

# **GUIDANCE ON REFERRAL FEES, REFERRAL ARRANGEMENTS AND FEE SHARING TO APPROVED REGULATORS**

## **INTRODUCTION**

### **The provision of Guidance**

1. Section 162 of the 2007 Act allows the Board to give Guidance:
  - a. about the operation of the 2007 Act and any order made under it
  - b. about the operation of any rules made by the Board under the 2007 Act
  - c. about any matter relating to the Board's functions
  - d. for the purpose of meeting the Regulatory Objectives
  - e. about the content of licensing rules
  - f. about any other matters about which it appears to the Board to be desirable to give Guidance.
2. Guidance under s.162 may consist of such information and advice as the Board considers is appropriate. The Board will have regard to the extent to which an approved regulator has complied with this Guidance when exercising its functions.

## **BACKGROUND**

3. The LSB published a consultation document entitled Referral Fees, Referral Arrangements and Fee-sharing in September 2010. In May 2011 it published its decision document. This Guidance forms part of that decision document.

### **Application of the Guidance**

4. The Board considers that the information provided here gives sufficient clarity as to the outcomes to be delivered, whilst allowing an appropriate degree of discretion for approved regulators to decide how best they can be secured.

5. Section 162(5) of the 2007 Act says “when exercising its functions, the Board may have regard to the extent to which an approved regulator has complied with any Guidance issued under this section which is applicable to the approved regulator”.
6. The LSB will examine the extent to which an approved regulator has demonstrated that its regulatory arrangements deliver the outcomes set out in this Guidance. It will do this through the rule approval process for any individual rules relating to referral fees, referral arrangements and fee sharing; the scrutiny of more general codes or handbooks where they are submitted for approval and in its oversight of any other relevant regulatory functions.
7. The Guidance sets out the issues that approved regulators may wish to take into account in assessing how they are proposing to deliver the outcomes. There are a number of alternative ways in which these outcomes could be delivered and the Board would expect the approved regulator to have available evidence to support their choice of approach. This evidence would need to be compelling, reasonable and present the regulatory rationale.

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### **OUTCOMES**

8. This document provides Guidance for the delivery of the outcomes which have been identified by the LSB for approved regulators. The outcomes to be delivered are set out below:
  - a. regulators have in place arrangements that:
    - i. reduce the likelihood of detriment to consumers as a result of allowing referral fees, referral arrangements and fee sharing
    - ii. can justify any ban or restriction on referral fees, referral arrangements and fee sharing with reference to evidence, regulatory objectives and Better Regulation Principles.
  - b. consumers know when referral fees and/or referral arrangements are or may be in place in order to inform their choices.

### **JUSTIFYING REGULATORY ARRANGEMENTS**

9. Each approved regulator that has imposed, or wants to impose, a ban on referral fees, referral arrangements or fee sharing must be able to justify their approach. To justify an existing ban on referral fees (or the proposal for a ban), the Board would expect an approved regulator to establish evidentially the extent to which a ban or restriction is compatible with the Regulatory Objectives and is in accordance with the Better Regulation Principles and regulatory best practice. This assessment is likely to include, but need not be limited to, consideration of:
  - a. Why a ban is relevant to the particular market in question, demonstrating the approach taken to market segmentation by legal service provider e.g. large/small firms and type of consumer such as experienced or first-time user
  - b. What the risks associated with referral fees, referral arrangements and fee sharing are in particular market segments – as well as any evidence of those risks materialising in practice

- c. The costs and benefits of other less prescriptive measures to manage the risks identified
  - d. How referral fees impact or would impact on different groups of consumers in the specific markets
  - e. The extent to which this evidence supporting the decision has been published and made subject to external scrutiny
  - f. How the impact of the ban will be monitored and how an assessment will be made on its continued appropriateness.
10. The Board considers that such justification needs to be segmented by reference to the various activities, markets and consumers in which authorised persons, overseen by an individual approved regulator, operate. It considers that blanket bans imposed without this segmented analysis call for a particularly high standard of analytical justification.

