



BAR
STANDARDS
BOARD

REGULATING BARRISTERS

**Bar Standards Board response to
LSB Consultation – ‘Alternative Business Structures: approaches to licensing’**

Introduction

1. The Bar Standards Board (BSB) welcomes the opportunity to comment on the consultation paper on the proposed approaches to licensing Alternative Business Structures (ABSs).
2. The BSB’s approach, as evidenced by the process it adopted in considering how to amend its Code of Conduct to facilitate the intentions of the Act, is to embrace the concept of change but to proceed with it cautiously and where possible on the basis of evidence, as a responsible regulator acting in the public interest. Impacts of the incremental effects of these major changes, be they regulatory or in relation to equality and diversity, have to be considered if potential risks to the market and consumers are not to come to fruition. The LSB accepts this approach as can be seen, for example, in its proposed research and evidence collection in relation to consumers’ understanding of the provision of non-reserved legal activities by non-authorized persons vis-a-vis reserved legal activities by authorised persons¹. The approach of proceeding forward based on evidence/effect could usefully be applied more generally to the significant changes under the Act. It is particularly important in the area of diversity, which the LSB acknowledges².
3. It is also fair to point out here that, as the LSB will be aware, the BSB is still considering whether or not to permit barristers to practise in the full ABS regime when

¹ Consultation paper, para 18

² Para 31

it is implemented³. This will be the subject of further consultation by the BSB during the course of 2010. The outcomes of that consultation will inform the BSB's decision as to whether or not to apply to become a Licensing Authority (LA). The contents of this response are therefore limited by this current position in the BSB's consideration of ABSs.

4. The BSB notes the expectation that the LSB will expect LAs to take an "outcomes based approach" to regulating ABSs⁴. The BSB's own review of its Code of Conduct largely follows this line; it creates a set of regulatory principles that those regulated can follow and against the performance of which those regulated may be assessed. However, the BSB believes that this approach can only be at its most effective when regulatory principles and the assessment of outcomes are supported by clear and robust framework of rules to which those regulated are obliged to adhere.
5. The BSB favours the flexible approach encouraged by the LSB as long as regulatory framework has sufficient clarity that those subject to it have no excuse for not appreciating the boundaries of what is and is not acceptable behaviour.
6. It is entirely logical that a 'risk-based' approach⁵ to regulation should inform LAs regulation of ABSs. It is an approach that the BSB is increasingly taking in relation to the regulation of chambers through its developing Chambers Monitoring Scheme, which itself will be extended to entities should the Board decide to become an entity regulator⁶.
7. The BSB acknowledges the impetus toward 'regulatory focus on the entity'⁷ but suggests that the effectiveness of regulation of the conduct of individual lawyers should not be underestimated against this backdrop. References are made through the consultation paper to the exploration by the LSB of financial services models of regulation; it should be borne in mind that the FSA has itself in recent times reiterated the importance of the effectiveness of regulation of the individual as opposed to that of the entity. Others have observed that the recent financial crisis has exposed the shortcomings of the financial services regulation model and, although those shortcomings

³ Although, participation in the limited transitional ABS regime that are LDPs was of course permitted as of the 19/11/09 Board meeting

⁴ Consultation paper ,para 5

⁵ Para 6

⁶ Consulting during 2010

⁷ Consultation paper, Para 7

were derived from regulators failing to understand the risks involved in the business done, care must be taken not to appear to take too much from that model if the new framework for legal services is to retain credibility.

