

To:	Legal Services Board	
Date of Meeting:	29 January 2014	Item: Paper (14) 01

Title:	SRA performance in ABS authorisations	
Workstream(s):	Developing regulatory standards	
Author / Introduced by:	Fran Gillon, Director of Regulatory Practice fran.gillon@legalservicesboard.org.uk / 020 7271 0087	
	James Meyrick, Regulatory Project Manager james.meyrick@legalservicesboard.org.uk / 020 7271 0083	
Status:	Unclassified	

Summary:

We have been monitoring the SRA's performance on authorisations since January 2013. This followed increasing frustration and concern from a number of sectors about the way the SRA appears to have been considering applications for ABS licences.

In September 2013 the Board asked for a report to be prepared for this meeting that covers:

- a) SRA performance on ABS authorisations (and whether expected improvements have been delivered)
- b) the SRA's progress in introducing other changes in relation to regulatory scope and action issues surrounding MDPs (and whether this is credible and acceptable)
- c) the sustainability of the improvements put in place.

We consider that the SRA performance has greatly improved and it has credible plans to improve the capacity and capability of the firm based authorisation team to ensure that these improvements are sustainable and there is continuous improvement. There remain issues regarding the amount of information required and how that information is used and we have some concern about the age of applicants that have withdrawn. We intend to visit the SRA to discuss their use of information and they have introduced changes that should help to reduce the number of withdrawals.

The most troubling issue remains the apparent difficulty faced by applicants that do not look like traditional legal businesses. Business services type firms and those offering multi-disciplinary services are more likely to withdraw their application or still be under consideration. Firms in these categories that do eventually get granted a licence take longer than applications from traditional law firms. Anecdotally those businesses that have been granted licences have had to make changes to their structure and business model above and beyond what they had originally contemplated. We conclude that the main driver for these difficulties are the SRA's

rules and its approach to the scope of regulation.

The SRA appears, at Executive level, to be committed in its desire to resolve the negative impact of the separate business rule and surrounding rules on ABS applicants and to engage with applicants. However we still consider that the SRA's approach is impacting competition, access to justice and negatively affecting consumers. The LSB considers that the SRA needs to set out publically its objectives and timetable for work in this area. The LSB will also have to conduct work in this area to ensure appropriate pace and activity.

Recommendations:

The Board is invited to:

- a) Agree that the LSB should continue to monitor and report on the SRA's performance in ABS authorisation and note that the LSB will visit the SRA in the next few months.
- b) To agree that we should continue to press for work on the separate business rule, that the scope of regulation should be prioritised and, that we should be prepared to tackle it ourselves in the absence of sufficiently clear commitments
- c) To agree that it is not necessary to undertake a formal review into the issue of ABS authorisations at this point, but to maintain the issue as a standing agenda item in the CEO's report, or separately, at least until the middle of the year.

Risks and mitigations

Financial: None

Legal: We have used our information gathering powers to support this project. We have sought additional legal advice on our powers in relation to enforcement and oversight.

Reputational: Our strong pursuit of this subject is impacting relationships and co-operation with the SRA – both staff and Board - and may also potentially do so with other regulators. However change of personnel within SRA may make it less of an issue than previously.

Resource: This work remains a significant, but thus far manageable, burden on staff, especially the senior team, but this reflects the priority which the Board has given to authorisations.

Consultation	Yes	No	Who / why?
Board Members:		X	
Consumer Panel:		X	N/A
Others:	None		

Freedom of Information Act 2000 (Fol)

Para ref	Fol exemption and summary	Expires
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LEGAL SERVICES BOARD

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SRA performance in ABS authorisations

1. We have been monitoring the SRA's performance on authorisations since January 2013. This followed increasing frustration and concern from a number of sectors about the way the SRA is considering applications for ABS licences.
2. After the Board to Board discussion in July 2013 which gave a high profile to the issue, the Board received a detailed report on the SRA's performance at its September meeting. Short updates were provided in the CEO update for the subsequent meetings of 2013. In September 2013 the Board asked for a report to be prepared for this meeting that covers:
 - a) SRA performance on ABS authorisations (and whether expected improvements have been delivered)
 - b) the SRA's progress in introducing other changes in relation to regulatory scope and action issues surrounding MDPs (and whether this is credible and acceptable)
 - c) the sustainability of the improvements put in place.

This paper covers these issues and makes recommendations about next steps.

Overall performance and work in progress

3. According to the data provided, by 15 January 2014 the SRA had received 418 applications for ABS status since it was designated as a licensing authority. Of these applications the SRA has granted 243 licences. 106 have withdrawn and 55 remain work in progress. The remainder (14) appear to have been errors in the data provided (most of the errors are from the spreadsheets provided in early 2013). Since January 2013 the SRA has closed 80 applications through withdrawals and granted 168 ABS licences. A series of charts showing the detailed monthly statistics are provided at annex A.
4. It takes an average of 7 months from the submission of an application for a firm to be granted an ABS licence and 20% of applicants had to wait over 9 months for their licence.
5. The average age of a „work in progress' application is currently 4.6 months and 29% of the work in progress applications are over 6 months old. However, none of the applications are over 12 months old (although the oldest dates from 18 February 2013). Figure 1 below shows the reduction in the old „work in progress' applications over the last year.