## **DELIVERING INFORMATION TO CONSUMERS**

11. Approved regulators must be able to demonstrate that regulatory arrangements are in place to tell consumers about referral fees and arrangements. This is because the Board considers that such a requirement may help to inform consumer choice, which can in turn promote confidence in markets where referral fees and arrangements are in use. This demonstration is likely to include, but need not be limited to:
- a. How requirements to tell consumers about referral fees and arrangements are appropriate to:
    - i. different market segments – for example, conveyancing, probate
    - ii. different services – for example, general legal advice, litigation
    - iii. different types of consumers – for example, experienced, informed or repeat consumers, first time users of legal services
  - b. What information authorised persons are required to provide to consumers to tell them about the existence and extent of a referral fee. Typically this could include information such as price, the identity of recipient of the referral fee or arrangement and a reminder of the consumer's right to shop around

- c. Whether the timing of giving information to consumers should vary for different market segments, services and/or consumers
- d. Whether the types of information given to consumers should vary for different market segments, services and/or types of consumers
- e. At what point in the process of getting legal advice the approved regulator requires information to be disclosed so as to ensure that it assists consumers to make informed decisions about their choice of legal service provider
- f. Whether the timing of information disclosure should vary for different market segments/services/consumers
- g. Whether disclosure should highlight all exchanges as part of referral arrangements or just monetary exchanges and whether this varies for each of the segments
- h. Whether the form and medium of disclosure will be prescribed or whether legal services providers will be given guidelines about the type and form of information disclosed. Consideration should be given to whether this should vary for each of the segments outlined above. Evidence should be available to support the choices made by approved regulators.

## **DELIVERING INFORMATION TO THE MARKET**

12. Approved regulators must be able to demonstrate that their regulatory arrangements provide information to the market about referral fees and arrangements. This is because the wider market and other stakeholders should have confidence in the operation of referral fees and arrangements. The provision and publication of information will help to deliver this, not least by enabling disinterested research and improving competition. Approved regulators will need to have considered the case for providing information to the market, with particular regard to the Better Regulation Principles. The demonstration of this by approved regulators is likely to include but not be limited to:

- a. Consideration of who would be expected to use the information in a particular market and in what ways this would contribute towards meeting the Regulatory Objectives
- b. The extent to which referral contracts are in writing
- c. The extent to which publishing agreements might aid competition such as by addressing information asymmetry between referring agents/agencies and legal service provider/s
- d. The extent to which the level of concentration in a particular market segment may increase the risk of collusion
- e. The collection of information, including consideration of:
  - i. How referral contracts will be collected. Consideration should be given to the impact alternative methods of collection are likely to have on the accuracy of information provided
  - ii. The cost collection methods will impose on authorised persons and the regulator
  - iii. The frequency with which the information should be collected - for example, annually or when contracts are signed or updated
  - iv. When information should be collected - for example, with practising fee certificate information or at some other time
  - v. The form in which referral agreements or information about referral agreements should be published - for example, approved regulators may choose to publish full agreements, key facts, summaries, aggregations or reports about agreements
  - vi. Where information should be published - for example, on an approved regulator's website, the firm's website or by some other means. An approved regulator would also need to assess whether any option for publication would be likely to facilitate anti-competitive behaviour
  - vii. The ability of stakeholders to use the information

- f. What other risks are associated with the publication of information and how they might be tackled by the approved regulator – for example, closer monitor of market behaviour and pricing.

## **COMPLIANCE AND ENFORCEMENT**

13. Approved regulators must be able to demonstrate that their approach to compliance and enforcement of regulatory arrangements relating to referral fees and referral arrangements promote good regulatory practice. This demonstration is likely to include but not be limited to:
  - a. The type of information and data they collect about referral fees and arrangements, including consideration of the need to collect details of:
    - i. the amount that individuals and entities pay for referral of work (including an assessment of the value of work undertaken in place of a referral fee)
    - ii. the percentage of turnover made up from referral fees and arrangements
    - iii. the number of referral contracts that firms and individuals have
  - b. How they assess whether their regulatory arrangements are being delivered by authorised individuals and entities – for example, through collection of data, visits, surveys
  - c. the frequency with which they request information about referral fees and arrangements from those they regulate – for example, annually or more frequently
  - d. how they have established that the information they collect is sufficient to support their compliance and enforcement activities
  - e. how they address poor compliance with regulatory arrangements – for example, financial penalties, enhanced compliance activities, provision of additional monitoring information

- f. how they assess the way in which their regulated community works with other bodies and/or individuals who also have contact with consumers and are involved in provision or receipt of fees or referral arrangements – for example, the provision of information to consumers

## **CO-OPERATION**

- 14. Referral fees and arrangements are a feature of several markets. The overriding consideration for approved regulators must be their ability to demonstrate that this is not a barrier to consumer understanding of referral fees and arrangements and the role they play in the wider legal services market. Their demonstration of how they have achieved this is likely to include but not be limited to:
  - a. Whether working with other approved regulators, regulators from other markets, trade bodies and professional bodies could enhance their ability to ensure the regulation of referral fees and arrangements meet the shared Regulatory Objectives. For example, this may include consideration of common disclosure standards or information sharing.