



## **Legal Services Board – Decision Notice issued under Part 1 of Schedule 10 to the Legal Services Act 2007**

The Law Society made an application under the Legal Services Act 2007 (“the Act”) for the Legal Services Board (“The Board”) to recommend that an order be made by the Lord Chancellor designating the Law Society as a Licensing Authority for its existing reserved legal activities (exercise of a right of audience, conduct of litigation, reserved instrument activities, probate and the administration of oaths).

**The LSB has decided to make a recommendation to the Lord Chancellor that an order be made designating the Law Society as a Licensing Authority for the reserved legal activities of exercise of a right of audience, conduct of litigation, reserved instrument activities, probate and the administration of oaths.<sup>1</sup>**

**In making its recommendation to the Lord Chancellor, the LSB will also recommend that the proposed licensing rules are at the same time treated as having been approved by the LSB. This includes the entire Solicitors Regulation Authority (“SRA”) Handbook.<sup>2</sup>**

In this document, references to the “Law Society” are to the applicant seeking designation as a licensing authority, and references to the “SRA” are to the body currently performing an approved regulator’s regulatory functions, and proposing to perform a licensing authority’s regulatory functions, on behalf of the Law Society.

This Notice sets out the basis for the LSB decision.

### **Authority for the decision**

1. **Annex 1** sets out the authority under which the LSB has made this decision.

### **Background**

2. The Law Society is already an approved regulator under the Act. The regulatory functions of the Law Society are delegated to the SRA who prepared both the application and the licensing rules (which are contained in the SRA Handbook). The Law Society approved the application and the proposed licensing rules at its meeting on 23 March 2011 and submitted the application on 25 March 2011.

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<sup>1</sup> The application included in the list of reserved legal activities immigration advice and services but as this is not a reserved legal activity it is not referred to in the designation recommendation.

<sup>2</sup> This Decision Notice should be read alongside that issued under Schedule 4 Part 3 on the SRA’s application to change its regulatory arrangements published here [http://www.legalservicesboard.org.uk/what\\_we\\_do/regulation/applications.htm](http://www.legalservicesboard.org.uk/what_we_do/regulation/applications.htm)

3. In order to achieve a “level playing field” between the community of firms and individuals (recognised bodies and solicitors) and licensed bodies (ABS) regulated by the SRA, the SRA has undertaken a wide ranging review of its overall approach to regulation and its organisation. This has resulted in the ‘Outcomes Focused Regulation (OFR)’ programme of work. In preparation for making its licensing authority application, the SRA has also reviewed the entirety of its regulatory framework which has necessitated revisions to the regulatory arrangements contained in the SRA Handbook. The revised regulatory arrangements are subject to LSB approval as a change for the existing regulated community (under Schedule 4, Part 3 of the Act) as well as forming the licensing rules with which SRA licensed bodies will have to comply. The decision with regard to the Schedule 4, Part 3 application is the subject of a separate Decision Notice.

### **Analysis of the application**

4. The LSB performed an analysis of the application in line with the requirements specified in Schedule 10 to the Act and in line with LSB’s rules and guidance made under that Schedule.<sup>3</sup>
5. Before determining an application and making a recommendation to the Lord Chancellor, the Board must be satisfied on the matters set out in Schedule 10, paragraph 11(2) and 11(3). These matters are
- That the proposed licensing rules comply with the requirements of section 83(5) of the Act<sup>4</sup>
  - That if an order were to be made designating the Law Society as a Licensing Authority, there would be a body with the power to hear and determine appeals
  - That if an order were to be made designating the SRA as a Licensing Authority, the SRA would be competent and have sufficient resources to perform the role of Licensing Authority in relation to the activity at the time the order takes effect
  - That the exercise of regulatory functions is not prejudiced by representative functions
  - That decisions relating to the exercise of the regulatory functions are taken (as far as possible) independently from decisions relating to the exercise or representative functions
6. In considering the detailed analysis against these criteria, the following issues of significance were raised.

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<sup>3</sup> [http://www.legalservicesboard.org.uk/what\\_we\\_do/regulation/pdf/Designating\\_LA\\_rules.pdf](http://www.legalservicesboard.org.uk/what_we_do/regulation/pdf/Designating_LA_rules.pdf)  
[http://www.legalservicesboard.org.uk/what\\_we\\_do/regulation/pdf/abs\\_guidance\\_on\\_licensing\\_rules\\_guidance.pdf](http://www.legalservicesboard.org.uk/what_we_do/regulation/pdf/abs_guidance_on_licensing_rules_guidance.pdf)

<sup>4</sup> Section 83(5) Licensing rules of a licensing authority must contain appropriate qualification regulations for Licensable Bodies; provision for how the Licensing Authority, when considering the regulatory objectives in connection with an application for a licence, will take account of the objective of improving access to justice; contain appropriate arrangements (including conduct rules, discipline rules and practice rules) under which the Licensing Authority will be able to regulate the conduct of bodies licensed by it and their managers and employees; contain appropriate indemnification arrangements; contain appropriate compensation arrangements; provision required by sections 52 and 54 regarding the resolution of regulatory conflict; provision required by sections 112 and 145 in relation to complaints handling (including compliance with our signposting requirement); any other provisions required to be contained in the licensing rules.

