



**A RESPONSE BY ILEX PROFESSIONAL  
STANDARDS LIMITED**

**REFERRAL FEES, REFERRAL ARRANGEMENTS  
AND FEE SHARING**

**CONSULTATION BY THE LEGAL SERVICES  
BOARD ON THE REGULATORY TREATMENT OF  
REFERRAL FEES, REFERRAL ARRANGEMENTS  
AND FEE SHARING**

**DATE: 20 DECEMBER 2010**

## **ILEX Professional Standards**

This response represents the views of ILEX Professional Standards (IPS), the regulatory body for Legal Executives. Legal Executives are members of the Institute of Legal Executives (ILEX). ILEX is the professional body representing 22,000 qualified and trainee Legal Executives and is an Approved Regulator under the Legal Services Act 2007 (LSA 07).

ILEX and IPS are committed to regulating Legal Executive businesses and businesses in which Legal Executives are partners and directors by 2012. IPS will establish regulatory arrangements that not only comply with the requirements of the Act and with any regulations made by the Legal Services Board (LSB) under the Act but that also provide public protection. The consultation paper is wide ranging and IPS does not propose to respond in detail to all of the issues, but hopes the general observations below may be of value.

Answers are set out below, to the questions in the consultations, where IPS is able to offer a view.

## **Conclusions – Personal Injury and Conveyancing**

### **1. Do you agree with our analysis of the operation of referral fees and arrangements?**

The LSB collected a significant amount of research to ensure that its analysis was founded upon a wide understanding of consumer views of referral fees and an accurate economic analysis of their impact upon the market. The Consumer Panel identified appropriate key topics against which to test the impact of referral fees. These were quality, costs, competition, independence, choice and access to justice.

It was fair to conclude that the existence of referral fees or arrangements has not affected the quality of service received by consumers as evidence indicated that levels of satisfaction with outcomes and service for consumers using introducers is high (over 90%). It is understood that the improvement in standards in some cases is due to investment in IT and case management systems. This finding was compared against evidence of dissatisfaction among clients using 'factory firms'. However, in those cases the case management process did not seem to have an impact on the outcome of legal advice.

The consultation highlights that the evidence showed that referral fees have made a contribution to keeping costs down. This was the case both in conveyancing, in which conveyancing fees charged were found to be lower among firms paying referral fees and in personal injury in which the Advisory Committee on Civil Costs had concluded that claims management companies do not make excessive profits.

It was just to say that referral fees/arrangements aid access to justice in the area of personal injury, as introducers increased the awareness of the right of those who have suffered accidents to claim compensation and facilitated the claims process. This is seen by some as fuel to the so called 'compensation culture'. However, the LSB identifies several other factors which may have influenced the rise in compensation claims. The Consumer Panel has viewed claims management companies as providing a marketing and support role and that for those reasons referral fees and arrangements have widened access to justice.

According to the consultation there is no evidence that lawyers' ability to act with independence is affected nor is there evidence that consumer choice is undermined by referral fees and arrangements. However, the LSB has concluded that they are concerned about the unequal power relationship between lawyers and introducers and that the current disclosure mechanisms do not adequately protect consumers.

It is clear that unequal power is not the same as influence or the undermining of independence. The Consumer Panel identified that the key factor that would create the opportunity for introducers to exert improper influence was not evidenced as the Panel did not find that law firms were over-reliant on work coming from a single introducer. Furthermore in relation to independence, the SRA uncovered that there were very few breaches of its independence rules.

IPS considers it essential for any changes in this area to tackle the root causes rather than the symptoms. Despite the lack of evidence of symptoms, (e.g. improper influence and the undermining of independence) they would stem from the root cause: the unequal power relationship. It is that area which must be tackled.

Even so, the consultation does not appear to provide a compelling argument as to why the evidence has led to concerns about the unequal power relationship between lawyers and introducers. The potential for an unequal power relationship must always exist. Being transparent about the relationship will not make it any less unequal; and as established an unequal relationship does not mean there is improper influence or that independence is undermined. For this reason a high level of transparency between providers and their consumer may have little effect. The level of transparency between

provide and Approved Regulator is however more important, as the Approved Regulator would be more equipped than the consumer to assess the relationship between introducer and lawyer.

**2. Do you have additional evidence about the operation of referral fees and arrangements that should be considered by the LSB?**

IPS does not have any such evidence.

