



### Summary of decision

The purpose of this summary sheet is to provide a high level and accessible synopsis of the Legal Services Board's ("the LSB") decision. Readers are recommended to read the formal decision notice below for further detail. **This summary is not and should not be taken as a formal part of the LSB's decision notice under the Legal Services Act 2007 ("the Act").**

The LSB's decision is to grant in full the application from the Council for Licensed Conveyancers (CLC), approving alterations to its regulatory arrangements in respect of its Compensation Fund. The application proposes that the contribution level is to reduce by 60% for all firms, other than those who pay only the minimum contribution.

Following the assessment of the CLC's application, the LSB has concluded that the changes do not meet the refusal criteria in the Act.

## Decision notice

### **The Council for Licensed Conveyancers (CLC) application for approval of alterations to its regulatory arrangements relating to Compensation Fund contributions for 2019/20**

The Legal Services Board (“**LSB**”) has granted an application from the Council for Licensed Conveyancers (“**CLC**”) for approval of Compensation Fund Determinations for 2019/20 which set the level of contribution to the Compensation Fund for CLC practices.

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.
2. This application has been made by the CLC in its capacity as an approved regulator.
3. This decision notice sets out the decision taken, including a summary of the changes. The notes at page 7 of this notice explain the statutory basis for the decision.
4. The chronology for the LSB’s handling of this application is also set out below.

## Chronology

- The LSB confirmed receipt of an application from the CLC on 27 August 2019.
- The 28 day initial decision period for considering the application ends on 23 September 2019.
- This decision notice is effective from 23 September 2019.
- The decision notice will be published on the LSB’s website by 25 September 2019.

## Background

5. On 27 August 2019, the CLC submitted an application to the LSB for the approval of changes to its regulatory arrangements relating to Compensation Fund contributions.
6. Each year the CLC considers the level of contributions required for the Compensation Fund from the practices that it authorises.
7. The established methodology for calculating contributions to the Compensation Fund, which the CLC has relied on since 2010, is:
  - (i) contributions are set at minimum fixed levels based on the four bands of turnover, (“The Fixed Contribution”); plus
  - (ii) a percentage based uplift for all bands (excluding band 1) is added where the turnover exceeds the minimum for the band (the “Uplift”).

This methodology is set out in the table in Annex A.

8. Since 2011 the CLC has permitted the level of reserves in the Compensation Fund to increase significantly. The CLC's application confirms that the balance of the Compensation Fund stood at £7.18million in December 2018. The CLC has forecast that the fund will hold £6.98million by December 2019.

### **Proposed changes**

9. The CLC proposes a 60% reduction to both the Fixed Contribution and the Uplift for firms whose turnovers exceed £100,000. No changes are proposed for firms with turnovers of £100,000 or below, so they will continue to pay the minimum contribution of £500. The CLC has forecast that this will provide for total contributions of £388,553 for 2019/20, compared to final projected contributions of £678,114 for 2018/19.

### **Key issues considered in the assessment**

10. Having considered the CLC's application and supporting documents, the LSB has identified the following key issues in relation to the application.

#### Impact of reduction

11. Annex 2 of the CLC's application includes a table which provides examples of the impact of the reduction on CLC firms with certain levels of turnover. This shows that the largest beneficiaries of the reduction are firms with the largest turnovers.
12. During the course of the assessment of the application the LSB asked the CLC to explain the rationale for maintaining the minimum contribution of £500 for smaller firms (i.e. those with a turnover of £100,000 or less).
13. The CLC has explained that it considers it appropriate to maintain a minimum firm contribution of £500 overall. While this results in a larger contribution level relative to turnover, the CLC considers that this is justified for smaller firms, as they are more likely to generate costs to the Compensation Fund. This relates to increased likelihood of both interventions<sup>1</sup> and closure without adequate succession planning. The latter in particular can regularly result in costs relating to file storage.

#### Compensation Fund Reserves

##### *Assurance of funding*

14. As noted in paragraph 8 above, the CLC's application confirms that the balance of the Compensation Fund stood at £7.18million in December 2018. The CLC's reserves policy provides that it should seek to maintain reserves of £2 million for its Compensation Fund. During the course of the LSB's enquiries, the CLC explained why the reserves were so large.