*Capacity and capability of SRA as a Licensing Authority*

7. Schedule 10, paragraph 11(2)(d) requires that, in making a recommendation to the Lord Chancellor, the Board must be satisfied that a prospective licensing authority will be competent and have sufficient resources to perform the role of licensing authority at the time the order takes effect. The Board is satisfied that the SRA will have in place, at the point of designation, the processes, systems and people that it needs to be a competent licensing authority at that time.
8. In reaching this view the Board recognises that the process for designation of a licensing authority means that the Law Society has had to submit its application before the SRA has fully implemented all of its practices and processes.
9. The SRA has confirmed that it is on track to launch the online ABS application form in August 2011. Should this not be achieved, based on its planning assumptions about the number of applications, the SRA will be able to operate a paper based application process. We are therefore confident that the SRA will have the ability to receive and process applications at the point of designation.
10. The Act and the LSB's rules prescribe certain criteria that a licensing authority must consider when assessing applications from potential licensed bodies. These are contained in the SRA's licensing rules.
11. Although much of the authorisation process will be automated, a degree of judgement will be required. The SRA Board has approved a proposal under which a member of the Senior Management Team (SMT) will approve all applications for ABS for at least the first six months. The SRA is taking this approach to ensure robustness and consistency in decision making. In addition, the SRA has assured us that all decisions will be reviewed for consistency and to inform its future approach.
12. The experience of the decisions made by SMT in the first six months of approving applications will inform the roll-out and systemisation of decision making by SRA staff once the decision making authority is delegated from SMT. Once finalised, any decision making criteria beyond those approved through the rules covered by this document will require LSB approval (as it will form a regulatory arrangement requiring approval under Schedule 4, Part 3).
13. In preparation for the assumption of decision-making responsibility, all decision makers will go through scenario-based training covering competition and human rights law as well as law on public authority decision-making. All staff will be assessed following completion of the training.
14. The Board considers that the approach the SRA is taking to the first applications is acceptable but acknowledges that there is some risk in terms of over reliance on key people, in particular should there be higher numbers of applications than expected. The SRA are alert to this risk and have in place succession plans and retention strategies to mitigate this. We note that the SRA will be considering whether it has the appropriate flexibility within its

reward strategy to attract and retain key people. The Board will keep itself updated on this issue.

15. Other risks that have been considered include delivery of the remainder of the transformation programme (including implementation of the IT infrastructure to support the delivery of the OFR Programme), embedding the new culture throughout the organisation and recruiting and retaining the right staff at the right levels. The SRA has identified these areas as key risks and have in place appropriate mitigation plans and actions, which the Board has reviewed.
16. The SRA proposes to take a risk based approach to supervision for all those it regulates. This will enable resources to be targeted on the areas presenting most risk and for the SRA to provide a proportionate response. We are satisfied that the SRA has in place appropriate arrangements and resources to apply its new supervisory approach to ABS.
17. The LSB has concluded that we have sufficient information and assurance from the SRA and its Board to allow us to conclude that the SRA will be a competent licensing authority. In the period leading up to designation it will be important that the SRA Board closely monitors all continuing workstreams to ensure that progress is maintained. The SRA has agreed to provide regular reports to the Board in its capacity as oversight regulator.
18. As highlighted in the Consumer Panel's advice, evaluation will be an essential part of making OFR a success in the medium-term<sup>5</sup>. The Board and the SRA have agreed that a suite of management information will be provided post designation. The details of this will be developed by the end of June but will include both quantitative and qualitative data. A formal review will take place two years into the new regime, by which time the SRA will have experience of a full year's reporting cycle.

#### *Separate Business Rule*

19. The Board recognises that this is not a new rule but has considered it as there is a risk that it will have an adverse impact on ABS. It was devised as a way of preventing solicitors from separating non-reserved activities, from their regulated reserved activities, as a means of avoiding regulatory obligations and the attendant costs. However, in the ABS environment, the Board expressed concern that it may have exclusionary side effects on legitimate business structures that have the potential to bring significant consumer benefits through diverse delivery methods, new investment, and new ways of running firms with better links to clients through association with other services. In addition, the basis on which turnover based fees are calculated may pose a barrier to entry through the disproportionately high cost of regulation.
20. The SRA view is that the Separate Business Rule is necessary to mitigate the following risks:

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[http://www.legalservicesboard.org.uk/what\\_we\\_do/regulation/pdf/20110404\\_lscp\\_advice\\_on\\_sra\\_la\\_app.pdf](http://www.legalservicesboard.org.uk/what_we_do/regulation/pdf/20110404_lscp_advice_on_sra_la_app.pdf)

- that statutory protections attached to the provision of legal services will be lost if businesses sever part of their work into an unregulated firm to avoid regulation. By requiring all SRA regulated activities to be provided from the same entity, consumer protections (such as indemnity insurance, access to compensation fund, complaints) will apply to all activities and not just the reserved legal activities; and
  - that an unregulated provider will not be able to guarantee equivalent levels of consumer protection and that this would not be evident to consumers as the entity would be under no obligation to disclose the fact.
21. The Board remains concerned about the potential exclusionary effect of the SRA's approach and consider that conditions attached through the licensing regime would be a more proportionate way to address the risks highlighted by the SRA.
22. There is also a risk that the rule has the potential to achieve what it seeks to prevent: by driving legal services providers away from the provision of reserved legal activities, in order to avoid regulation altogether. In the ABS context in particular, the rule may also provide a barrier to entry for certain business models.
23. The Board has focused on minimising the risk that it is used in a way that has an exclusionary effect by seeking assurance from the SRA on its approach to the use of waivers where unintended or unjustifiable restrictions are created.
24. SRA's guide to authorisation for applicants will make clear its willingness to consider waiver applications generally, and particularly in relation to the Separate Business Rule where potential applicants consider the rule might restrict their chosen business model and the SRA can be satisfied that there is a low risk to consumers in allowing the waiver. The Board considers that this action will mitigate the risk that the rule has an exclusionary effect.
25. The Board is considering a broader review of the continuing relevance of the rule and its practical application in the light of experience as one element of its work on the scope of regulation.

#### *Ownership requirements for ABS*

26. Ownership requirements present one of the main changes and biggest challenges in the new regime and the Board needs to be satisfied that the SRA has appropriate arrangements to apply the ownership tests properly.
27. Schedule 13 of the Act sets out various tests to establish whether a person holds a material interest (i.e. 10% or more) in an ABS. These tests can extend to associates (which includes a wide range of people from a spouse/civil partner and children/stepchildren to employees and those acting in concert with them in terms of voting arrangements). So in practice, individuals connected by association may combine to be a material interest holder.
28. LSB guidance on licensing rules suggests that Licensing Authorities should apply a 3% *de minimis* in order to make the associate test workable in practice, i.e. checks do not need to be made for associates with a holding of less than 3%.<sup>6</sup> This issue applies to initial authorisation but also to the ongoing notification requirements under Schedule 13.

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<sup>6</sup> The 3% was based on listing authority rules and the approach taken by the Gambling Commission.

29. Although this approach is not spelled out in the licensing rules, the SRA has confirmed that it plans to adopt this as its general operating model, both for reasons of general proportionality and to ensure that the framework does not inadvertently restrict listed companies or those that are considering IPOs from applying for a licence. While the SRA considers that the rules must provide the ability for all associates to be checked, no matter how small their holding if risks make this appropriate, its working practice will be to make a judgement as to whom the ownership tests will apply and how the ongoing notification requirements will operate.
30. This has provided assurance to the Board that the arrangements are workable in practice for a wide range of organisational models. In particular, the Board sought and received explicit assurance from the SRA that it is open to applications from listed companies and those considering IPOs
31. The Board has also been concerned to ensure that this approach is appropriately communicated to ensure that there is no potential for the rules to put off potential applicants or their advisors, particularly in circumstances where they do not wish to enter into pre-application discussions with the SRA. SRA has confirmed that the guide to licensing authority applicants will be explicit that the SRA will welcome applications from listed companies and those considering IPOs. They will also review their approach if in practice their application process deters applicants.

## **Decisions**

32. Paragraphs 11(2) and 11(3) of Schedule 10 to the Act set out the matters on which the Board must be satisfied when granting an application for designation as a Licensing Authority.
33. The Board has considered the applications and satisfied itself that the issues raised have been satisfactorily addressed. It is satisfied that the criteria for granting a Licensing Authority designation application have been met.
34. Therefore the Board decided to
  - grant the application under Paragraph 12(1) of Part 1 of Schedule 10 to the Act;
  - recommend to the Lord Chancellor that the Law Society be designated as a Licensing Authority for the reserved legal activities of exercise of a right of audience, conduct of litigation, reserved instrument activities, probate activities and the administration of oaths under Paragraph 14(2) of Part 1 of Schedule 10 to the Act; and
  - include in the recommendation to the Lord Chancellor, the recommendation that the licensing rules be treated as approved for use by the Licensing Authority when the Lord Chancellor exercises his authority under Paragraph 16(1) of part 1 of Schedule 10 to the Act.
35. This document constitutes the Decision Notice which is being provided to the applicant under Paragraph 12(3) and is being published under Paragraph 12(12) (5) of Part 1 of Schedule 10 to the Act.