8. Similarly, the BSB notes the LSB's role as an oversight regulator⁸ and the possibility of competition between the Approved Regulators (ARs) beneath the framework set by the LSB. Whilst it is possible for such a situation to be healthy, the BSB highlights the risk of 'dumbing down', acknowledged by the LSB as a very high one which will require great care to prevent.
9. In relation to 'ownership tests'⁹ for non-lawyer managers and owners, the BSB suggests that 'a test for non-lawyer managers' is just one dimension of the issue; actual pressures on HoLPs and HoFAs in post will have to be scoped out and specifically addressed within the overarching regulatory framework if proper protection is to be given to consumers through 'outcomes based' regulation. In particular HOLPs should be required to be managers. Unless the HOLP is a partner or director, they are unlikely to carry sufficient weight in the deliberations of the ABS to enable them to protect consumers.
10. Such considerations also extend to the issue of ownership; 'strong ownership tests' would have to be absolutely right if there really is to be 'no (permitted) restriction on how much of the business non-lawyers will be allowed to own'¹⁰. However, the tests proposed¹¹ do not seem to be particularly strong tests at all. The BSB has corresponded separately with the LSB in relation to this point and the BSB's ability, in light of it, to set itself out as a niche regulator of specific types of ABSs based on specified lawyer/non-lawyer ownership structures and this point is also referred to below¹².
11. In relation to any potentially publicly listed corporate ABS¹³, issues of conflict of obligations to clients versus shareholders have the capacity to complicate matters further. The solution referred to by the LSB is similar to how Slater & Gordon in Australia (as the first publicly floated law firm) tried to clarify and deal with those

⁸ Consultation paper, Para 11

⁹ Para 14

¹⁰ As above

¹¹ Pages 21 - 32

¹² At paras 20-22

¹³ Consultation paper, Para 15

conflicting duties¹⁴. However, such arrangements have never been tested (in the courts) and what is envisaged through the Act, and by the LSB, is on a scale not seen in legal services markets anywhere in the world.

12. Access to Justice is a difficult area in terms of definition: the consultation paper¹⁵ suggests that it can be achieved through ABSs by their 'creating new diversity in the range and value of legal service offerings and providers'. However, this risks confusing access to justice with access to legal services. The difference is in part defined by the degree to which quality of service is a factor. Good access to poor quality legal services is not access to justice.
13. Nor is it clear how the desired for effect of greater 'access to justice' through ABSs will be ensured; the consultation paper refers to the need for LAs to 'track the impact of the ABS regime'¹⁶ but it is far from clear how that tracking will be done in practice. The BSB is of the view that any related research or tracking is better done by the LSB in its position as oversight regulator than by individual LAs in a disparate fashion. In broad terms, therefore, the BSB welcomes the references within the paper¹⁷ which suggest there may be scope for slowing the implementation process to permit proper reflection of actual impact (as, in common with all the ARs, the BSB is, for example, statutorily obliged to do in relation to equality and diversity impact) by allowing a period of special grace to permit entities to make the transition from one arrangement to another.
14. In relation to the issue of LAs educating consumers about what are non-reserved legal activities provided by non-authorised persons as opposed to reserved legal activities by authorised persons, the BSB has some concern that, however well informed those individuals might be, it remains slightly anomalous that consumers will be relatively unprotected in relation to a whole raft of quasi legal services which will be entirely unregulated, compared to the panoply of obligations, rules and remedial powers applicable to regulated legal services. Although this situation in relation to unreserved legal services is not new, with the introduction of the new regulatory framework it is reasonable to suggest that this should now be addressed because consumers will assume that such services are regulated.

¹⁴ Para 86

¹⁵ Para 21

¹⁶ Para 22

¹⁷ Such as at para 33

Proposed Outcomes

Q1: What is your view of basing the regulation of ABS on outcomes?

- a. **Should all LAs have the same core outcomes?**
- b. **Are the proposed outcomes appropriate?**
- c. **Is the division between entity and individual regulation appropriate?**

15. As stated at paragraph 4 above, the BSB's own Code of Conduct will be changing to one where core principles are set out, supported by clear rules, guidance and advice on the correct and acceptable forms of practice. However, it is keen that the notion of 'outcomes' is precise enough to form a proper basis for the regulation of firms. There therefore will need to be real clarity between what are the general 'core outcomes' applicable to all LAs and how they will be achieved which may be specifically applicable to (and formulated by) the LAs themselves. A good example of the latter in relation to the Bar is the Cab-Rank Rule; although often disparaged by other professions, nevertheless for many practitioners this has a real impact of the way in which they practise and provides real benefits for consumers and access to justice. If one of the key proposed outcomes relates to upholding justice and the rule of law, the cab-rank rule warrants specific reference as a means to oblige practitioners to provide it. In this context, it may not be appropriate for all LAs to have the same approach to achieving the core outcomes.
16. The LSB appears to be using outcomes in two different ways in the consultation paper. Some of the proposed outcomes are matters which will need to be reflected in the ARs' regulatory regimes e.g. requirements as to behaviour of lawyers and employees, and others are outcomes which can be achieved only over a longer period of experience in operating the new regime e.g. consumer confidence. Whilst the outcomes seem sensible at a high level, there is still the question of how they are actually achieved. The paper contains no 'route map' for non-lawyers to follow; this is an example where the LSB should take a more prescriptive approach where there is good reason to be prescriptive.
17. The principles/outcomes set out in paragraphs 37 to 43 of the consultation are all unquestionably valuable but there is little offered to show how they might be secured in practice. As such, whilst there is clearly a need not to overburden ABSs with

