



Summary of decision

The purpose of this summary sheet is to provide a high level and accessible overview of the Legal Services Board's ("the LSB") decision. Readers are recommended to read the formal decision notice below for further detail. **This summary is not and should not be taken as a formal part of the LSB's decision notice under the Legal Services Act 2007 ("the Act").**

The LSB's decision is to grant in full the application from the Solicitors Regulation Authority (SRA) approving alterations to its regulatory arrangements in respect of its Compensation Fund. The application proposes that the contribution level for 2020/21 is £14.5m (reduced from £17.5m in 2019/20). This will mean an individual contribution of £50 (2019/20: £60) and a firm contribution of £950 (2019/20: £1,150).

Following the assessment of the SRA's application, the LSB has concluded that the changes do not meet the refusal criteria in the Act.

Decision notice

The Solicitors Regulation Authority (“SRA”) rule change application for approval of alterations to the regulatory arrangements relating to Compensation Fund contributions for 2020/21

1. The Legal Services Board (“**LSB**”) has granted an application from the Solicitors Regulation Authority (“**SRA**”) for approval of Compensation Fund Determinations for 2020/21 which set the level of contribution to the SRA Compensation Fund for individual solicitors, and recognised sole practitioners and recognised bodies who receive or hold client money, authorised by the SRA.
2. The LSB is required by Part 3 of Schedule 4 to the Legal Services Act 2007 (“the Act”) to review and grant or refuse applications by approved regulators to make alterations to their regulatory arrangements. The Law Society is an approved regulator and the SRA is the regulatory arm to which the Law Society has delegated its regulatory functions.
3. This decision notice sets out the decision taken, including a description of the changes. The notes at page 7 of this notice explain the statutory basis for the decision.
4. The chronology for the LSB’s handling of this application is also set out below.

Chronology

- The LSB confirmed receipt of an application from the SRA on 16 July 2020.
- The 28-day initial decision period for considering the application ends on 12 August 2020.
- This decision notice is effective from 12 August 2020.
- The decision notice will be published on the LSB’s website by 14 August 2020.

Background

5. On 16 July 2020, the SRA submitted an application to the LSB for approval of changes to its regulatory arrangements relating to Compensation Fund contributions.
6. Each year the SRA considers the level of contributions required for the Compensation Fund from the individuals and firms that it authorises.
7. The established apportionment used for allocating the cost of the Compensation Fund is that 50% of the cost is contributed by regulated individuals and 50% is contributed by regulated firms holding client money. The SRA sets the proposed level of contribution by assessing expected pay outs and levels of claims against historic trends on claims numbers, amounts and timings.
8. In recent years the SRA has taken steps to increase the size Compensation Fund. The increase was made to take account of a number of cases of exceptionally high

cost, arising largely from solicitor involvement in investment schemes where consumers have suffered significant losses.

9. During the same time there has been a decline in the number and complexity of “business as usual” interventions. The impact of this decline has resulted in a lower level of claims.
10. In addition to the trends described above, the SRA has also considered the potential impact of the Covid-19 outbreak on the solicitor profession.
11. As a result of its analysis, the SRA considers that the minimum reserve requirements it has set can be satisfied by a lower level of contribution in the coming year.

Proposed changes

12. A contribution level of £14.5m has been proposed for 2020/21 compared to £17.5m for 2019/20. The SRA has therefore determined that the contributions required are £50 from individuals and £950 from firms. Contributions for 2019/20 were £60 and £1,150, respectively.

Key issues considered in the assessment

13. The LSB notes the fact the SRA has been able to propose a reduction in contributions whilst maintaining an appropriate fund to provide contingency for high value contentious claims and the impact of Covid-19.
14. Having considered the SRA’s application and supporting documents, the LSB makes the following key points in relation to the application.

