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Dear Hazra

**Legal Services: removing barriers to competition (consultation on proposals to make amendments to the Legal Services Act 2007)**

Thank you for the opportunity to respond to this consultation on proposals to amend specific provisions around the licensing of alternative business structures (ABS) in the legal services market. The LSB is pleased to see this consultation. In July 2015 we highlighted the need for these changes in our joint submission with the regulators to ministers.<sup>1</sup> These proposals will have a net deregulatory effect on legal services, allowing regulation to be more targeted and proportionate. We agree that experience since 2011 has indicated there is nothing inherently riskier about ABS that requires a more stringent or inflexible approach to authorisation than that in place for a traditional law firm.<sup>2</sup> That being so, it is appropriate that regulators are allowed to exercise a similar level of discretion in their approach to authorising ABS as they may do at present for traditional law firms. The support for a level playing field for legal services firms seeking authorisation is a positive development and promises benefits for competition, innovation and growth.

**The LSB's oversight role**

The LSB will have a key role in overseeing and approving the new licensing rules that will follow from these proposed amendments to the Legal Services Act 2007 (the Act). For example, when existing licensing authorities (LAs) make changes to their regulatory arrangements, they must seek LSB approval of the changes. Further, when we assess applications from approved regulators (ARs) to become LAs we review and assess the suitability of the proposed licensing rules. These functions provide assurance to the public that the LAs are fulfilling their obligations under section

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<sup>1</sup> *Proposals for minor changes to the Legal Services Act 2007*. A joint submission to Ministers from the legal services regulators of England and Wales. June 2015. Available at: [http://www.legalservicesboard.org.uk/what\\_we\\_do/pdf/20150720\\_Proposals\\_For\\_Changes\\_To\\_The\\_Current\\_Legislative\\_Framework.pdf](http://www.legalservicesboard.org.uk/what_we_do/pdf/20150720_Proposals_For_Changes_To_The_Current_Legislative_Framework.pdf)

<sup>2</sup> LSB. 2016. *Evaluation: Changes in the legal services market 2006/07–2014/15*. Available at: <https://research.legalservicesboard.org.uk/news/latest-research-14/>

28 of the Act: to regulate legal services in line with the regulatory objectives, the principles of better regulation and best regulatory practice.

### **LSB guidance**

In support of our oversight responsibilities, in 2010 we published guidance on the content of licensing rules. The Act allows the LSB to have regard to how the regulators have considered this guidance when we exercise our functions of approving rules and recommending designation. Subject to the progress of the amendments in this consultation, we expect to revise and update our 2010 guidance on licensing rules to reflect these developments.

In publishing guidance on closely related topics, the LSB has demonstrated that it sees both the value and the need for guidance, both for LAs and for ourselves fulfilling our statutory responsibilities. Therefore, in our view we do not consider there is a need to introduce an explicit statutory duty on the LSB to produce guidance about these particular areas of discretion around ownership. The power is already available to the LSB under section 162 of the Act and we have already demonstrated we are willing to use this power to produce guidance in this area.

### **Planning for implementation**

The consultation paper does not provide detail on plans for transition to the new approach. We will support the implementation of these proposals by seeking the most efficient approach to rule approvals, using specific or generic exemptions where appropriate, and working to the statutory time limits.

Ideally, we would hope that the commencement of any new powers for LAs to exercise their discretion in this area would be timed to coincide with the publication of revised LSB guidance. Subject to Parliament's approval of the proposals in this consultation, we estimate that development and consultation on new LSB guidance would take around four months. We would ask the Ministry of Justice (MoJ) to adopt a phased approach that allows the LSB to publish revised guidance to the LAs before they seek to make changes to their regulatory arrangements. This would help to avoid any risk that LAs seek to implement new rules around ownership before we have completed the revision of our guidance.

The LSB does not "call in rules" for review or amendment. Our powers under Schedule 4, Part 3 of the Act only allow us to assess regulatory arrangements following a regulator's application for approval. If it is necessary to use our enforcement powers to direct a regulator to change its rules, this is a lengthy process following the statutory procedures laid out in the Act. Therefore, we would also ask the MoJ to give thought to how it can encourage LAs to take full advantage of the discretion these amendments can offer.

The LSB's response to the individual questions posed in the consultation is annexed to this letter. If you wish to discuss any aspect of our response further, please contact my colleague, Kate Webb.

