable of operating with prohibited separate businesses, subject to conditions regarding disclosure and separation, but others are not. It has not however, published a policy about how it determines whether a waiver is appropriate and the conditions imposed appear to vary with no clear rationale.
- 7.13. The list of what is permitted and what is not is confusing. For instance a solicitor's firm can be connected with a business that deals with company formation as company secretarial services are permitted. But, seemingly, not with one that compiles and files a company's accounts, as this may constitute tax advice and so be considered by the SRA as the conduct of any matter that may come before court. Both services may appear to have similar characteristics to a consumer. Therefore, it is unclear why one should be considered to be a mainstream legal service (and so prohibited) but the other will not. This confusion, together with the extent of waivers issued to the rule, makes it doubtful that the separate business rule achieves the second objective of ensuring that protections afforded to the clients of practising lawyers are in place in relation to certain mainstream legal services.
- 7.14. The third objective of the rule appears to duplicate the SRA's handbook principle to act in the best interest of the client⁵⁴ and the outcomes in relation to client care.⁵⁵ The SRA appears to be suggesting that it wants to restrict the ability to take a matter, separate it into its constituent parts and provide some

⁵⁴ SRA Handbook, Version 10, 1 July 2014, *Part 1: SRA principles*, <http://www.sra.org.uk/solicitors/handbook/handbookprinciples/content.page>

⁵⁵ SRA Handbook, Version 10, 1 July 2014, *Chapter 1: Client care*, <http://www.sra.org.uk/solicitors/handbook/code/part2/content.page>

of the constituent parts through the SRA regulated entity and some through a connected (and not necessarily regulated) entity. However, if such unbundling were not in the best interests of a client then the authorised person should not be doing it. The outcomes for client care include a requirement to treat clients fairly and to disclose *whether and how the services provided are regulated and how this affects the protection available to the client*.⁵⁶

- 7.15. Finally the very existence of permitted separate business activities undermines the aims of the third objective. For example, an SRA regulated entity may consider that an aspect of the matter they were handling, for instance litigation, would be better resolved through an alternative dispute resolution (ADR) service. The list of permitted separate business activities allows the SRA regulated entity to be connected to a provider of ADR services. This provider of ADR services need not be regulated by a legal services regulator. The SRA regulated entity carrying out litigation for a client could refer the client to its connected ADR provider (provided that it disclosed the implications to the client on the scope of regulation). The same matter may return to the SRA regulated entity for further litigation if it is not resolved through ADR. This may all be in the best interest of the client concerned. Therefore in certain circumstances the rule itself allows matters to be separated and provided by the most suitable provider.
- 7.16. A report produced for the LSB questioned the proportionality of the SRA's separate business rule and recommended it as an area for further investigation. The report observed that the separate business rule distorts competition. The report also questioned the transparency and effectiveness of the rule.⁵⁷
- 7.17. The SRA's restrictions are the most complicated of all the approved regulators. We also identified doubts whether they will achieve the SRA's objectives. We consider that the way the rule is constructed means that the disclosure and separation requirements for permitted separate business activities is likely to meet the SRA's first objective of reducing consumer confusion and such a requirement is consistent with the regulatory objective of protecting the interests of consumers.
- 7.18. The confusing and seemingly arbitrary nature of what is permitted and prohibited, combined with a large number of waivers, suggests that the SRA's second objective is unlikely to be achieved by the rule as currently operated. It is likely to have negative impact on the objectives of promoting competition and access to justice.
- 7.19. Finally, the SRA's third objective is arguably a duplication of existing regulatory requirements and on its own terms cannot be said to be achieved in all circumstances because of the existence of permitted separate business activities. This is likely to not be consistent with the better regulation

⁵⁶ O(1.7), SRA Handbook, Version 10, 1 July 2014, *Part 1: SRA principles*, <http://www.sra.org.uk/solicitors/handbook/handbookprinciples/content.page>

⁵⁷ Page 18, Malcolm (June 2013), *The proportionality of legal services regulation*, <https://research.legalservicesboard.org.uk/wp-content/media/2013-06-14-LSB-final-report-STC.pdf>

principles. The SRA's rule is therefore the one that is the most in need of thorough review. We understand that the SRA has committed to such a review and we welcome this initiative.