**Conclusions – Criminal Advocacy**

**3. Do you agree with our analysis of the operation of referral fees or fee sharing arrangements in criminal advocacy?**

IPS agrees that, because there is no effective measure allowing the LSB to evidence the quality of criminal advocacy, there is no systematic evidence that fee sharing is reducing quality in criminal advocacy. The LSB has also concluded that there is no evidence that lawyers are consistently putting financial interests ahead of their duties to their clients.

The evidence, although not qualitative data, has however, led to concerns that a focus on profitability has caused in-house advocates and external solicitor advocates to be appointed for cases beyond their competency; and that this can adversely impact the defence of the accused. The absence of quality measures has made it difficult to assess the extent of detriment from the use of inexperienced advocates. The LSB should reassess this area once the Quality Assurance of Advocacy scheme is implemented.

IPS agrees with the LSB's conclusion that the interests of consumers are best protected where competitive markets are able to flourish. Therefore we agree that providing consumers with important information about the amount of the referral fee or fee sharing arrangements will improve the competitiveness of the market. However, the level of transparency needs to be considered.

The evidence shows that the existence of a referral does of itself not mean there is improper influence or independence is undermined. Providing consumers with additional information including the size of the fee, may allow the consumer to judge the relative importance of the referral arrangement. The consumer will be able to consider only the relative importance in their cases alone because they know the details and background of their case. The LSB has recognised that consumers will more likely be concerned about the overall costs of the service. As a result there appears to be no compelling reason why full agreements should be published.

An overall picture can be gained by Approved Regulators collecting agreements. Approved Regulators will be able to assess whether the relationship between lawyer and introducer has affected independence, created influence and had an affect on the client's freedom of choice. This is because an unequal relationship, which affects the interest of consumers as a whole, will usually develop over a period of time through a number of cases. This has been identified by the Consumer Panel which placed, as a key factor to determining independence, whether law firms were over-reliant on work coming from a single introducer. To assess market trends, transparency with the regulator will be of more benefit than transparency (providing full agreements to clients) on a case by case basis with the consumer.

- 4. Do you have additional evidence about the operation of referral fees or fee sharing arrangements that should be considered by the LSB?**
- 5. In particular, do you have evidence about the impact of referral fees or fee sharing arrangements on the quality of criminal advocacy?**

IPS does not have any such evidence.

### **Recommendations for improving transparency and disclosure**

- 6. Will the proposals assist in improving disclosure to consumers?**

The proposals, if adhered to, would assist in improving disclosure to consumers. However, those proposals that are directly applicable to lawyers may have little impact given that those categories of lawyers who are able to enter into financial arrangements are obliged to follow rules, currently laid out by their regulatory body which are not so different.

The proposals recommend that the legal service provider should provide the client with key information about the agreement, in particular, whom the referral fee is paid to and for what services, the value of the referral fee and the consumer's right to shop around for alternative legal service providers. Lawyers who are able to enter into financial arrangements are currently required to ensure the arrangement is in writing and that the client has knowledge of the existence and the amount of the financial arrangement. Furthermore the LSB recommends that the lawyer provides the consumer with this key information as soon as feasible at the start of the relationship.

In contrast it would appear that providing the client with this information before any contract for services is agreed with the lawyer would be in the consumer's interest. ILEX Practice Management Rules, which will apply to practitioners with independent practice rights, specify that ILEX Practitioners fully disclose any financial arrangement in writing to their proposed client prior to accepting instructions. This requirement would also coincide with the time at which the consumer is entitled to be informed that they have a right to shop around for alternative legal service providers.

In relation to the client's freedom of choice, it is unclear when the client's right to shop around ends. The consultation states that according to UK case law the client has the freedom to choose another solicitor before the commencement of any inquiry or proceedings. A definition of 'inquiry' is needed to assist lawyers in this area. The case of *Sawar v Alam* [2001] cited in the consultation paper provides that the obligation to permit the client (in this case 'the insured') to select a lawyer of their choice is triggered when efforts to settle a claim by negotiation have failed and legal proceedings have to be initiated. Clear guidance is needed because an inquiry could be made before legal proceedings have to be or have been initiated. Furthermore, if consumers must be informed before an inquiry is made (we assume this means making an inquiry with lawyers to take on the case); the introducer would be the person in the best position to inform the consumer of their freedom of choice.

The proposals in relation to the action Approved Regulators should take will assist in improving disclosure to consumers. Publication of agreements would be the ultimate disclosure. But thought needs to be given as to whether the consumer will benefit from sight of the entire agreement. The agreement essentially is a commercial contract between the introducer and the lawyer and is not drafted for a consumer reader. Reading the entire agreement will not benefit the consumer if it serves only to cause confusion. Publication could be limited to key information that lawyers are required to provide the client. This would ensure, that if lawyers failed in their duty to provide the client with that information, the information would be available to them nevertheless.