Covid-19 Impact

15. The SRA has made provision for the impact of Covid-19 on the profession. The application notes that it is not possible at this time to predict the impact of Covid-19 on the Compensation Fund, however it considers that it is reasonable to conclude that some firms will close as a result of the economic impact of the pandemic. It has made allowances for an increase in the number of firm closures and associated interventions, which often result in a call on the Compensation Fund, in the forecasting model.
16. The SRA application notes that the highest level of grants paid out in the last 15 years was in 2010 when grants from the fund amounted to a total of £27m. If such a year were repeated, grants would be £9m above the current forecast.
17. Having considered the impact increases in interventions could have and historic levels of compensation paid the SRA is satisfied that the proposed contribution and forecasted reserves are suitable to meet the risks associated with a potential increase in calls on the compensation fund flowing from the pandemic.

Holding client money

18. In the 2019 decision notice we stated that the SRA should consider taking steps to make it clearer to firms that they will not be liable to pay a contribution to the fund if they do not hold client money. We explained that this would reduce the risk of firms who do not need to contribute to the fund making unnecessary payments.
19. We asked the SRA whether it had considered taking any action based on our comment. During our consideration of the application the SRA confirmed that firms go through an online process to calculate both periodic fees and Compensation Fund contributions they are required to pay. One of the questions they complete is whether they hold client money, and this then forms part of the fee calculation. It is only after completing the process that they are informed of the fees that they must pay and issued with an invoice for payment. Consequently, we are satisfied that the risk of overpayment has been mitigated, as firms are not expected to calculate their own fees.

Consultation

20. In last year's decision¹ the LSB set out an expectation that the SRA would either consult on the proposed level contribution or explain the reasoning behind decisions not to consult in its application.
21. In this year's application the SRA set out its consultation on its Corporate Strategy for 2020-2023 as providing respondents with an opportunity to influence the SRA programme of work, and in turn, its budget.
22. The SRA also explained it held a specific consultation exercise around the future of its compensation arrangements² from January-April 2020. The consultation was focused on the purpose of the fund, eligibility and on its proposals to cap grants from the fund. It should be noted that at the time the application was developed the consultation responses were under consideration. The application for 2020/21 fees is therefore based on the existing arrangements and methodology.
23. The SRA has now published a document summarising the consultation responses and confirming its position³. It intends to submit proposed alterations to its compensation fund rules to the LSB for formal approval.
24. In addition, the SRA explained that the consultation on its 2020/21 Business Plan⁴ includes a consultation question on proposed principles for setting the level of contributions to the Compensation Fund. Once agreed, the principles will inform the

¹ <https://www.legalservicesboard.org.uk/wp-content/uploads/2019/08/PCF-Decision-Final-Copy.pdf>

² <https://www.sra.org.uk/sra/consultations/consultation-listing/comp-fund-reform-2020/?s=c>

³ <https://www.sra.org.uk/globalassets/documents/sra/consultations/compensation-fund-summary-of-responses-and-sra-position-1.pdf?version=4a21ed>

⁴ <https://www.sra.org.uk/sra/consultations/consultation-listing/business-plan-2020-21>

process for setting the contribution in future years and will provide further clarity to fee payers in the future.

25. The SRA did not directly consult on the proposed level of contribution for this year and did not explain in its application the reasoning behind its decision not to consult. We asked the SRA about this omission during the course of our consideration of the application.
26. The SRA stated that it considered, in line with previous years, that it would not be possible to provide sufficient information to allow for a meaningful consultation on the specific quantity of compensation fund contributions, given the sensitive information that its calculations are based upon. However, in recognition of the points raised by the LSB last year, it is now consulting on the general principles, as set out above.
27. The SRA has confirmed that future applications will refer directly to the principles and how they have applied them. We expect the SRA to describe how the principles have been applied in future applications but also to provide a similar description to firms and individuals who contribute to the fund.