General restrictions

- 7.20. The BSB prevents practising barristers from providing legal services through non-authorised practitioners. The BSB has drawn up its own definition of legal services and it goes beyond the reserved legal activities and is different to the definition of legal activities in the Act.⁵⁸ It seems likely that these restrictions are in place to reduce the likelihood of consumer confusion regarding the extent to which the services are regulated by the BSB and consumer access to the Legal Ombudsman.
- 7.21. The BSB does allow unregistered barristers to provide legal services (excluding reserved legal activities) to consumers providing they disclose that they are not acting as a barrister and that only a limited extent of BSB regulation applies to those services (including the lack of access to the Legal Ombudsman).⁵⁹
- 7.22. This brings a lack of consistency in the regulation of barristers (whether practising or unregistered). This arises because of the unique feature of the title barrister which is awarded and controlled by the Council of the Inns of Court and not the BSB. This lack of consistency may be justified because unregistered barristers cannot provide reserved legal activities. However, it is not clear whether this is the reason that the different treatment exists.
- 7.23. The BSB's restrictions and exemptions arise from the historical title of barrister and who awards it. The BSB does not restrict the businesses they can own but does restrict the extent to which individual barristers can provide legal services from an unregulated entity. The BSB's rule restricting practising barristers from providing legal services to the public through unregulated businesses may be an appropriate restriction to prevent public confusion and therefore protect the consumer interest. However, it does go beyond the requirements of statute and there may be a more proportionate approach.

Requirements to notify

- 7.24. Three of the regulators (the BSB, CLC and IPReg) operate, or intend to operate, a notification process on authorised persons being connected with, investing in or owning other businesses. The BSB intends to use this notification process to inform its risk assessment process for entity regulation and so determine supervisory policy towards a BSB regulated entity. It operates a similar approach to individual barrister associations. The other two regulators use the notification to help them determine whether the connection is acceptable and/or whether conditions should be applied to the authorised person.

⁵⁸ Section 12, Legal Services Act 2007

⁵⁹ Page 82, BSB Handbook 1st edition, January 2014, *Section D4: Unregistered barristers*, https://www.barstandardsboard.org.uk/media/1553795/bsb_handbook_jan_2014.pdf

- 7.25. We consider the BSB's proposed approach to entities to be appropriate. We accept that there is a risk that consumers may get confused about regulatory scope when using services from businesses that are connected or owned by authorised persons. By assessing the risk of connections between BSB regulated entities and other businesses, the BSB, where it determines a regulated entity's connections represent a higher risk, will be able to adopt a more active supervisory approach. Such a supervisory approach will be able to review the BSB regulated entity's public facing documentation and determine whether it is clear about the regulatory scope. If it is not the BSB will be able to require changes to reduce the risk of consumer confusion.
- 7.26. CLC and IPReg's use of permissions and conditions provides them with the freedom to take a case by case approach according to the likely risk and impact. For instance if a sole trader applies to the CLC for a probate licence and intends to provide a will writing service, the CLC may consider that it is appropriate to regulate, through a permission, both activities. It may do this because it considers that consumers will not realise what is regulated and what is not when there only one individual providing the services. In similar circumstances but with a much larger applicant or a more distant connection between the services, it may allow the applicant to carry on the unreserved work in a ring fenced and separately branded organisation.
- 7.27. Such an approach is not without its downsides. There is a risk that conditions and permissions may lead to inconsistencies and lack transparency. However, disclosure of conditions and permissions by regulators and requirements for clear disclosure to consumers by regulated firms reduces the risk of problems arising.

Final assessment

- 7.28. This section has shown that those regulators that impose restrictions on authorised persons being connected with, investing in or owning other businesses should review those requirements. The rationale for the imposition of these restrictions does not appear to be consistent with the better regulation principles. We do accept that such restrictions will reduce the likelihood of consumers being confused about the scope of regulation.
- 7.29. All of the regulators allow some connections between those they regulate and certain other businesses. When connections are allowed, regulators tend to impose disclosure and separation requirements. This appears to suggest that regulators accept that appropriate separation and disclosure of regulatory scope can reduce the risk of consumer confusion about whether a service connected to an authorised person is regulated or not. Yet they still impose restrictions in addition to these requirements. Considering this, the imposition of such restrictions appears disproportionate and the imposition of restrictions is likely to have a negative impact on competition and access to justice.
- 7.30. We consider that those regulators that assess connections between authorised persons and other businesses according to risk and either impose conditions or alter their supervisory approach are more likely to be acting in a way that is consistent with the better regulation principles. Although there is a risk of a lack of transparency and consistency. However, this can be mitigated by having published policies on the granting of conditions and/or permissions;

the publication of conditions and/or permission imposed; and, where necessary imposing requirements for disclosure on legal services providers.

