



## **Legal Services Board – decision notice issued under Part 3 of Schedule 4 to the Legal Services Act 2007**

### **The Solicitors Regulation Authority (SRA) rule change application for approval to changes to the SRA’s regulatory arrangements concerning the referral by law firms of clients to third parties for financial services**

The Legal Services Board (LSB) has granted an application from the SRA who sought approval to changes to the SRA Code of Conduct 2011, the SRA Financial Services (Scope) Rules 2001, the SRA Financial Services (Conduct of Business) Rules 2001 and the SRA Handbook Glossary 2012.

This decision notice sets out the basis for the LSB granting the application and the decision taken, including a brief description of the changes.

#### **Introduction**

1. 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.
2. Paragraph 25 of Schedule 4 to the Act explains that the LSB may only refuse an application setting out a proposed change to the regulatory arrangements if it is satisfied that by granting the application one or more of the criteria specified in sub paragraph 25(3) (and listed in the footnote below<sup>1</sup>) will be met. For example, the LSB’s granting of the application to alter the regulatory arrangements must not be prejudicial to the regulatory objectives overall. Accordingly, 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.
3. As provided for by paragraphs 20(1) and 23(3) of Schedule 4 to the Act, the LSB has made rules<sup>2</sup> about how the application to alter the regulatory arrangements must be made including the contents of that application. The rules highlight the applicant’s obligations under section 28 of the Act to have regard to the Better Regulation Principles.

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<sup>1</sup> The Board may refuse the application 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 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.

<sup>2</sup> [Rules for Rule Change Applications – Version 2 \(November 2010\)](#)

The rules also require that the applicant provides information about the nature and effect of each proposed change and of appropriate consultation undertaken. Sub paragraph 25(3)(f) of Schedule 4 to the Act requires that each proposed alteration has been made or is likely to be made in accordance with the procedures (whether statutory or otherwise) which apply in relation to the making of the alteration. This therefore includes the LSB's rules.

4. The chronology for the LSB's handling of this application can be found towards the end of this decision notice.

### **Proposed alterations**

5. The proposed alterations are to outcome 6.3 and indicative behaviour 6.2 in Chapter 6 of the SRA Code of Conduct on *Your client and introductions to third parties*. This change was prompted by a reconsideration of the referral arrangements in the light of the Financial Services Authority (FSA) requirement that, after 31 December 2012, only advisers who consider types of investment products from all firms across the market will be able to describe themselves as "independent". It is not known at this stage what impact, if any, this will have on the availability of independent financial advice in the retail financial services market.
6. There are also consequential amendments to the SRA Financial Services (Scope) Rules 2001, the SRA Financial Services (Conduct of Business) Rules 2001 and the SRA Handbook Glossary arising from changes in terminology in the Financial Services Authority rules.

### **Decision**

7. Consistent with the development of its outcomes-focused Code of Conduct, the SRA has decided to remove its requirement that clients needing financial advice are referred to an independent intermediary. Outcome 6.3 of the Code of Conduct will be changed to "*clients* are in a position to make informed decisions about how to pursue the matter".
8. This outcome is supported by a revised indicative behaviour (IB(6.2)) "*any referral to a third party who can only offer products from one source is made only after the client has been informed of this limitation*".
9. In making its decision the LSB was mindful of the concerns expressed in the responses to the SRA consultation, including whether the change could impact on the independence of the law firm and the risk of an increase in negligence claims (against either firms or the SRA Compensation Fund) because of inappropriate referrals.
10. The SRA says in the Board paper which accompanied the application that its research shows no evidence to suggest that independence will be compromised and that the SRA will monitor the ways in which the legal profession interacts with financial advisers and responds to the SRA's removal of the original prescriptive outcome in respect of introductions. It has been noted that the revised outcome does not prevent solicitors

from referring clients to independent financial advisers and the new wording is consistent with Chapter 9 of the SRA Code on *Fee sharing and referrals*.