prescriptive rules and regulations so they can focus on ‘delivering quality legal services that are tailored to consumers’ needs’¹⁸, there is a counter-balancing requirement to make explicitly clear the regulatory parameters within which the ABS is working; in the experience of the BSB, consumers themselves also derive comfort and reassurance if the rules applicable to conduct of the entity (or individual) with whom they are dealing are clear so that the expectation they have in relation to services they receive can be similarly clear.

18. Simplifying existing regulation on the introduction of ABS, should not mean that regulation should be any less rigorous. It is acknowledged that¹⁹ there will be instances where outcomes or principles based regulation will be inadequate on its own; even if supplemented by guidance, the BSB remains concerned that outcomes based principles will be just too vague to deal with certain scenarios unless supported by at least some binding rules. Without such rules there is a risk that ‘simplification’ is merely a ‘dumbing down’ of differing levels of regulation found to be appropriate for different regulators.
19. In relation to the balance/division between entity and individual regulation, the phrase ‘regulatory maze’²⁰ is apposite; for the consumer to have confidence, the boundary between what is applicable to the lawyer with whom s/he is dealing as an individual and what is applicable to the entity that lawyer is part of in relation to service provided, must be absolutely clear or a key aim of the whole reform of legal services regulation will have failed.

Ownership

Q2: Do you think our approach set out in this Chapter to the tests for external ownership is appropriate?

20. The discussion in paragraphs 69 to 114, does not appear to go into sufficient detail of the risks attendant on non-lawyer ownership and how these might be effectively mitigated.

¹⁸ Para 52

¹⁹ Para 54

²⁰ Para 66

21. The principle that ‘there should be no limit on external ownership’²¹, as referred to above, could adversely affect consumer choice if individual Licensing Authorities are not allowed to choose to regulate only a sub set of ABSs with particular types of ownership. The LSB will know that the BSB is contemplating setting its stall out as a specialist niche regulator of advocacy/barrister-focussed entities. One of the ways of defining characteristics would be to specify levels of barrister ownership (as a percentage); the principle in the consultation paper would not permit this. Whilst the concept of not permitting any such limitation seems right, in fact it reduces consumer choice; the choice to select the services of advocacy/barrister-focussed entities regulated by the BSB would not be not permitted. In correspondence, the LSB has suggested that this could still be achieved if the key defining characteristic was instead by function ie the BSB would instead regulate entities which primarily provided ‘advocacy services’. In the near future the BSB will issue a survey to determine barrister interest in new business structures. The results of the survey might indicate that there is a strong demand for an entity that is predominantly barrister owned or managed.
22. However, it has been often generally argued that ‘the power follows the money’ and that in fact it is the composition of the ownership structure which sets the culture and modus operandi of an organisation albeit within the parameters of the regulatory framework applicable to those delivering the services. Even if prospective owners pass a ‘fitness to own’ test, that an ABS’s constitutional documents specifically states that duties to shareholders will not compromise duties to the courts and to clients, great care must be taken to prevent economic incentives for profit-maximisation to override, interfere or compromise these professional duties of the lawyers actually providing these legal services. The problems caused by such profit-making imperatives in other scenarios such as claims management companies and referral fees are well documented and have occurred even with clear and strong regulations in place.
23. The exchange of correspondence with the LSB does not dissuade the BSB from its desired rationale for entity regulation ie defined by ownership and not just by function. We will certainly want to restrict by function as well as by ownership. The response from the LSB is slightly contradictory; on the one hand it states:

‘I would urge you not to assume (without objectively justifiable evidence) that any entity

²¹ Para 72

without a “barrister majority” of owners and/or managers is inherently more risky....I would therefore encourage the BSB to consider positioning its approach to regulating entities in the context of “advocacy/specialist legal advice” rather than the more limited approach of focussing on how individuals qualified as lawyers’

However, on the other hand it states:

‘we do recognise that not all Licensing Authorities will be competent to regulate all types of ABS, in particular those ABS with complex ownership structures’

In fact, it is precisely this latter point that drives the ABS approach of defining entities it is likely to regulate by ownership and not just by function. This is not necessarily on the basis of risk, as in the first reference above, but rather an issue of competence as highlighted and acknowledged in the second reference above.