8. Conclusion and next steps

- 8.1. Regulators are not required by statute to restrict authorised persons from being connected with, investing in or owning other businesses. But regulators can impose such restrictions to fulfil their duties to act in a manner compatible with the regulatory objectives providing such interventions are consistent with the better regulation principles.
- 8.2. We have assessed the imposition of such restrictions against the regulatory objectives and the better regulation principles. We have concluded that such restrictions may sometimes be compatible with some or all of the regulatory objectives. But blanket restrictions (by which we mean wholesale restrictions on the sorts of businesses an authorised person can be connected with) do not appear to be justified by evidence and are unlikely to be consistent with the better regulation principles.
- 8.3. Looking at the regulators in turn:
 - CLSB, ICAEW and IPS do not impose any restrictions to prevent authorised persons from being connected with, investing in or owning other businesses.
 - The BSB, CLC and IPReg operate, or intend to operate, a notification process on authorised persons being connected with, investing in or owning other businesses. Following notification, these regulators may impose conditions, grant certain permissions or supervise the regulated entity differently.
 - The Master of the Faculties and the SRA impose specific restrictions to prevent authorised persons from being connected with, investing in or owning other businesses. The Master of the Faculties restricts notaries from being appointed representatives for regulated financial services companies but allows any other connection providing there is consumer disclosure and other requirements to reduce confusion. The SRA restricts authorised persons from being connected with certain business activities but allows them to provide others so long as there is disclosure and appropriate separation.
- 8.4. It is likely that these specific restrictions will have a negative impact on the requirement to promote competition and access to justice. However, they may have a positive impact on the protection of consumer interests, although there is little evidence to reach a conclusion either way. The way the rules are imposed is unlikely to be in line with the better regulation principles because the rules are not proportionate, consistent or targeted. These rules are in need of review.
- 8.5. We conclude that those regulators that operate a notification and conditions process are more likely to be operating in line with the better regulation principles providing that the conditions imposed are transparent and are consistent and proportionate to the risk posed.
- 8.6. More generally we consider that disclosure requirements, when referring individuals to unregulated connected companies, are more likely to be the

most appropriate regulatory intervention to protect consumer interests and reduce the risk of consumer confusion.

- 8.7. We expect regulators to review their current restrictions and processes against the regulatory objectives and consider what changes can be made. We understand that the SRA is intending to review the separate business rule and we support this initiative.⁶⁰
- 8.8. We also encourage other regulators, working collaboratively where appropriate, to review the issues raised by this paper. In particular, the need to consider the most appropriate regulatory approaches to deliver the outcome that consumers understand what is regulated and what is not. Research shows that consumers lack understanding in this area. This is relevant for all regulated legal services providers; however, it is amplified when services are provided by a firm connected to a regulated legal service provider.

⁶⁰ Paul Philip (4 September 2014), speech to Westminster Legal Policy Forum keynote seminar: The future of legal services regulation, <http://www.sra.org.uk/sra/news/events/conference-2014-09-04-westminster-legal-policy-forum.page>

9. Glossary of terms

ABS	Alternative Business Structures. From October 2011, non-legal firms have been able to offer legal services to their customers in a way that is integrated with their existing services. Equally, law firms are now able to develop their portfolios to compete across wider areas compared to previous regulatory restrictions
Approved regulator	A body which is designated as an approved regulator by Parts 1 or 2 of schedule 4, and whose regulatory arrangements are approved for the purposes of the LSA and which may authorise persons to carry on any activity which is a reserved legal activity in respect of which it is a relevant approved regulator
Authorised Person	A person authorised to carry out a reserved legal activity
BSB	Bar Standards Board – the independent Regulatory Arm of the Bar Council
Consumer Panel	The panel of persons established and maintained by the Board in accordance with Section 8 of the LSA to provide independent advice to the LSB about the interests of users of legal services
ILEX Professional Standards Board	Institute of Legal Executives Professional Standards – the independent regulatory arm of the Chartered Institute of Legal Executives
Chartered Institute of Legal Executives	Representative body for Legal Executives
Licensing Authority	An approved regulator which is designated as a licensing authority to license firms as ABS
LSB or the Board	Legal Services Board – the independent body responsible for overseeing the regulation of lawyers in England and Wales
LSA or the Act	Legal Services Act 2007
Regulatory Objectives	<p>There are eight regulatory objectives set out in the Legal Services Act 2007:</p> <ul style="list-style-type: none"> • protecting and promoting the public interest • supporting the constitutional principle of the rule of law • improving access to justice • protecting and promoting the interests of

	<p>consumers</p> <ul style="list-style-type: none"> • promoting competition in the provision of services in the legal sector • encouraging an independent, strong, diverse and effective legal profession • increasing public understanding of a citizen's legal rights and duties • promoting and maintaining adherence to the professional principles of independence and integrity; proper standards of work; observing the best interests of the client and the duty to the court; and maintaining client confidentiality.
<p>SRA</p>	<p>Solicitors Regulation Authority - Independent regulatory body of the Law Society</p>