Apportionment and Impact

28. The SRA is continuing to use its established apportionment for contributions to the fund.
29. The SRA identified in its 2017 application that the apportionment it uses is likely to have a greater impact on sole practitioners and firms with 2-4 partners. It has also identified that this means there is a greater impact on BAME (Black, Asian, and Minority Ethnic) solicitors who are disproportionately represented in this cohort.
30. The SRA has referenced this differential impact in each of its applications from 2017-2020 and has on several occasions stated that it has been reviewing or consulting on revisions to the Compensation Fund rules.
31. During the course of the application we asked the SRA to provide us with any equality, diversity and inclusion (EDI) impact assessment it had undertaken to inform those findings. Despite having identified a greater impact on sole practitioners and firms with 2-4 partners in 2017 the SRA has not undertaken an EDI impact assessment relating directly to Compensation Fund contributions.
32. The SRA explained that as part of the ongoing fees review it will be considering whether the current apportionment is appropriate, and any proposed changes will be supported by an EDI impact assessment.
33. We sought further assurance from the SRA that through its fees review and associated EDI impact assessment it would not only consider the differential impact it has identified but consider how it will be mitigated. The SRA explained that the review will include identification of differential impacts and will either propose to mitigate them

or offer an explanation in circumstances where it concludes such mitigation is not appropriate.

34. It is regrettable that an updated EDI has not been provided in the period since the differential impact has been identified. However, we are assured by the commitment of the SRA to include within its fees review a focus on the EDI implications of the compensation fund contributions.
35. We expect the next application relating to Compensation Fund contributions to include an explanation of progress in relation to the differential impact the SRA has already identified regardless of whether the wider fees review has been completed.

Decision

36. The LSB has considered the SRA's application against the refusal criteria in paragraph 25(3) of Schedule 4 to the Act. It considers that there is no reason to refuse this application and accordingly, the application is granted.
37. **Annex A** to this decision notice contains the Determination of Compensation Fund contributions approved by the LSB.

Matthew Hill, Chief Executive

Acting under delegated authority granted by the Board of the Legal Services Board

Notes:

1. The LSB is required by Part 3 of Schedule 4 to the Act to review and grant or refuse applications by approved regulators to make alterations to their regulatory arrangements.
2. Paragraph 25(3) of Schedule 4 to the Act explains that the LSB may refuse an application setting out a proposed change to the regulatory arrangements only if it is satisfied that:
 - (a) granting the application would be prejudicial to the regulatory objectives
 - (b) granting the application would be contrary to any provision made by or by virtue of the Act or any other enactment or would result in any of the designation requirements ceasing to be satisfied in relation to the approved regulator
 - (c) granting the application would be contrary to the public interest
 - (d) the alteration would enable the approved regulator to authorise persons to carry on activities which are reserved legal activities in relation to which it is not a relevant approved regulator
 - (e) the alteration would enable the approved regulator to license persons under Part 5 [of the Act] to carry on activities which are reserved legal activities in relation to which it is not a licensing authority, or
 - (f) the alteration has been or is likely to be made otherwise than in accordance with the procedures (whether statutory or otherwise) which apply in relation to the making of the alteration.
3. The designation requirements referred to in paragraph 2(b) above are set out in paragraph 25(4) of Schedule 4 to the Act and are:
 - (a) a requirement that the approved regulator has appropriate internal governance arrangements in place
 - (b) a requirement that the applicant is competent, and has sufficient resources to perform the role of approved regulator in relation to the reserved legal activities in respect of which it is designated, and
 - (c) the requirements set out in paragraphs 13(2)(c) to (e) of Schedule 4, namely that the regulatory arrangements are appropriate, comply with the requirements in respect of resolution of regulatory conflict (imposed by sections 52 and 54 of the Act) and comply with the requirements in relation to the handling of complaints (imposed by sections 112 and 145 of the Act).
4. In accordance with paragraphs 20(1) and 23(3) of Schedule 4 to the Act, the LSB has made rules⁵ about the manner and form in which applications to alter regulatory arrangements must be made. Amongst other things, the rules highlight the applicant's obligations under section 28 of the Act to have regard to the Better Regulation Principles. They also require applicants to provide information about each proposed change and details of the consultation undertaken.
5. If the LSB is not satisfied that one or more of the criteria for refusal are met, then it must approve the application in whole, or the parts of it that can be approved.