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<sup>1</sup> Where the CLC identifies that an organisation needs to be closed down to protect the public interest, CLC will 'intervene'. All documents and papers that relate to its clients, including files and accounting records are removed from the intervened firm.

15. The CLC explained that the balance of the Compensation Fund currently makes provision for (i) probable claims of approximately £2.35million and (ii) contingent liabilities of approximately £3.46million. These figures are updated versions of the figures reported in the CLC's financial statements<sup>2</sup>. The vast majority of the probable claims and contingent liabilities relate to a small number of high value historic cases where the full costs have not yet been confirmed and become payable. The CLC's application includes projections on future reserve levels that assume that these costs are not realised during 2020, although it is foreseeable that they could be realised during 2020. The CLC has emphasised that the above amounts represent the maximum the CLC would expect to pay if all probable claims and contingent liabilities were paid in full.
16. Excluding funds allocated to probable claims and contingent liabilities, the fund is left with a minimum available reserve of approximately £1.37million. This would then increase to around £1.685 million as, subject to the LSB approving its application, the CLC expects to receive fresh contributions of £315,000 (net of the costs of running the fund) for 2019/20. This is therefore slightly below the £2 million minimum reserve provided for in its reserves policy. This £1.685 million is the pot from which it would expect to be able to meet costs that arise during 2020.
17. In terms of the likely costs to the compensation fund, the CLC explained that, since 2011, the average annual claims on the Compensation Fund amounted to £415,799. However, the CLC was of the view that this average figure was inflated due to two exceptional interventions in 2013. Since 2013 the CLC has not had any similar interventions. If those outlier interventions were excluded, the average figure for annual claims on the Compensation Fund would decrease to approximately £200,000 per year.
18. The CLC also explained that it has taken mitigating action in order to reduce the risk of interventions. This has included:
  - proactively requesting bank requisitions from firms on short notice in order to identify issues,
  - maintaining a list of sole practitioners so that the CLC is, as far as possible and appropriate, able to maintain close contact with those sole practitioners, and
  - increased interactions with firms through a risk focused approach.
19. The LSB will be interested to receive reports about the effects of the CLC's mitigations in future applications.
20. Overall, if 2020 sees costs in line with the annual average of £200,000, the CLC's minimum available reserves (excluding probable claims and contingent liabilities) would be reduced to around £1.485 million. CLC has predicted that if contribution levels are maintained, it will take approximately 6 years for its minimum available reserves to steadily increase to £2 million (in line with its policy).

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<sup>2</sup> <https://www.clc-uk.org/wp-content/uploads/2017/12/CLC-Annual-Financial-Statements-2018.pdf>

21. The LSB notes that (i) this projected timescale for the minimum available reserves to recover and (ii) the level of minimum available reserve, only apply if the probable claims and contingent liabilities set out in paragraph 15 above conclude and are paid out in full. If any of the contingent liabilities or probable claims result in costs below the maximum that has been set aside, this would release funds that could increase the available minimum reserve.
22. The LSB considers that future applications would benefit from a clearer articulation of the CLC's policy on the minimum amount needed for its Compensation Fund. This application refers to a minimum reserve of £2million, but it is apparent from the additional information the CLC has provided to the LSB that the CLC does not consider that it is necessary to hold this amount each year, in the light of the additional funds allocated to probable claims and contingent liabilities.
23. The LSB also expects future applications to include more detail on the allocation of money held in the Compensation Fund, to provide a complete picture of the position in relation to reserves, probable claims and contingent liabilities.

#### *Estimated costs*

24. The CLC's application confirms that it has been tracking the level of payments from the Compensation Fund in recent years. It further explains that such tracking has enabled the CLC to anticipate with greater confidence the likely costs in any one year. However, it has explained that it had not modelled the likely costs of interventions and payments made from the Compensation Fund for 2019/20. We asked for further information on likely costs for 2020.
25. As noted above, the CLC provided us with an analysis of previous costs on the compensation fund. Since 2011, the average annual costs to the compensation fund have been £415,799. This is inflated by two exceptional interventions in 2013. If those outlier interventions were excluded, the average figure for annual claims on the Compensation Fund would decrease to approximately £200,000 per year. Over the last four years, CLC has intervened in up to 3 practices per year with costs ranging from a few thousand pounds per intervention up to costs in excess of £350,000.
26. In future applications we expect the CLC to provide an explanation of the expected costs, how these have been determined and what the impact will be on reserves and the ability of the fund to meet its obligations.

