



**ALTERNATIVE BUSINESS STRUCTURES :
APPROACHES TO LICENSING**

**CONSULTATION ON DRAFT GUIDANCE TO LICENSING
AUTHORITIES ON THE CONTENTS OF LICENSING RULES**

A RESPONSE BY THE INSTITUTE OF LEGAL EXECUTIVES (ILEX)

19 FEBRUARY 2010

Introduction

This Response represents the views of the Institute of Legal Executives (ILEX), an Approved Regulator under the Legal Services Act and the professional association for Legal Executives, trainee Legal Executives and others employed in delivering legal services.

ILEX and its regulatory arm ILEX Professional Standards Limited (IPS) are committed to regulating Legal Executive businesses and businesses in which Legal Executives are Managers/owners by 2012. IPS will be responsible for establishing that those regulatory arrangements are appropriate for public protection and comply with the requirements of the Legal Services Act and any regulations made by the Legal Services Board under the Act.

Answers are set out below to the questions in the consultation paper, where ILEX is able to offer a view.

THE NEW APPROACH TO REGULATION – STRUCTURE OF LICENSING FRAMEWORK

Question 1 – What is your view of basing the regulation of ABS on outcomes?

We agree that all licensing authorities (LAs) should have the same core outcomes. This is on the basis that the outcomes will be high level. To approach matters differently would lead to confusion for the consumer, assuming that the consumer is at all interested. There is an argument to say that provided the Legal Services Board (LSB) is happy with different core outcomes introduced by different LAs, similarity across core outcomes should not matter.

ILEX is not satisfied that all of the proposed outcomes are appropriate. Our overall view is that not all of the statements made under 'proposed outcomes' in the consultation are indeed outcomes. We believe that a much smaller list would be more consumer friendly. For example it is unclear what the fourth bullet point under 'indemnity and compensation' means. The fifth bullet point

under the same heading is also somewhat vague; what is it to 'unduly restrict commercial decisions?' Under the heading 'Access to Justice', it is unclear whether the outcomes would come from the ABS structure and regulation of them as opposed to anything else. Under 'Appellate bodies', the first bullet point is not an outcome for LAs in their regulation of ABS, although they might be outcomes for the LSB in their requirements of LAs. The same comment applies under the heading 'Special bodies'. Under HoLP/HoFA, we do not view the first bullet point as necessarily an outcome of the regulatory approach to ABS. The regulatory framework cannot ensure that HoLPs and HoFAs come from a wide range of backgrounds and diversity unless the LAs introduce some form of quota arrangements. Under 'Complaints handling for ABS', the first bullet point is not an outcome. Under 'International issues', it is difficult to see how any LAs regulatory approach should lead to this outcome directly.

Our final comment in relation to the outcomes is that they would benefit from the use of plain English.

ILEX agrees that the division between entity and individual regulation as proposed in the paper is appropriate. In any event, the Legal Services Act makes it so.

The consultation does not ask any questions about entity level considerations (paragraph 62, 63, and 64). ILEX would expect in almost every case to see that the entity level consideration will include financial viability, contrary to the statement in the consultation paper. For example, in accrediting private training providers to comply with our responsibilities with Ofqual, we expect information about financial viability. Nothing could be more damaging to a consumer than for them to place their trust and business with an entity that then goes bust. Since the LSB wants to know the Approved Regulator's business strategy planning and reporting, together with 3 year business plans and budgets, it seems sensible that information around these issues ought to be required from those entities who seek regulation. Additionally, in relation

to diversity and social mobility, it might be sensible for entity level considerations to include information about recruitment and retention.

OWNERSHIP TESTS

Question 2 – Do you think our approach set out in this Chapter to the tests for external ownership is appropriate?

ILEX has considerable support for the approach taken by the LSB to the issues of external ownership.

It is difficult to argue against there being a consistency of approach to the tests across all LAs. Otherwise it is very difficult for anyone to describe to a consumer all the pros and cons of each regime. However, ILEX believes that this should be the case in relation to high level core issues, but there should be no restriction on LAs if they wish to impose higher or more stringent tests.

We agree with the LSB's approach to the fitness to own test. The proposals reflect the current proposals in relation to becoming a Legal Executive. We believe the LSB might like to consider including within a fitness to own test issues around disqualification of Directors of limited companies.