⁵ LSB's Rules for applications to alter regulatory arrangements – Version 2 April 2018
[https://www.legalservicesboard.org.uk/what_we_do/regulation/pdf/New%20folder%20\(2\)/FINAL_Rules_for_applications_to_alter_regulatory_arrangements.pdf](https://www.legalservicesboard.org.uk/what_we_do/regulation/pdf/New%20folder%20(2)/FINAL_Rules_for_applications_to_alter_regulatory_arrangements.pdf)

Annex A – SRA Fee Determinations

Determination of Compensation Fund contributions 2020

This determination is made by the Solicitors Regulation Authority Board under rule 1.2 of the SRA Compensation Fund Rules, with the approval of the Legal Services Board under paragraph 19 of Schedule 4 to the Legal Services Act 2007.

- (1) Every person who applies for a practising certificate to commence on or after 1 November 2020, or who applies for initial registration or renewal of registration as a registered European lawyer or registered foreign lawyer to commence on or after 1 November 2020, shall pay with the fee payable in respect of that application, a contribution of £50 to the Fund.
- (2) Every recognised body or recognised sole practice that has held or received client money (as defined in the SRA Accounts Rules) during the period 1 November 2020 to 31 October 2021, shall pay with the annual periodical fee, a contribution of £950 to the Fund.
- (3) Every person that:
 - (a) applies for initial recognition as a recognised body or initial recognition as a recognised sole practice to commence during the period 1 November 2020 to 31 October 2021; and
 - (b) intends to hold or receive client money (as defined in the SRA Accounts Rules) at any time during the period 1 November 2020 to 31 October 2021.

shall pay with the fee payable in respect of that application, a contribution to the Fund as follows:

- i. £950 on applying for initial recognition to commence in the period 1 November 2020 to 31 December 2020;
 - ii. £712 on applying for initial recognition to commence in the period 1 January 2021 to 31 March 2021;
 - iii. £475 on applying for initial recognition to commence in the period 1 April 2021 to 30 June 2021;
 - iv. £237 on applying for initial recognition to commence in the period 1 July 2021 to 31 October 2021.
- (4) The SRA may waive the contribution payable under paragraph (3) above in circumstances where the initial application is made by a body which is changing its legal status or is succeeding to the practice of another authorised body and the predecessor body or practitioner has already paid a contribution to the Fund.

- (5) In this determination:

Fund means the Solicitors' Compensation Fund established and maintained under rule 1.1 of the SRA Compensation Fund Rules;

All other terms are to be interpreted in accordance with the Practising Certificate Fee Determination 2020.

- (6) This determination shall come into force on 1 November 2020.

Determination of Compensation Fund contributions for Licensed Bodies 2020

This determination is made by the Solicitors Regulation Authority Board under rule 1.2 of the SRA Compensation Fund Rules, with the approval of the Legal Services Board under paragraph 19 of Schedule 4 to the Legal Services Act 2007.

- (1) Every licensed body that held or received client money (as defined in the SRA Accounts Rules) at any time during the period 1 November 2020 to 31 October 2021, shall pay, with the annual periodical fee, a contribution of £950 to the Fund.
- (2) Every licensed body that intends to hold or receive client money (as defined in the SRA Accounts Rules) at any time from the date on which the body is authorised to 31 October 2020, shall pay, with the initial periodical fee, a contribution to the Fund as follows:
- i. £950 on applying for initial recognition to commence in the period 1 November 2020 to 31 December 2020;
 - ii. £712 on applying for initial recognition to commence in the period 1 January 2021 to 31 March 2021;
 - iii. £475 on applying for initial recognition to commence in the period 1 April 2021 to 30 June 2021;
 - iv. £237 on applying for initial recognition to commence in the period 1 July 2021 to 31 October 2021.
- (3) The SRA may waive the contribution payable under paragraph (2) above in circumstances where the initial application is made by a body which is changing its legal status or is succeeding to the practice of a recognised body or recognised sole practitioner and the predecessor body or practitioner has already paid a contribution to the Fund.
- (4) In this determination:
- Fund** means the Solicitors' Compensation Fund established and maintained under rule 1.1 of the SRA Compensation Fund Rules;
- All other terms are to be interpreted in accordance with the Licensed Body Fee Determination 2020.
- (5) This determination shall come into force on 1 November 2020.