### **Actions**

- SRA and LSB to agree management information (both quantitative and qualitative) and a programme of reviews covering the period until designation and first two years post designation. To be agreed by 30 June 2011

### **Chronology**

- The LSB confirmed receipt of an application from the Law Society on 25 March 2011
- The Decision Period started on 25 March 2011 and ended on 13 June 2011
- The application was published on the LSB website on 30 March 2011
- The advice from the Mandatory Consultees and Law Society and SRA responses were published on the LSB website on 6 June 2011
- This Decision Notice is being published on our website on 17 June 2011.

**Legal Services Board**  
**17 June 2011**

**Annex 1: Authority for the decision**

1. Paragraph 1(2) of Part 1 of Schedule 10 to the Act enables any body to make an application requesting that the LSB recommends that an order be made by the Lord Chancellor to designate that body as a Licensing Authority in respect of identified reserved legal activities. Paragraph 1(3) of Schedule 10 provides that a body may only make such an application if it is an existing approved regulator in relation to the activity or it has made an application under Part 2 of Schedule 4 (designation of approved regulators) for the Board to recommend that an order be made by the Lord Chancellor designating the body as an approved regulator in relation to the activity.<sup>7</sup>
2. Part 1 of Schedule 10 also documents the processes, participants and criteria that will be applied to any such application that is made. These provisions include duties being imposed upon the LSB to make rules at Paragraph 1(4) for the form and manner of the application, 1(5) for the amount of the prescribed (application) fee, 2(2) for procedures and criteria for considering whether to accept an application for consideration, and 9(3) about considering oral and written representations made to the LSB as part of the process of consideration
3. Paragraph 11(1) of Part 1 of Schedule 10 to the Act, also requires the LSB to make rules about how it will determine if it should recommend to the Lord Chancellor that an application for designation by a body to become a Licensing Authority in relation to identified reserved legal activities should be made. These Rules for Licensing Authority Designation Applications came into effect on 1 January 2010<sup>8</sup>.
4. The LSB may only grant an application in relation to a particular reserved legal activity if it is satisfied in relation to the requirements under Paragraphs 11(2)<sup>9</sup> and 11(3)<sup>10</sup> of Part 1 of Schedule 10. The Rules for Licensing Authority Designation Applications provide the

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<sup>7</sup> The term “approved regulator” is defined in section 20 of the Act and a list of the Approved Regulators and the reserved legal activities for which they are approved is contained in Schedule 4 Part 1 of the Act. The term “reserved legal activities” is defined at Section 12 of the act and a list of the reserved legal activities and a definition of what is comprised within each of them is contained in Schedule 2 of the Act. Both Schedules will be amended from time to time in accordance with activities conducted in accordance with provisions of the Act.

<sup>8</sup> The Rules for Licensing Authority Designation Applications can be found on the LSB website [http://www.legalservicesboard.org.uk/what\\_we\\_do/regulation/pdf/Designating\\_LA\\_rules.pdf](http://www.legalservicesboard.org.uk/what_we_do/regulation/pdf/Designating_LA_rules.pdf)

<sup>9</sup> Paragraphs 11(2)(a) to (d) provide that the LSB may only grant an application if satisfied that the applicant’s proposed licensing rules in relation to the activity comply with the requirements of section 83; that if an order to be made under paragraph 15 designating the body in relation to the activity there would be a body with power to hear and determine appeals; that if an order were to be made under paragraph 15 designating the body in relation to that activity, the applicant would have appropriate internal governance arrangements in place at the time the order takes effect; that if an order were made under paragraph 15 designating the body in relation to that activity, the applicant would be competent, and have sufficient resources to perform the role of licensing authority in relation to the activity at the time the order takes effect.

<sup>10</sup> Paragraphs 11(3)(a) and (b) of Schedule 4 provides that the LSB must in particular be satisfied that the exercise of the applicant’s regulatory functions would not be prejudiced by any of its representative functions and that decisions relating to the exercise of regulatory functions would, so far as reasonably practicable, be taken independently from decisions relating to the exercise of representative functions.

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mechanism through which the LSB carries out its assessment against these requirements and the LSB has therefore satisfied itself of compliance with the requirements of Paragraphs 11(2) and 11(3) by an assessment of the application and proposed regulatory arrangements against the Rules for Licensing Authority Designation Applications.

5. Paragraph 16(1) provides that where an order is made by the Lord Chancellor under Paragraph 15 of Part 1 of Schedule 10, the applicant's proposed licensing rules are at the same time treated as having been approved by the Board.