#### Consultation

27. The CLC consults on its Compensation Fund alongside its Licence and Practice Fee arrangements. Our analysis of the CLC's consultation is set out at Paragraphs 21-31 of the decision on the CLC's 2019/20 Practice Fees<sup>3</sup> under section 51 of the Act.

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<sup>3</sup> <https://www.legalservicesboard.org.uk/our-work/statutory-decision-making/section-51-practising-fees/2019-practising-fee-applications>

28. The only consultation response the CLC received that was of specific relevance to the Compensation Fund was a suggestion that firms with better claims records make reduced contributions. The CLC responded by explaining the proposed reductions to the Compensation Fund that are at the heart of its application to the LSB.

### **Decision**

29. The LSB has considered the CLC's application against the refusal criteria in paragraph 25(3) of Schedule 4 to the Act. It considers that there is no reason to refuse this application and accordingly, the application is granted.

30. **Annex A** to this decision notice contains the relevant extract from the CLC's fees framework approved by the LSB.

**Matthew Hill, Chief Executive**

**Acting under delegated authority granted by the Board of the Legal Services Board**

*Notes:*

1. The LSB is required by Part 3 of Schedule 4 to the Act to review and grant or refuse applications by approved regulators to make alterations to their regulatory arrangements.
2. Paragraph 25(3) of Schedule 4 to the Act explains that the LSB may refuse an application setting out a proposed change to the regulatory arrangements 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 [of the Act] 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.
3. The designation requirements referred to in paragraph 2(b) above are set out in paragraph 25(4) of Schedule 4 to the Act and are:
  - (a) a requirement that the approved regulator has appropriate internal governance arrangements in place
  - (b) a requirement that the applicant is competent, and has sufficient resources to perform the role of approved regulator in relation to the reserved legal activities in respect of which it is designated, and
  - (c) the requirements set out in paragraphs 13(2)(c) to (e) of Schedule 4, namely that the regulatory arrangements are appropriate, comply with the requirements in respect of resolution of regulatory conflict (imposed by sections 52 and 54 of the Act) and comply with the requirements in relation to the handling of complaints (imposed by sections 112 and 145 of the Act).
4. In accordance with paragraphs 20(1) and 23(3) of Schedule 4 to the Act, the LSB has made rules<sup>4</sup> about the manner and form in which applications to alter regulatory arrangements must be made. Amongst other things, the rules highlight the applicant's obligations under section 28 of the Act to have regard to the Better Regulation Principles. They also require applicants to provide information about each proposed change and details of the consultation undertaken.
5. 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.

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<sup>4</sup> LSB's Rules for applications to alter regulatory arrangements – Version 2 April 2018  
[https://www.legalservicesboard.org.uk/what\\_we\\_do/regulation/pdf/New%20folder%20\(2\)/FINAL\\_Rules\\_for\\_applications\\_to\\_alter\\_regulatory\\_arrangements.pdf](https://www.legalservicesboard.org.uk/what_we_do/regulation/pdf/New%20folder%20(2)/FINAL_Rules_for_applications_to_alter_regulatory_arrangements.pdf)

## **Annex A – extract from CLC Fees framework**

### **Compensation Fund Contribution**

5. The Compensation Fund contribution payable by a CLC Body as provided by
- (1) paragraph 5(a)(iv) of the CLC Recognised Bodies – Recognition Framework; and
  - (2) paragraph 7.11 of the CLC Licensed Body (ABS) Licensing Framework

shall be the turnover declared by the CLC Body for the purpose of determining the applicable annual premium payable in accordance with paragraph 10.1 of the CLC Professional Indemnity Insurance Code & Guidance as follows:

<b>Turnover Banding</b>		<b>Compensation Fund contribution</b>			
<b>From</b>	<b>To</b>	<b>Minimum Fee in Band</b>			
0	£100,000	£500			
		<b>Minimum Fee in Band</b>			<b>On Turnover in excess of</b>
£100,001	£500,000	£500	plus	0.16% <del>0.4%</del>	£100,000
£500,001	£3,000,000	£1,140 <del>£2,100</del>	plus	0.12% <del>0.3%</del>	£500,000
Over	£3,000,000	£4,140 <del>£9,600</del>	plus	0.08% <del>0.2%</del>	£3,000,000