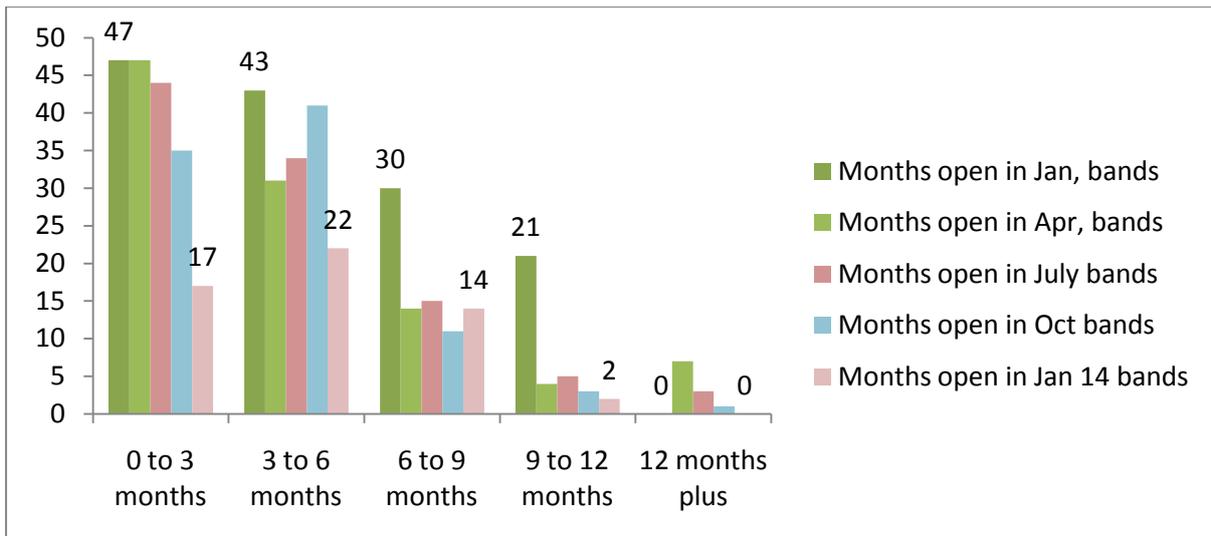


Figure 1: SRA work in progress in a sample of months since January 2013

6. The SRA has concentrated on making decisions on the oldest, more difficult and protracted applications (this includes decisions related to recognised bodies as well as ABS applications). The figure above shows the impact of this focus. There are now only two applications that are more than 9 months old and 14 are between six months and nine months old. By comparison, in January 2013 there were 21 applications over nine months old and 30 were between six and nine months old.
7. It remains the case that the SRA does not officially consider that the statutory decision period has begun until an application has been deemed complete and the licence fee invoice paid. This is broadly analogous with start of their “stage 2: research” status. Figure 2 below shows the current profile of the work in progress according to status of the applicant. The average age of the 24 applications that have not reached “stage 2 - research” status is three months old. The oldest application that has not been deemed complete is 8 months old.

	Number	Oldest	Average	%age
New application	10	2	1	18%
Stage 1 - Complete Application	14	8	4	25%
Stage 2 – Research	14	11	5	25%
Stage 3 – Evaluation	8	8	7	15%
Stage 4 - Decision	9	9	6	16%

Figure 2: Table showing status and age of work in progress in January 2014

8. The SRA has introduced a new triage approach to ensuring that files do not remain incomplete for a considerable length of time and applications that do not appear to be eligible for a licence are either resubmitted in a licensible form or withdrawn. The SRA has told the LSB that these changes, together with a greater degree of engagement with potential applicants before submission has delivered improvements. The SRA has also begun reporting to management and to the SRA Board on end-to-end figures as opposed to figures derived from the date an application is deemed complete. Both of these changes have

been advocated by the LSB for some time we consider that they are likely to deliver improvements.

Withdrawals

9. So far a quarter of all applicants have withdrawn their application and the SRA has not, according to the status shown in the spreadsheet, refused an application. To find out more about these applicants we have conducted some analysis of the November 2013 data to determine how long on average it takes for an applicant to withdraw their application.
10. The spreadsheet does not include a date of withdrawal for each applicant. Therefore, we must use the date of the spreadsheet in which an applicant was first listed as withdrawn as a proxy for withdrawal date. This meant we are unable to analyse the information from applicants that withdrew before we started monitoring the SRA's data in January 2013, and consequently, of the 99 withdrawals shown in the November 2013 data, only 76 could be analysed. Analysis of these applications shows that the average age of an application at withdrawal was around seven months, the same amount of time it takes to get a licence.
11. Figure 3 below shows the age bands of the withdrawn applications that we have been able to analyse. It shows that 57% of the analysed applications were older than six months old when they withdrew.