Criminal convictions should include spent convictions. This is a requirement in relation to our own members and there seems no reason why it should not be required with regard to ownership of an ABS. ILEX notes that there is an inherent risk in the whole procedure relating to licensing of ABS. Once that inherent risk is accepted, ILEX would urge a core or de minimis approach to regulation wherever possible. So although IPS requires all members seeking to become Fellows of ILEX to declare all convictions including those which are spent, this may be unnecessary in relation to the ownership of an ABS. It may be appropriate for the declaration of spent convictions to include only a set of serious offences relating to dishonesty in particular.

The same comment applies in relation to Associates with a material interest in the business. A risk based approach should require full disclosure of all share holding and directorships made in each licensing case.

However, we would say there should always be a requirement to declare the ultimate beneficial owner of an ABS.

We do not think that any modifications are needed to ensure the approach will work for a listed company. If a risk based approach is taken, that must include the same approach for listed companies. The detail, of course, may be different. Likewise we do not believe there is any particular need for modifications of approach for very small businesses.

There needs to be some flexibility for an LA in how it deals with non-owners, ultimate beneficial owners, and other persons of influence. The use of covenants from those identified as having a significant influence over an ABS is an interesting approach, but the question then becomes: how are the covenants enforced, is the use of a covenant, in fact, a further protection or only a feel good factor?

Where action is taken against people falls short of disqualification ILEX believes that the LSB should note the action taken but not interfere in a decision made by a LA. Tracking this kind of information through the Memorandum of Understanding may be part of the measures against which the LSB measures the LA itself and will certainly form part of the conversations between the LSB and LA regarding approaches to regulation and whether they have the appropriate assessment tools.

INDEMNITY AND COMPENSATION

Question 3 – Indemnity and Compensation

We believe that the consultation paper at paragraph 150 sums up the appropriate approach for PII. There should be a requirement on an ABS to demonstrate to the LA that it has sufficient PII for the risks it faces and the activities it carries out.

ILEX agrees that it is important to have a Compensation Fund in place to cover ABS for the purposes of protecting consumers. There must be

evidence of how a consumer will be compensated. We prefer an approach that puts the burden on the regulated entity, and not on the regulator.

RESERVED AND UNRESERVED LEGAL ACTIVITIES

Question 4 – Do you agree with our position on reserved and non-reserved legal activities?

ILEX agrees that ABS should be treated in a consistent way to non-ABS.

This is an area which needs to be treated with much caution. It would be wrong to prohibit an ABS from setting up separate un-regulated firms to carry out un-reserved legal work if the driver for this is a desire for control and to reserve all work to lawyers and their businesses.

The LSB concedes that making the ABS bring its un-reserved legal activities within the parameters of ABS regulation might lead to increased compliance costs. However, if it is right that an ABS would want to protect its brand value, the ABS will have processes in place to ensure that all advice is of a high standard. If that is the case then there is no need for alternative regulation because they will wish to protect their brand value.

We agree with the conclusion that there is a need for much more information about how well consumers understand the current situation and as to whether there is any actual or potential detriment arising from any confusion.

LA ENFORCEMENT POWERS AND FINANCIAL PENALTIES

Question 5 – Are the enforcement powers for LAs suitable?

The range of enforcement powers set out in the consultation reflects the powers available to LAs under the Legal Services Act 2007. Broadly speaking, ILEX supports the approach of the LSB.

ACCESS TO JUSTICE

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

ILEX generally supports the approach to the definition of access to justice in this context, particularly at paragraph 216, as basically appropriate. However,

we do not think that it is necessarily helpful in all cases to ask an ABS how they anticipate they will improve access to justice. The variations in response, and perhaps even the creativity of response, will not necessarily be relevant to the delivery of the particular legal services in question.

We concur that restriction should not be placed on any type of commercial activity unless there is clear evidence that the particular practice will cause significant harm. The market will decide. We agree with the LSB in their consultation at paragraphs 218 and 221.

It would be quite burdensome for LAs to independently monitor access to justice. We, in fact, believe that this is a role for the oversight regulator, i.e. the LSB in consultation with the LAs, thus ensuring that the LAs take ownership of any results from monitoring or research, but ensuring that there are not a variety of different ways of measuring access to justice

APPELLATE BODIES

Question 7 – What is your view of our preference for a single appeals body?