Yours sincerely



**Neil Buckley**

Chief Executive

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Enc: LSB response to consultation questions

## Annex A: LSB response to consultation questions

### Proposal to amend Schedule 11 of the Legal Services Act 2007

*Question 1: Do you agree with the proposal that there should not be a requirement to provide services consisting of or including reserved legal activities from a practising address as currently required by paragraph 15 of Schedule 11?*

*Question 2: Do you agree with the proposal that: a) the requirement for an ABS to have a practising address in England and Wales is retained in paragraph 15 of Schedule 11 but Licensing Authorities may waive this requirement or may make licensing rules enabling them to waive this requirement; or b) alternatively, paragraph 15 is replaced with a power enabling Licensing Authorities to make licensing rules about addresses?*

1. We note that the proposal to amend Schedule 11 is intended to provide equivalence between traditional firms and alternative business structures (ABS) and agree that this an appropriate guiding principle to encourage a level playing field. We note that the proposed amendment would only have an impact on a subset of ABS. It is already the case that a company or limited liability partnership with a registered office in England and Wales does not have to have a practising address as defined in paragraph 15(2). Of the two options presented in question 2, our preference would be for (b), giving licensing authorities (LAs) the power to make rules about addresses. This avoids the use of waivers and provides greater equivalence with arrangements in place for traditional firms.
2. We note that the impact of this change may mean some new firms choose to become licensed and entitled to carry out reserved legal activities, but do not offer necessarily offer these particular services to consumers. We anticipate that the costs and benefits to business of this change will be assessed as part of the Ministry of Justice's (MoJ) impact assessment. This would include the cost of complying with regulatory arrangements such as accounts rules, insurance requirements, and providing rights of access to the Legal Ombudsman, alongside commercial benefits for firms, potential service benefits for consumers, and additional protection for consumers when things go wrong.

### Proposal to amend Schedule 13 of the Legal Services Act 2007

*Question 3: Do you agree with the proposals to amend Schedule 13 to the 2007 Act and allow Licensing Authorities to make their own rules around ownership of an ABS, and to impose a statutory obligation on the LSB to provide guidance regarding ownership?*

3. The current requirements in Schedule 13 are extremely prescriptive. They were developed on the assumption that ABS would be more risky than traditional legal services providers. This position is not supported by evidence gathered from nearly five years of ABS licensing, as discussed in the consultation paper and in the LSB's recent Market Evaluation report.<sup>3</sup> The

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<sup>3</sup> LSB. 2016. *Evaluation: Changes in the legal services market 2006/07–2014/15*. Available at: <https://research.legalservicesboard.org.uk/news/latest-research-14/>

detailed requirements in this Schedule are preventing LAs from targeting their activity according to risk.

4. It is our view that LAs should be given greater discretion under the Act to make their own rules around ownership and we support the MoJ's proposal. It could be extended to removing the detail contained in paragraphs 38–40. At present these offer discretion to LAs with respect to rules around share limits and voting limits. It would be disproportionate to retain such a level of detail in a revised Schedule given the broader policy aim of this consultation. Further there may be a question as to whether these paragraphs need to be retained at all, given that detailed rules around share limits and voting limits would need to be made in anticipation of need, and that we are not aware that any LA exercised the discretion that these paragraphs currently allow.
5. There are considerable opportunities to amend Schedule 13 to give licensing authorities discretion to make rules around ownership of ABS, both at initial application and once a licence has been issued. Further we would consider that criminal offences under Schedule 13 could be removed. LAs have powers to address failures to comply without having to take firms to court and prove failure to comply to a criminal standard. We also note that none of these criminal offences have been prosecuted to date.
6. The aim for these proposals is to allow greater discretion around ownership rules. That being so, there is no requirement in our view to alter the LSB's role in prescribing consistent time limits for appeals and other decisions, and in our view this should be retained.
7. We note that not all of Schedule 13 makes provisions that if amended could be left to the discretion of a licensing authority. For example, paragraphs 47–51 place a responsibility on the LSB to keep records of decisions made by licensing authorities under this Schedule regarding objections to holding a restricted interest and conditions on holding a restricted interest. The LSB has yet to receive a notification under these provisions. In spite of this, we consider that these arrangements cannot be adequately replaced by giving additional discretion to licensing authorities. The LSB's oversight role means we are best placed to maintain central records of these decisions, as demonstrated by other recordkeeping roles we hold with respect to ABS such as section 100 lists of disqualified persons. There is no other organisation able to fulfil this role. We would recommend that these paragraphs are amended only as far as necessary to support the broader policy intention under consultation – that LAs have discretion over ownership rules – but that the LSB's core responsibility to maintain a list of decisions is retained, as is an LA's duty to notify the Board in particular circumstances.
8. The LSB has a role to play in supporting these changes. We already publish guidance on licensing rules and we would revise and update this guidance if Schedule 13 is amended by Parliament. Powers in section 162(1)(e) of the Act allow the LSB to produce guidance for regulators about the content of licensing rules. Under section 162(5) the LSB may have regard to the extent to which a regulator has complied with this guidance, similar to a "comply or explain" approach. This allows us to use our guidance in our statutory decision making functions, including rule change approvals under Part 3 of Schedule 4 of the Act. As the Board is currently exercising a pre-existing statutory power in this area, we would suggest that it is not necessary to introduce a new explicit duty on the LSB to produce guidance about these particular issues of discretion around ownership.