24. The ownership tests set out by the paper seem sound but, as referred to above, the pressures of commercial life may affect behaviour once these individuals are in post and it is not clear how these will be dealt with. Whilst it is expected that licences will specify a requirement to notify changes to character and suitability of people subject to these tests²², the suggestion that the veracity of this information might not need to be checked annually, even if the LA adjudges that the risk with a particular ABS justifies it, is a cause of concern and, again, could erode consumer confidence, particularly when the LSB acknowledges that the LAs should not place an ‘over-reliance’ on the results of the initial tests²³.
25. The BSB notes that the HoLP is expected to report at a senior level but there is no requirement that he or she should be a manager. This creates the risk that they would have little or no influence on decisions made by the managers.

Reserved and Un-reserved legal activities

Q4: Do you agree with our position on reserved and non-reserved legal activities?

26. The BSB welcomes the acknowledgement in the paper that this is an important issue which needs to be addressed but reiterates here its concern, recognised in the

²² Para 91

²³ Para 106

consultation paper²⁴, that there is risk in allowing ABSs to provide unreserved legal services through a separate unregulated business. This raises the general question of whether it is indeed the time for the LSB to reconsider redrawing the boundaries between what are reserved and unreserved legal services. On this basis, the Law Society argument²⁵ that ABSs should be prohibited from setting up separate unregulated firms to carry out unreserved legal services has some merit. As consistent with the BSB approach to these reforms, the intention to conduct research²⁶ to gather evidence about consumer understanding of the differences between reserved and unreserved legal activities is therefore welcomed.

27. The paper is unclear also on how the LSB actually envisages ABSs protecting consumers in relation to both reserved and unreserved legal activities. A consistent approach will be required: Solicitors have a separate business rule in their code of conduct preventing them providing unreserved legal activities through separate companies but there are concerns that this will be lost when ABSs are introduced; the CLC required such unreserved legal activities to be provided through separate firms.

LA Enforcement powers and financial penalties

Q5: Are the enforcement powers for LAs suitable?

a. What is your view on the proposed maximum level of financial penalty that a LA can impose on an ABS?

28. The BSB does not consider it appropriate that the level of penalty that an LA can impose on an individual or entity should be unlimited. This is considered to be disproportionate for many likely types of smaller scale ABSs.

Access to Justice

Q6: What do you think of our approach to access to justice?

29. Regrettably, the benefits of research referred to above are not followed through in relation to 'access to justice'²⁷. Sir David Clementi's report dealt with the theoretical,

²⁴ Para 159

²⁵ Para 161

²⁶ Para 171

²⁷ Para 215

albeit based on some research of its own; the world of practical reality may be somewhat different some 6 years on from that work. The BSB acknowledges that the ABS regime could deliver undoubted benefits for consumers but, equally, there could be risks and, as a responsible regulator, the BSB has a duty to try to identify and mitigate that risk.

30. It is logical not to place too a great a burden on ABSs, particularly as they are getting established, but when there is little evidence or research, it is difficult to assess their potential impact. There is a danger therefore that consumers might unnecessarily be exposed to adverse risks at the outset of this regime and action will only be taken when it is too late ie when 'there is strong evidence of consumer detriment'²⁸.

The general tenor of this chapter of the consultation paper seems, as referred to above²⁹, to confuse two things: access to justice and access to legal services. 'Access to justice' consists of a variety of often intangible qualities and is difficult to define. There are larger issues of having a sound legal system and preserving the rule of law. Access to justice is part of the BSB vision and should incorporate consumer access to good, honest, independent advocacy and expert legal advice.