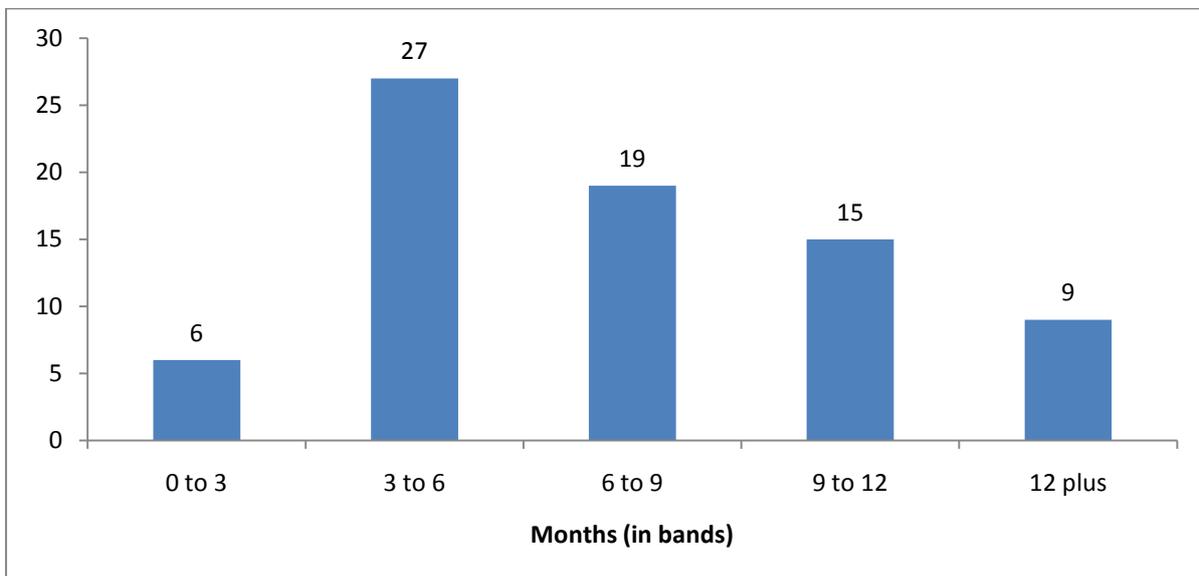


Figure 3: Age of withdrawn applications (up to November 2013)

12. The SRA recognises that a number of applications were allowed to stay incomplete for too long a period and that these files could have been dealt with earlier. It considers that the new approach to triaging applications for completeness and eligibility should reduce the risk of this occurring again. It also observes that its focus on the most protracted old cases led to a number of these applicants withdrawing their applications. This accounts for some of the oldest withdrawals. The SRA has conducted some analysis of applicants that have withdrawn. Based on this analysis it considers that the changes they

have made with regard to triaging and pre-application engagement should reduce the number of withdrawals and those that do withdraw should be younger at the time of withdrawal.

13. The SRA has surveyed all those applicants that have withdrawn their application, alongside a survey of successful applicants. As of 20 January the SRA had a disappointing response to this survey. However, it is also conducting qualitative interviews with applicants. The SRA expect to produce a report based on this research that will be considered by their board and for the research to be published in some form. We have made clear to them that we consider that the reputational damage arising from firms withdrawing applications out of frustration with delay or perceived over-complex investigation of an application is far greater than taking a robust evidence based decision to refuse an application at an early stage.

Category of applicant

14. We conducted analysis of the SRA’s data to see if we could determine whether applicants from certain categories of business or whether new entrants are encountering greater difficulties or a significantly longer decision making period than firms already regulated by the SRA.

15. The data provided does not make it easy to determine which applications were from existing SRA regulated firms or from new entrants. However, desk research has been undertaken by the LSB to attempt to determine figures. We also conducted desk research to determine what sector applicants came from.

16. Of the 418 applicants, 239 were from existing SRA regulated firms, 115 from those not regulated by the SRA at the time of application and for 64 their regulatory status at point of application could not be determined. 14 were errors in the data (as discussed at paragraph 3).

17. The SRA has licensed 150 firms that were already regulated by it. 70 licences have been issued to firms not already regulated by the SRA at the point of application and 23 to firms who it has not been possible to determine whether they were regulated by the SRA or not at the point of application. Therefore around 28% of licences have been granted to firms that were not already regulated by the SRA. Figure 4 below shows this breakdown

	Applicants	Licensed	WIP	Withdrawn / Other
Already SRA regulated	238	150	28	53
Not SRA regulated	115	70	8	32
Not known	64	23	18	21

Figure 4: Regulated status of applicant at the point of application and outcome as at January 2014

18. The figures suggest that it takes the SRA, on average, slightly, but not excessively, longer to grant an ABS licence to a firm that was not already regulated by it than one it already regulated (7.2 months compared to 6.4 months).

19. We also looked at whether applicants offering different types of service are encountering particular difficulties when applying for an ABS licence. Definitions were determined with reference to published information on individual firms' websites and the absolute numbers are relatively low so the information is indicative at best.
20. The two most prevalent categories of applicants remained the self styled „full service law firms' (consumer and commercial lawyers in the chart below), and those firms that describe themselves as „niche' or „specialist' (single legal discipline/consumer type in the chart below), excluding those who specialise in Personal Injury (PI) which we have recorded separately.