11. The SRA will assess whether the changes can be shown to have a causal link with increased numbers of negligence claims against law firms and increased numbers of claims on the Solicitors Compensation Fund because of inappropriate introductions. The LSB understands that the SRA will do this in a number of ways, including: through its regular communications with the FSA (and its successor Financial Conduct Authority) and Financial Ombudsman Service; review of the financial services press; and communications with trade representative bodies, as well as from the intelligence it gathers through its supervisory and risk initiatives.
12. The LSB takes assurance from the commitment by the SRA to review the impact of the changes.

### *Conclusion*

13. The LSB is satisfied that, having considered the SRA's application against the criteria in paragraph 25(3) of Schedule 4 to the Act, there is no reason to refuse this application; accordingly, the LSB grants this application.
14. Annex A to this decision notice contains the relevant amendments to the SRA Code of Conduct 2011, the SRA Financial Services (Scope) Rules 2001, the SRA Financial Services (Conduct of Business) Rules 2001 and the SRA Handbook Glossary 2012 to be implemented through the SRA Amendment to Regulatory Arrangements (Financial Services Rules) [2012].

### **Chronology**

- The LSB confirmed receipt of an application from the SRA on 10 December 2012.
- The 28 day initial decision period for considering the application ends on 6 January 2013.
- This Decision Notice is being issued to the SRA on 20 December 2012.
- This Decision Notice will be published on our website on 21 December 2012.

**Chris Kenny, Chief Executive**  
**Acting under delegated authority granted by the Board of the Legal Services Board**  
**20 December 2012**

## Annex A

### SRA Amendment to Regulatory Arrangements (Financial Services) Rules [2012]

#### Preamble

Rules dated [date of approval by the Legal Services Board] made by the Solicitors Regulation Authority Board under sections 31, 79 and 80 of the Solicitors Act 1974, sections 9 and 9A of the Administration of Justice Act 1985, paragraphs 2 and 3 of Schedule 14 to the Courts and Legal Services Act 1990, section 83 of, and Schedule 11 to, the Legal Services Act 2007 and section 332 of the Financial Services and Markets Act 2000, with the approval of the Legal Services Board under paragraph 19 of Schedule 4 to the Legal Services Act 2007.

#### Rule 1

The SRA Code of Conduct 2011 shall be amended as follows:

In outcome (6.3) the wording “if a *client* is likely to need advice on *investments*, such as life insurance with an investment element or pension policies, you refer them only to an *independent intermediary*” shall be deleted and replaced with the following:

" O(6.3) *clients* are in a position to make informed decisions about how to pursue their matter."

From indicative behaviour (6.2) delete the words “in respect of *regulated mortgage contracts*, *general insurance contracts* and *pure protection contracts*” and remove the comma after the word “source” so that the wording is as follows:

“IB (6.2) any referral to a third party that can only offer products from one source is made only after the *client* has been informed of this limitation”.

#### Rule 2

The SRA Financial Services (Scope) Rules 2001 shall be amended as follows:

- (a) in rule 5.1 replace "Packaged products" with "Retail investment products" and replace “*packaged product*” with “*retail investment product*”; and
- (b) in rule 5.3 replace “*packaged products*” with “*retail investment products*”.

#### Rule 3

The SRA Financial Services (Conduct of Business) Rules 2001 shall be amended as follows:

In rule 8.1 and note (iii) to rule 13.1 replace “*packaged product*” with “*retail investment product*”.

#### Rule 4

The SRA Handbook Glossary 2012 shall be amended as follows:

- (a) delete the definition of “**independent intermediary**” and replace with:

**“independent financial adviser**

means an adviser who provides unbiased and unrestricted advice based on a comprehensive and fair analysis of the relevant market and discloses this in writing to the *client*.”;

(b) delete the definition of "**packaged product**"; and

(c) after the definition of "**reserved work**" insert:

**"retail investment product**

has the meaning given in the Financial Services Authority Handbook.”

**Rule 5**

These amendment rules shall come into force on 1 January 2013 or the date of approval by the Legal Services Board, whichever is the later.