31. Whilst access to legal services is undoubtedly part of access to justice, there are also other elements. It is not right, for example, to dismiss the importance of pro bono work³⁰ in access to justice. The need for such services is greater than ever in current times and has been part of the Bar's defining ethics for some time. It would be a mistake if the culture of new forms of legal business were not inculcated with the same commitment to providing such services.
32. In terms of 'measuring the impact' of ABSs³¹, the BSB would draw attention to the importance of the requirement on the LSB and ARs to conduct Equality Impact Assessments. Although there could be positive impact, there could also be risks which must be mitigated. The BSB has looked at the Regulatory Impact Assessment that accompanied the Legal Services Bill and is of the view, supported by legal opinion, that it was inadequate. This places all the more emphasis on properly measuring the impact of these changes as they are rolled out in reality and the BSB is concerned that not much is in fact said in this consultation paper, see paragraph 29 below.

²⁸ Para 218

²⁹ Point 12

³⁰ Para 219

³¹ Para 222

33. Measuring impact is particularly important in relation to the potential effect on the costs of services for consumers. For example, it might be possible under present arrangements to procure the services of a junior barrister in a road traffic accident case for c.£50 per hour. Getting the equivalent service from a firm, with its associated overheads would cost in the region of £125 per hour. If there is a momentum behind practitioners moving to firms or ABSs in the future, it is therefore, for example, by no means certain that cheaper services for consumers will result.
34. In general therefore, the BSB does not feel that the approach to 'access to justice' is adequate. It is poorly defined as a concept and therefore the definition offered in the paper is insufficient. Until that is addressed, there can be no meaningful engagement with the sub-set of questions beneath Question 6.

Appellate Bodies

Q7: What is your view of our preference for a single appeals body?

35. The BSB suggests that consideration should be given to permitting each LA setting up its own appellate authority. A single Appellate Body for all decisions could prove very expensive and would not have the flexibility to manage the flow of cases, perhaps by fast tracking where appropriate for example, that smaller individual authorities might.
36. There is some linkage in this chapter to the proposals which form part of the Civil Law Reform Bill. The BSB would be interested to know how the LSB will link their proposals to that of the Bill.

Diversity

Q11: What are your views on our proposed course of action to conduct research and, depending on the results, either compel transparency of data or encourage it?

37. The BSB is of the view that the consultation paper is light in its understanding of diversity issues in general. As referred to above³², there is a requirement for public

³² Point 26

authorities to gather evidence in relation to the equality and diversity caused by such major policy changes. This example is not adequately reflected in the LSB's approach. For example, in relation to the comments at paragraph 310, there is no evidence whatsoever to support the assertions offered. Similarly, paragraph 314 offers generalisations of positive effects with no proper basis at all. Whilst it is hoped that they will be true, proper consideration of any adverse effects is also required. It should be for the LSB, as oversight regulator, to lead on monitoring impact in this area.

38. In relation to ABSs, it is, of course, difficult to speculate on specific outcomes, beyond perhaps some scenario planning and scoping of potential outcomes (both positive and negative) but this creates a further responsibility to gather data now in relation to the extant situation to bench-mark the present composition of the professions, consumer groups (in terms of gender, ethnicity, age etc) to be able to better monitor the actual impact of these changes. The very real risk with this approach is that by the time any adverse risk to, for example, BME or small firms, is identified, the damage will have been done, perhaps irreparably. Consequently, the BSB's response to the questions at Question 11, are mainly no and where positive, only speculatively so.

International Issues

Q12: Do you agree with our approach to international issues?

39. Similarly to issues raised in the points immediately above, it is hoped that the 'robust protections' envisaged for ABSs will be sufficient to protect the traditional independence of lawyers. Again however, some of the comments in this chapter about the benefits brought by absorbing non-legal sector business and management skills into ABSs³³, are unsubstantiated speculation. The BSB believes therefore that the LSB has dismissed too lightly the objections of other states to ABSs. Where those objections manifest themselves in actual restrictions of ABSs as envisaged from practising in international jurisdictions, there are real potential negative impacts on the ability of ABSs to secure external investment in the first place.

LDPs, Recognised Bodies and other similar entities

³³ Para 330

40. The BSB would be interested in knowing what the outcomes of the LSB research into the LDP and CLC recognised body regime, referred to at paragraphs 337 to 339, actually was.

**Bar Standards Board
February 2010**