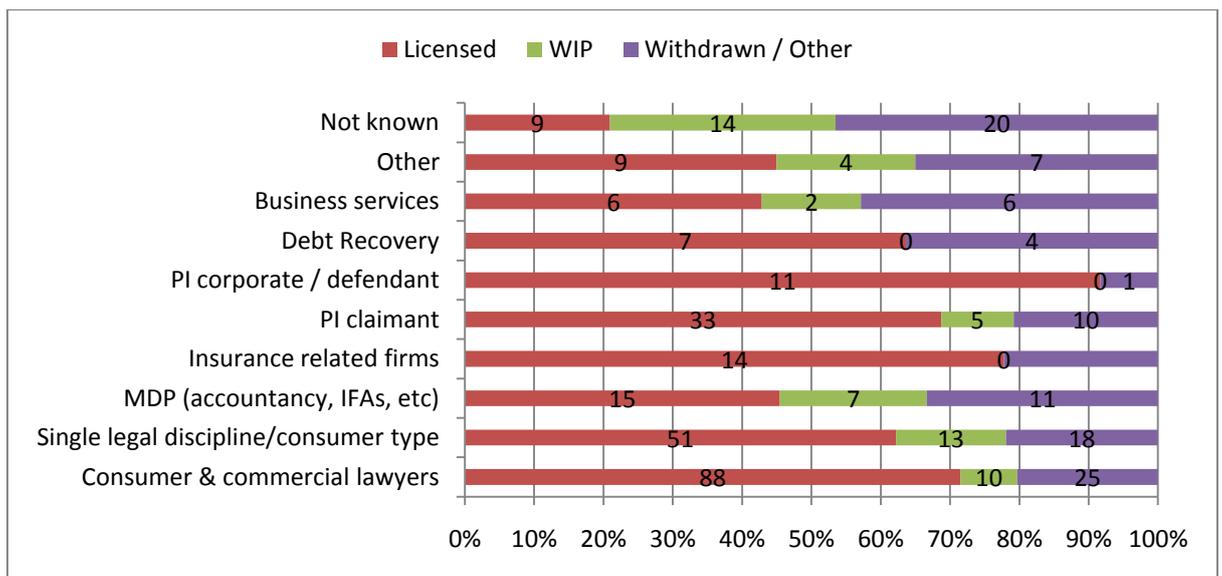


Figure 5: Status of applicants from different business category (January 2014)

21. The data labels in figure show the absolute numbers of applicants and on the x-axis the percentage for each category. The figure shows that, aside from firms where it was not possible to determine what services they offer, the least successful applicants so far have been applicants classed as business services; only 43% of these applicants have been granted a licence. These are firms that typically offer HR, employment or other services to businesses. The next least successful are those categorised as „other' and the category of „accountants, IFAs or wealth managers' or MDPs; only 45% of applicants from these categories have been successful. MDP applicants are typically firms that are seeking to offer, or already do offer, a number of regulated services in addition to legal services. (e.g. they are regulated by the FCA, the accountancy regulators or other statutory regulator). Applicant categorised as „other' includes recruitment/employment agencies, legal outsourcers and consultancies, membership bodies and a variety of other firms.
22. The category of applicant that is granted its licence in the quickest average time are those from the categories of consumer and commercial law, insurance and debt recovery. All with an average of 6 months. The longest average time is for applicants from the category of MDP (Accountancy, IFAs, etc) with an average time to grant a licence of 8.5 months.

23. The LSB considers that the data shows that the SRA has been able to issue licences to more straightforward applicants or service offerings that they are more comfortable with in a swifter manner. Applicants, that are more complex businesses or are offering services that are not necessarily akin to a traditional law firm appear to have to wait longer for a decision to be made and are more likely to withdraw their application. This apparent preference towards traditional law firm-like applicants may be impacting the level of innovation and so competition in the market for legal services. The Act was passed with the intention of liberalising the market for legal services and for greater provision of „one-stop-shop’ style services for individual consumers and business.
24. We also understand that some of those atypical applicants have felt compelled to set up separate law businesses when there are no commercial drivers to do so. Also we have been told by applicants that the SRA is insisting on regulating all “legal activities” – including tax advice – even when it is clear that these activities are subject to other regulatory oversight by other bodies. This has led to the situation where some atypical applicants that have been granted licences have had to alter their business model in a manner that they would not have chosen to do so.
25. We consider that there are a number of drivers that have led to the picture painted by the data.
- a) The first is the existing rules of the SRA. This includes the separate business rule primarily but is also complicated by the SRA interpretation of the PII rules, the compensation fund and the practicing fee requirements.
 - b) The second reason is cultural. We consider that the SRA has, perhaps understandably, found it easier to understand applicants that are akin to those they already regulate. Therefore these applicants have been granted their application more quickly.
 - c) The third reason is the initial approach by the SRA to risk. We consider that initially it looked at applications and the accompanying business plan in a risk averse manner in which there was not necessarily a presumption of issuing a licence.
 - d) Fourthly, the SRA has an approach to regulation that appears to assume that all activities undertaken by an ABS or connected companies are subject to SRA regulation even if said activities are regulated by others or not subject to legal regulation ordinarily.
 - e) Finally, the SRA has indicated to the LSB that it considers that the Solicitors Act 1974 *requires* them to regulate all activities carried out by a recognised body. However, the LSB takes the view that the Solicitors Act 1974 provides discretion,
26. The SRA has asserted that it has an aspiration to undertake work on the scope of regulation, the authorisation of MDPs and the separate business rule. This work does not yet have a timetable or endorsement from their Board.