*Question 4: Do you think amending Schedule 13 and giving Licensing Authorities greater discretion in deciding on the necessary checks for licensing, would encourage more applications from businesses to become ABS?*

9. We would expect that other organisations, including the LAs, would be better placed to comment on this question. In principle, we would observe that as well as encouraging more applications from businesses to become ABS, these reforms also offer two further areas of benefit that could be assessed. First, we would expect the reforms may allow a LA to approve more applications, even if the rate of initial applications did not increase. Second, we would also expect licensing decisions could be taken more quickly, allowing swifter access to the legal services market.

*Question 5: Do you think giving Licensing Authorities greater discretion would reduce the timescales and cost of the licensing process, and if so, by how much?*

10. Yes, as noted in answer to the previous question, in principle this should be a positive outcome from these reforms. We would expect current LAs to be able to provide greater detail on the benefits for timescales and costs.

#### **Proposal to repeal section 83(5)(b) of the 2007 Act**

*Question 6: Do you agree with the proposal to repeal section 83(5)(b) of the 2007 Act?*

*Question 7: Do you agree that Licensing Authorities and ABS applicants would make savings in terms of costs, time and resources, if we were to repeal section 83(5)(b)?*

11. We fully support the proposal to repeal section 83(5). This provision duplicates other statutory duties and obligations around access to justice, such as section 28(2) of the Act. If repealed, LAs will still have a duty to promote the regulatory objectives in the decisions they make. The current arrangements add cost and time to the authorisation process while generating no additional value.

#### **Proposal to amend sections 91(1)(b) and 92(2) of the 2007 Act so that the Head of Legal Practice and Head of Finance and Administration of an ABS are only required to report a "material" failure to comply with licensing rules**

*Question 8: Do you agree with the proposal to amend sections 91(1)(b) and 92(2) of the 2007 Act?*

*Question 9: Do you agree with the proposal that regulators should provide guidance to businesses on how they define "material" failure to comply with licensing rules?*

*Question 10: Do you agree that regulators and ABS businesses would make savings in terms of costs, time and resources if we were to amend sections 91(1)(b) and 92(2) as proposed, and if so by how much?*

12. We support the proposal to amend section 91(1)(b) and 92(2) of the Act. In the interests of consistency we consider that changes to section 91(3) and 91(4) may also be needed.



13. The current requirements on Heads of Legal Practice and Heads of Finance and Administration go further than the equivalent obligations placed on traditional firms. The requirements also introduce unnecessary additional costs for regulators in the time they spend reviewing reports. They prevent regulators from targeting regulation in accordance with the better regulation principles. There is no evidence in support of this additional burden on ABS, and it would be more proportionate and consistent if the same arrangements applied to all firms. In principle, therefore, we would expect regulators and ABS to make time, cost and resource savings as a result of these changes. Other respondents, including the regulators and firms, would be better placed to provide details of such savings.
14. We do not consider that LAs should be statutorily required to provide guidance on definitions of "material" failure. We note that the SRA has produced such guidance for traditional law firms without being required to do so by Parliament. We would expect other LAs to act in a similar manner should licensed bodies require support to comply with regulatory duties. We do not see any reason why introducing materiality for ABS reporting should trigger the need for a statutory obligation to provide guidance, when such an obligation was not deemed necessary in respect of traditional firms' reporting. Further, statutory guidance may be perceived differently by providers to other, non-statutory guidance prepared by the LA, and may influence how providers comply.

#### **Further potential areas for simplification and reducing unnecessary regulatory burdens.**

*Question 11: Do you agree that the proposed changes to ABS regulation are sufficient to ensure a level playing field for entry to the market and regulation in the market for ABS and other firms? If not, what further changes do you think would be needed?*

15. In our response to question 8 we note that consequential amendments in section 91 of the Act would be needed. Changes to the statutory framework are useful and important steps in helping to deliver a level playing field for ABS and other firms, and we note that the Competition and Markets Authority's interim findings, published last month, did not find any substantial barriers to entry. We await their final report in December. However, the full potential of these changes will be realised when licensing authorities opt to exercise the discretion these amendments provide for and alter their regulatory arrangements.

*Question 12: Are there any further amendments that might be made to a specific provision of, or schedule to, the 2007 Act which deals with the regulation of ABS? If so, please explain why and where possible provide evidence to support your argument.*

16. We have no further amendments to propose at this time. We may identify further amendments in the future and if so will revert to the MoJ.

#### **Cost / Benefit Analysis**

*Question 13: We would welcome additional data or evidence in relation to these proposals, in the light of which the cost assessment will be revised and published with the government's response to this consultation.*

17. Our previous response on the proposals to amend Schedule 11 note a specific point on the impact of removing the requirement to carry on reserved legal activities at a practising address for some ABS (see paragraphs 1-2). We have no further comments.

### **Equality Impacts**

*Question 14. We welcome your views in terms of any potential equality impacts of the proposals. Are there other ways in which these proposals are likely to impact on race, sex, disability, sexual orientation, religion and belief, age, marriage and civil partnership, gender reassignment or pregnancy and maternity that you are aware of? If so, please tell us how, together with any supporting extra sources of evidence.*

18. We have nothing to add to the consultation paper's discussion of these issues.