We accept that a single body is appropriate to hear all appeals. We take this view having considered not only the impact on consumers but in terms of looking at an appellant body that can build up a body of expertise.

We are not in a position to comment particularly on the identification of the GRC as an appropriate body to hear appeals. There is no indication of their capacity to hear such appeals, or of the costs that would arise from using the GRC as an appellate body. This is an area that does require quite considerable further research and discussion.

SPECIAL BODIES

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

Generally we agree with the approach of the LSB to the regulation of special bodies. We agree that it is inherently unsatisfactory that special bodies should be outside of the normal ABS framework in terms of securing quality of

legal services provided and the investigation of complaints. We agree that the risks associated with special bodies are relatively low, which should in due course make the approach to regulation of them fairly straightforward.

HEAD OF LEGAL PRACTICE AND HEAD OF FINANCE AND ADMINISTRATION

Question 9 – Do you think that our approach to HoLP and HoFA is suitable?

We agree that the approach to HoLP and HoFA is appropriate. We support the approach of the LSB in relation to these appointments i.e. that the HoLP and HoFA should undergo a fit and proper test, that there should be training requirements for them and that, dependent upon the ABS itself, the HoLP and HoFA could be the same individual.

COMPLAINTS HANDLING FOR ABS

Question 10 – Do you think that our approach to complaints handling is suitable?

We generally support the approach of the LSB to complaints handling as set out in the consultation.

Our position goes back to first principles which we set out in our Response to Sir David Clementi's Review. ILEX believes in resolving complaints within the firm/ABS, whenever and wherever possible. This raises issues about having clear procedures that are understood by the complainant; clear and appropriate information to all clients; and a positive approach to handling complaints in-house. If however, a complainant is not satisfied with the in-house resolution it is appropriate for all complaints from all quarters including multi-disciplinary practice consumers to go to the OLC. Our position on Clementi was reached precisely to avoid confusion by consumers, and the way to avoid that is for there to be a single 'one stop shop' for complaints. It will then be for the OLC to take that responsibility away from the consumer and to find the appropriate resolution forum if, in fact, the complaint is about a financial services issue (to the FSA) or a misconduct issue (to an AR).

DIVERSITY

Question 11 – 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?

ILEX supports the position taken by the LSB with regard to diversity and ABS. We agree that the overall impact is unlikely to be adverse to the diversity of the profession; indeed there is every possibility that it will assist on diversity issues. It is certainly a distinct possibility that the non-lawyer managers and owners of ABS may open career paths for lawyers and therefore have a positive impact on career progression, sufficient to offset the potential impact of the closure of small firms. We remain cautiously optimistic. Until the whole issue of social mobility, diversity and equality is embedded in all commercial businesses and not merely legal services businesses, it cannot be taken as fact that there will not be a significant impact as the result of closure of small firms.

ILEX is of the view is that it is for ILEX as an LA to obtain or require information about the diversity of workforces within an ABS, and not for the LSB.

INTERNATIONAL ISSUES

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

It is clear that if the international community frowns upon ABS, and inhibits lawyers from other jurisdictions from dealing with lawyers from within an ABS, there could be a significant reluctance on the part of firms which currently have international work from becoming or embracing the ABS structure.

In response to the one question ‘Do you agree with our approach to international issues’, ILEX would agree that there is no reason to limit English and Welsh ABS from expanding internationally if they are able to do so. However, ILEX would want to know much more about the LSB’s intentions when it refers ‘to work with other jurisdictions to inform them about the ABS framework and the protection it provides for lawyers and consumers’, before wholeheartedly agreeing with the LSB approach to international issues.

LEGAL DISCIPLINARY PRACTICES (LDP)s, RECOGNISED BODIES AND OTHER SIMILAR ENTITIES

Question 13 – Should LDPs, Recognised Bodies and other similar firms have transitional arrangements into the wider ABS framework in the way we propose?

OTHER ISSUES

Question 14 – Should ABS licences be issued for indefinite periods?

We believe this is one area which it should be for each individual LA to decide. This would increase competition between LAs and, provided the LSB is satisfied that the approach meets consumer protection standards; there should be no reason to inhibit how licences are issued and over what period.

REGULATORY OVERLAPS

Question 15 – Do you agree with our approach to managing regulatory overlaps?

ILEX is broadly supportive of the LSB approach to regulatory overlaps.