However, the SRA is keen to stress that the work does have momentum. The LSB in its draft business plan for 2014/15 suggested that it may undertake a thematic review on the extent to which regulation (for example the SRA's Separate Business Rule) unnecessarily prevents legal services providers from structuring their businesses, offering different types of legal and non-legal services and rewarding their employees in ways that they want to commercially. We may also wish to consider conducting a thematic review on scope of regulation issues in relation to authorisation. Once we have considered all the responses to the business plan consultation we will determine what thematic reviews we intend to undertake during 2014/15. It may be that we will gain sufficient clarity about SRA intentions to not undertake the work ourselves, but we are some way from that point at this moment.

27. The issue of cultural change and risk appetite is considered below.

Capacity and capability

28. A new Director of Authorisation took up post in June 2013. Before that date and increasingly since the Director took up her post the SRA has delivered changes to its authorisation process in line with our priorities. It has got rid of the two stage application process and made the single application form available on-line. It has reduced its backlog and the oldest outstanding cases. It is reporting on end-to-end time taken for decisions (not the partial measure of complete application to decision). We also consider that overall performance appears more stable in the area of ABS authorisations: since May 2013 the SRA has issued between 9 and 15 ABS licences each month. The number of work in progress applications has reduced from over hundred in May 2013 to 55 in January 2014.

29. [REDACTED]

30. The new Head of Authorisation will be given the mandate to review the whole firm authorisation process and to develop improvements. Therefore it does not envisage wholesale changes to its approach in the immediate future. What it is doing is trying to make minor iterative improvements to the application form and its approach. The aim is to minimise the amount of common errors and omissions and to remove unnecessary information requirements.

31. The LSB remains concerned about the assessment of applicants' business plans that is part of the authorisation process. We consider that it is not a regulator's job to judge the likely success of an applicant's business model prior to authorisation. However, we do accept that such information can assist in devising a supervisory approach and risk assessing a regulated firm. The SRA has assured the LSB that it is using such information to understand the

structure of the applicant and determine where significant influence lies. However, the SRA has stated that it will review this in the near future.

32. The LSB accepts the SRA's point about making iterative improvements rather than wholesale changes at this point. The SRA has asked the LSB to visit the firm based authorisation team to observe how their approach to risk is operating at the authorisation stage and see the new team in operation.

General conclusions

33. We consider that the SRA has made significant progress since the LSB started monitoring ABS authorisation in January 2013. It has cleared significant amounts of backlog, resolved the oldest most protracted cases and (anecdotally) applications made using the new single application form appear to be progressing well. The SRA is also committed to making iterative improvements to the application form as necessary. The LSB considers that the SRA's information requirements from applicants still go beyond the requirements of the Act and we are concerned that its approach to business plans and risk may be disproportionate and untargeted.
34. The SRA has not changed its approach to the decision period (paragraph 2, schedule 11 of the Act). Therefore it remains questionable whether this is reasonable. However, the SRA is reporting and measuring performance based on the end-to-end decision time and not an artificial period based on when the SRA deems an application complete. It is the end-to-end approach that reflects the experience of the applicant. We consider that the SRA should make its performance on this measure publically available.
35. The most troubling issue remains the apparent difficulty in getting authorised that is faced by applicants that do not resemble traditional legal businesses. Business services type firms and those offering multi-disciplinary services (along with those categorised as other) are more likely to withdraw their application or to be work in progress. Firms in these categories that are successful take longer to be granted licences than traditional legal businesses. Anecdotally those businesses that have been granted licences have had to make changes to their structure and business model above and beyond what they had originally contemplated. We consider that this has the potential to damage competition and dull the impact of the Act on the market for legal services. We conclude that the main driver for these difficulties is the SRA's rules, in particular the Separate Business Rule, and its approach to the scope of regulation. We also do not know the extent to which the approach of the SRA is having a chilling effect on the market.
36. We have received reports from MDP applicants, including some of the most high profile ones, and other potential applicants of a more positive attitude from the SRA in recent months. The SRA itself has reported to the LSB that there is a determination and momentum to work on these issues. However, we have not been provided with any key objectives or timeline for work on the underlying issues.

37. While progress on MDPs is welcome, we also need to be mindful of comments received from the ICAEW, suggesting that the SRA's approach to the scope of regulation is having the effect of restricting the services which can be offered by solicitors in entities regulated by a different licensing authority. Hence, it can have the effect of skewing a new entrant's choice of licensing authority. There are therefore broader questions about the SRA's position on the scope of regulation which need to be pursued and the Chief Executive has already started to address that issue with the incoming CEO at SRA.
38. In conclusion, we consider that the SRA performance has greatly improved and it has credible plans to improve the capacity and capability of the firm based authorisation team to ensure that these improvements are sustainable and there is continuous improvement. The LSB, while welcoming of the willingness of the SRA to talk seriously about the impact of the separate business rule on applicants and to engage with MDP-type applications, still considers that the SRA's approach has the potential to adversely impact competition, access to justice and negatively harm consumers. The LSB considers that the SRA needs to set out publically its objectives and timetable for work in this area. The LSB will also probably have to conduct work in this area to ensure appropriate pace and activity.