The LSB has stated that the referral fee/arrangement agreement is evidence of whether or not the parties have the intention of acting in the best interest of their clients. Based on the agreement it would be difficult to conclude that the level of services received by a solicitor was directly reflective of the amount of the referral fee. To be able to assess whether a referral fee has affected the quality and cost of legal service, competition within the market, the consumer's freedom of choice, the lawyer's independence and access to justice, a criterion against which to assess the agreement would be needed. An individual agreement may not provide enough evidence to assess the impact on the key areas above. Therefore the individual agreement

constitutes only some of the evidence of whether or not the parties have the intention of acting in the best interest of their clients. It would be of no value for full agreements to be put in the public domain without some kind of criterion against which the agreement and the relationship between the lawyer and introducer could be measured. Criteria will also help consumers assess their own agreements because if the agreement is complex in nature and key factors are not highlighted, consumers may resort to assessing the agreement solely on the amount of the referral fee or a worst case scenario, comparing the agreement with other published agreements without knowledge of the details and background of the case.

**7. Are there other options for disclosure that Approved Regulators should consider?**

IPS has not been able formulate any additional options for disclosure, but we would emphasise that criteria against which agreements and relationships are assessed are crucial.

**8. What are the issues relating to the disclosure of referral contracts by firms to Approved Regulators and their publication by Approved Regulators?**

In the consultation it is proposed that Approved Regulators should collect agreements between introducers and lawyers. However, there may be issues in relation to capacity and resources to administer collection and publication. Furthermore, it is unclear what the LSB wants Approved Regulators to do with the agreements. If Approved Regulators merely collect agreements and do nothing with them, collection serves no purpose. On the other hand for Approved Regulators to amend the agreements would be to interfere in market forces.

Publication of the full agreement may be excessive and in actual fact may not benefit the consumer. Publication may also produce confidentiality issues, in relation to commercially sensitive information.

There is an issue which requires clarification. The majority of ILEX members work in law firms and it is unclear whether individual lawyers or the firm itself would be responsible for submitting copies of agreements to Approved Regulators. In addition, if the individual lawyer is responsible, would the agreement be submitted to the individual's regulator or the regulator that regulates the firm?

## **9. How should these issues be addressed?**

Publication should be limited to key information which the lawyer would be required to provide the client. Commercially sensitive information should be withheld. This type of decision could be made against set criteria and could take place on a case by case basis.

## **Recommendations for delivering active regulation**

### **10. Will the proposals assist in improving compliance and enforcement of referral fee rules?**

As there is evidence that the current disclosure mechanisms do not work well, with evidence of wide non-compliance with them, change is needed to ensure that information about referral arrangements is disclosed to consumers. It is important to recognise the possible impact of the proposals. Publishing these commercial arrangements could impact on businesses, reduce competition, drive down the number of referral arrangements and increase costs for consumers.

Active regulation should assist in securing control and reinforcing ethical behaviour. However, delivering active regulation as proposed in the consultation will likely result in increased costs for regulators. Regulation measures should be proportionate to the potential risks. Publication of referral arrangements is an area where proportionality needs to be considered. Applying a test of proportionality may reduce costs.

The LSB identified that the introduction of ABS, in less than a year's time, will open up the legal services market and challenge disclosure requirements and rules. This leads us to raise the question whether changes to disclosure requirements and rules should take place after ABS has been introduced, when the profession is better informed of the impact of ABS. Referral fees may become redundant in the near future, so it may be wise that substantial resources are not currently invested in the area.

### **11. What measures should be the subject of key performance indicators or targets?**

The way each Approved Regulator approaches active regulation of referral fees and arrangements should be different because the impact is different on different lawyers within the profession. A one-size-fits-all approach will not work. Key performance indicators should be drawn up by the Approved Regulator itself. Approved Regulators should also set their own targets which are reviewed periodically based on actual outcomes and experience over time.



## **12. What metric should be used to measure consumer confidence?**

Consumer confidence may be difficult to measure; furthermore, mechanisms used may not provide definitive results. One way to measure the lack of consumer confidence may be the number of complaints made in this area. A survey may be another tool. A survey will likely produce more definitive results because the questions within the survey can be carefully selected in order to ascertain relevant information from consumers.

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