Recommendation

39. The Board is invited to:
- a) Agree that the LSB should continue to monitor and report on the SRA's performance in ABS authorisation and note that the LSB will visit the SRA in the next few months.
 - b) To agree that we should continue to press for work on the separate business rule and the scope of regulation should be prioritised and be prepared to tackle it ourselves in the absence of sufficiently clear commitments
 - c) To agree that it is not necessary to undertake a formal review into the area of ABS authorisations at this point, but to maintain the issue as a standing agenda item on the CEO report or separately at least until the middle of the year.

Annex A: Detailed ABS performance statistics (month by month)

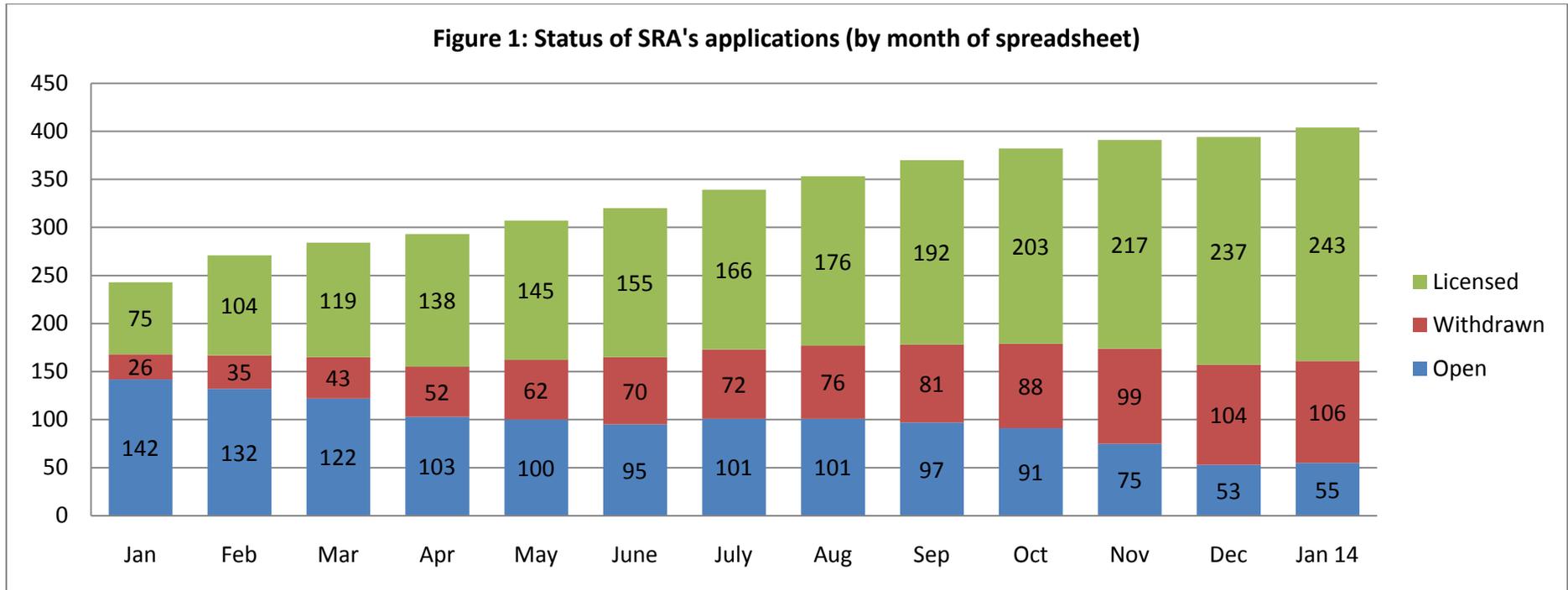


Figure 2: Frequency of licence granted by month

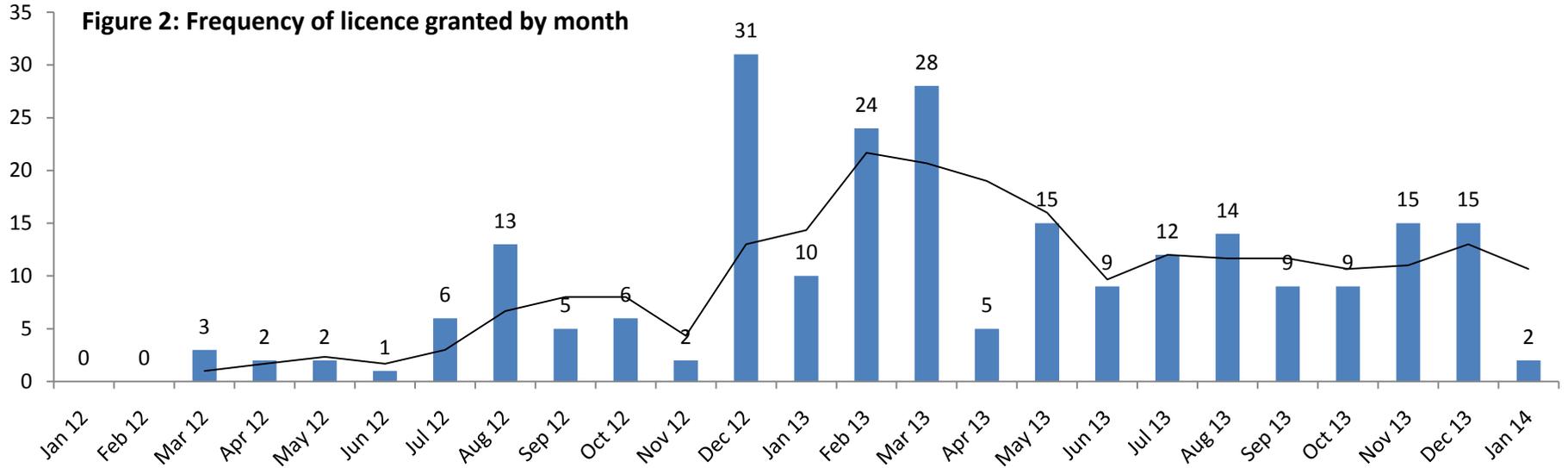


Figure 3: Time taken from application to licence granted (by month of spreadsheet)

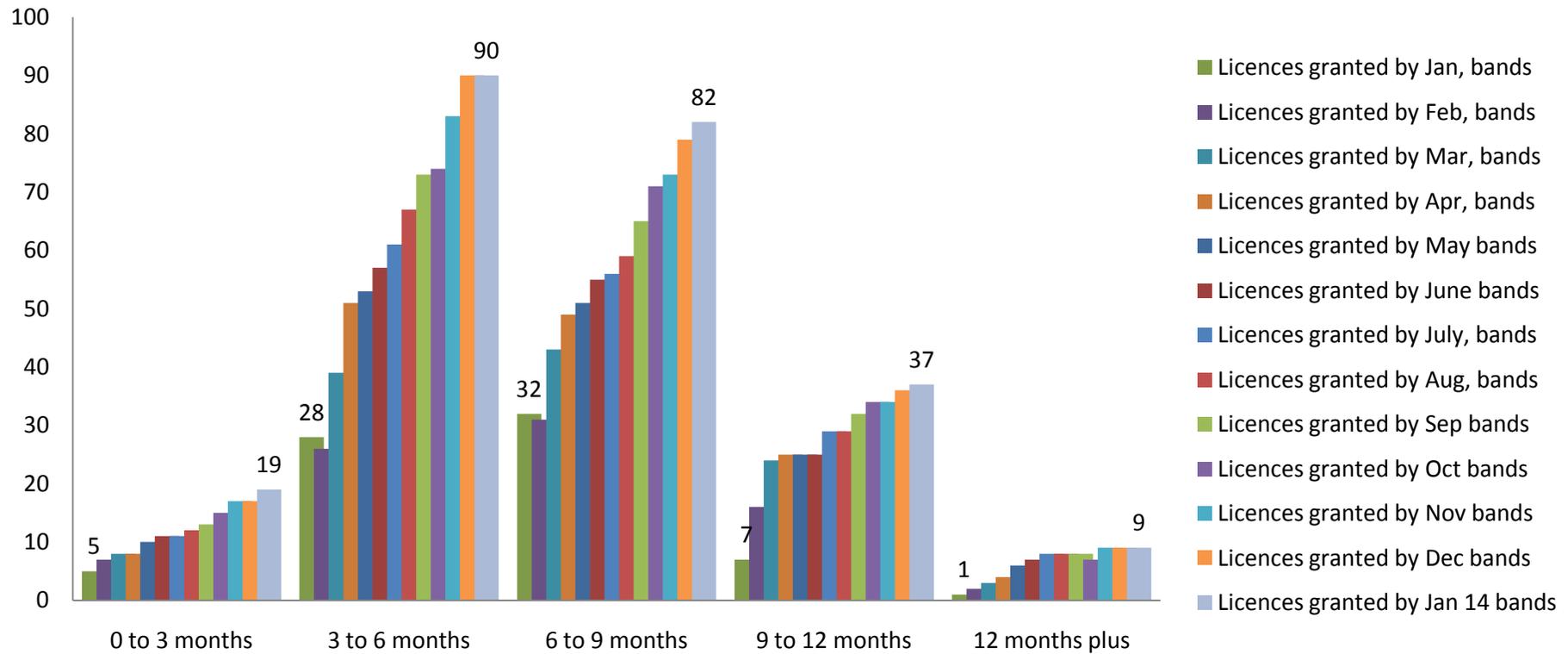
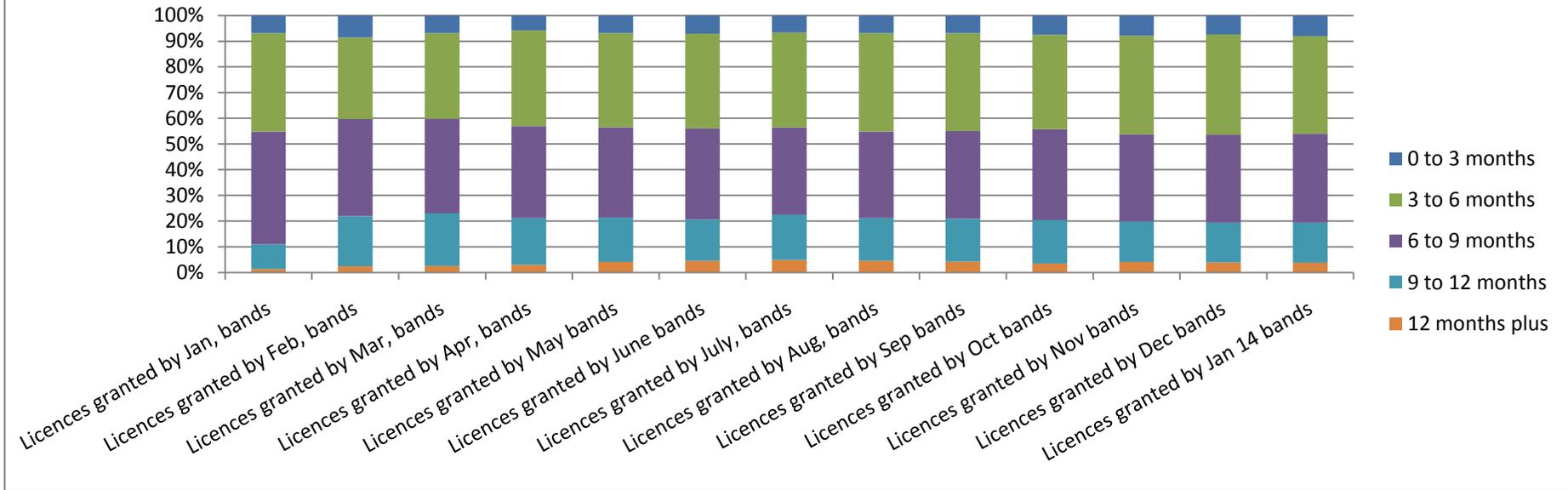


Figure 4: Licence decisions in percentages (by month of spreadsheet)



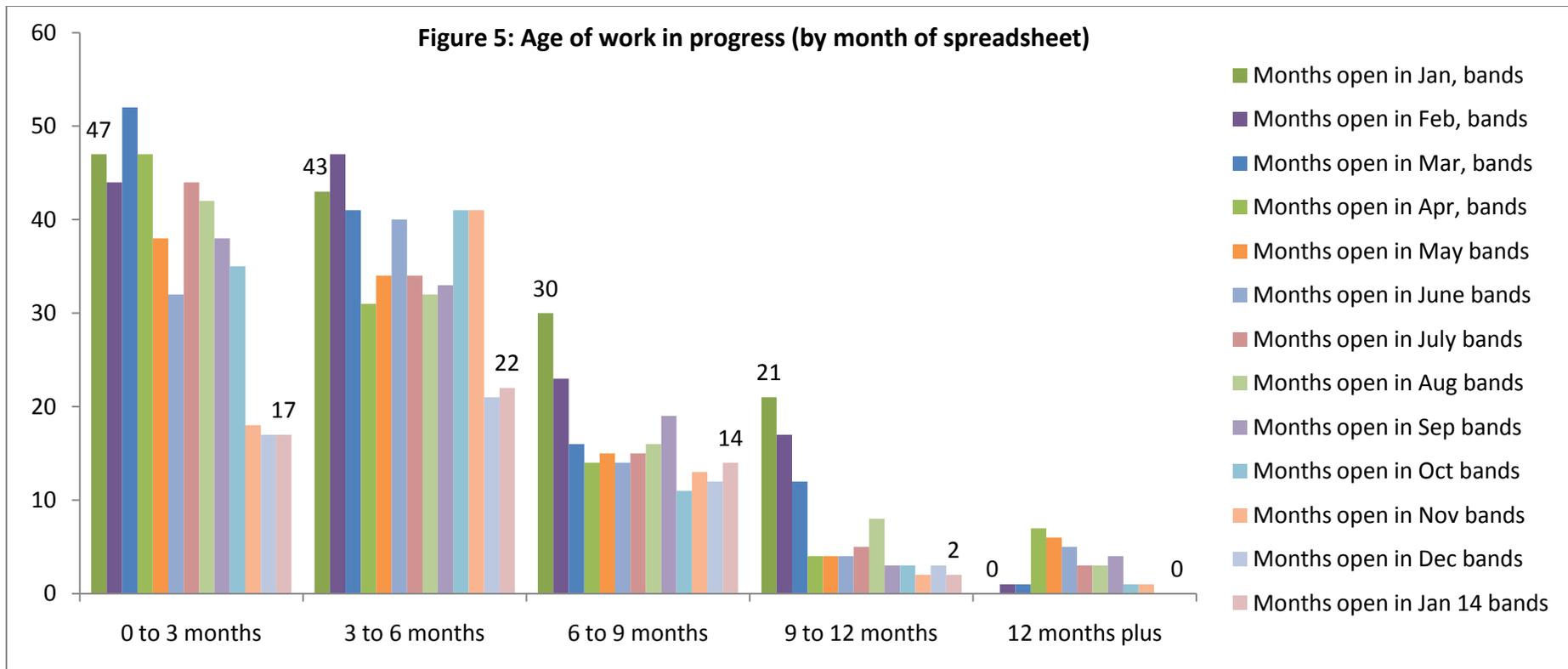


Figure 6: Age of work in progress in percentages (by month of spreadsheet)

