Solicitors Regulation Authority

SRA response

Proposed rules under section 30 of the Legal Services Act (Part 2), Legal Services Board consultation

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Practising fees and the links with section 30: introduction and overview

1. We agree that the provisions of section 30 to secure regulatory independence, and those in section 51 on fee setting, are inextricably linked. Our views in relation to section 51 are based on the following principles which flow from the Act:
    a. Practising fees are mandatory and must be used for regulatory or public interest activities only. Where the representative arm uses practising fee income for permitted purposes under the Act, the use of that income must be transparent;
    b. Section 51 of the Act puts beyond doubt that the setting of practising fees is part of the regulatory arrangements of an approved regulator;
    c. The regulatory arm must be responsible for determining the budget which it requires for regulatory purposes;
    d. Where services are shared between regulatory and representative arms, there must be a transparent and equitable means of apportioning those overheads.
2. The total cost of regulation (including the funding of permitted purposes) has to be collected from the regulated community as fairly as possible. Allocating the cost can involve a number of difficult policy issues and choices. We believe that the intention of the Act is that such decisions should not be made by a representative-controlled approved regulator, but as part of the regulatory arrangements, subject to the approval of the Legal Services Board (LSB). The consultation paper does not deal explicitly with this point, and it would be helpful for the LSB to confirm that this reflects its understanding of the Act.
3. The complication caused by the fact that the total cost of regulation can include the cost of "public interest" activities provided by the representative function of an approved regulator, and the cost of shared services, reinforces the

need for mechanisms such as the independent oversight body or the independent and objective forum proposed in the part of the consultation on section 30 rules (in relation to the Law Society, we have suggested that this should be a corporate board).

4. There are a number of stages to the setting of practising fees. Arguably the most important is the initial budget-setting and agreement process. That process will lead to the identification of what the Financial Services Authority refers to as the annual funding requirement (AFR) which needs to be collected. The regulatory arm must be free, subject to the usual constraints, to set its own budgets to fund its regulatory activities, including its share of shared services costs. The budget for "permitted purposes" provided by the representative arm would be a matter for the representative arm—subject, we assume, to appropriate consultation with the regulated community. The corporate board would be able to consider the totality of budgetary requirements, in particular in relation to the allocation of shared services costs.

5. The next stage is to decide how to allocate the AFR among the regulated community. For some regulators, that decision may be relatively straightforward; for others, it may be a more complicated matter. The SRA is about to consult on making a significant change in the way it allocates the cost as a result of changes introduced by the Legal Services Act bringing about firm based regulation and legal disciplinary practices.

6. We believe that the approval by the LSB of "practising fees" will need to take all these stages into account. The key variable each year is likely to be the budget setting leading to the calculation of the AFR. Provided that the LSA procedures capture the approval of that process and, if necessary, the amount of the AFR, and provided they are satisfied with the fairness of the formula used to allocate the cost among the regulated community, approval of the final stage—the setting of the level of the practising fees—should in most cases be a final step which is a relative formality.

7. Therefore, while section 51 refers to the LSB approving "the level of the fee", we believe the focus of the approval process should be on earlier stages of the fee-setting procedure. There is an additional advantage to such an approach. What will probably be common to all regulators is that the final setting of the level of the fee can only be done a relatively short time before it is necessary to begin the

collection process. Ensuring that the final approval of the LSB can be given quickly will be essential. We would therefore advise that front-loading the approval process into the earlier stages is the right way forward.

The permitted purposes

Question 9

Do you agree that the mandatory permitted purposes currently listed in statute should be widened to include explicit provision for regulatory objective (g), i.e. "increasing public understanding of the citizen's legal rights and duties"?

8. We agree that the permitted purposes set out in section 51 do not clearly include activities aimed at increasing public understanding of citizen's legal rights and duties, and that it should be added to the list. This regulatory objective is shared by the LSB and all approved regulators. Whether it is more effective for the LSB, like the FSA, to take a lead in fulfilling this objective, or the regulatory or representative arms of approved regulators, is a matter for further discussion. It would clearly be cost effective to avoid unnecessary duplication of effort in relation to this particular regulatory objective.

Question 10

Should any other (general or specific) purpose be permitted under our section 51 rules?

9. We have no other suggestions for additional purposes to be permitted under section 51.

The application process

10. We agree that one size cannot fit all and the general proposal to set criteria applicable to all, with different detailed arrangements being agreed with each approved regulator according to a published Memorandum of Understanding is a sensible approach.

Question 11

What do you think about our proposal to seek evidence that links to the regulatory objectives in the Act?

11. We are not sure whether seeking evidence specifically linking the proposed level of practising fees to regulatory objectives will in itself do much to assist the LSB's ability to approve the level of fees. It could turn into a bureaucratic box-ticking exercise. Our point is not that the LSB does not need evidence establishing that approved regulators are acting in a way which is compatible with and takes into account the regulatory objectives. It is rather that the LSB should already have assurance through its work on regulatory reviews referred to in chapter 4 of the LSB's business plan. What is important is that the regulatory activities meet the regulatory objectives and better regulation principles [https://www.sra.org.uk/sra/strategy#appendix] . We are not sure why additional evidence should be required as part of the practising fee approval process. This may be what paragraph 4.13 is referring to.

12. We consider it would be important for the LSB to concentrate on understanding the budget-setting process and the underlying cost of the activities of each approved regulator at a much earlier stage in the process rather than at the point of being asked to approve the fee. We agree that, once this detailed exercise has been undertaken, probably as part of the regulation review, from that point on it would be appropriate for the LSB to concentrate on the need for any increases or reductions in future years, as the level of practising fees is normally a consequence of any increase or decrease in regulatory activities.

Question 12

What criteria should the Board use to assess applications submitted to it?

13. We believe the criteria should reflect the different stages of a fee-setting process as discussed in the opening paragraph of this section of the response [#part-1] . We find it difficult to say more than that the high level criteria should refer to the regulatory objectives and better regulation principles, and should learn from the development of work on regulation reviews which, we assume, will deal with the way in which approved regulators will demonstrate accountability and cost effectiveness.

Question 13

If they are adopted, what should Memoranda of Understanding between the Board and approved regulators contain? For approved regulators in particular, are there any particular implications for the organisations?

14. As indicated above, we believe that an MOU with each approved regulator will be important to reflect the particular circumstances of that approved regulator. If that is achieved, MOUs should not have any particular implications for the organisations. The MOUs are likely to include details to show how each approved regulator's processes and procedures would deliver against the high level criteria. This would be different for each approved regulator and may also depend upon the impact of the rules made under section 30 on individual corporate governance arrangements. Key issues will include the process for approving the budget, the need for consultation with the regulated community and other stakeholders and, in particular systems, to make sure that costs are transparent. They are likely to set out the budget-approval timetable for each approved regulator and should indicate at what stage the LSB will be consulted and asked to give particular approval.

Question 14

Should there be a requirement on approved regulators to consult prior to the submission of their application each year—and, if so, who should be consulted and on what? Should there be a distinction drawn between approved regulator with elected representative councils or boards; and those which have no such elected body?

15. Consultation should be required as a principle, but the detail of the extent and timing should be covered in the MOU, as the extent of consultation will, we believe, depend on the circumstances. Clearly, any significant change in the formula for the allocation of the cost among the regulated community must be the subject of consultation with the regulated community. For those approved regulators with an elected council or similar representative body, a minor adjustment to a formula may in some cases only need to be the subject of a consultation with that body. However, if the formula for the allocation of costs among the profession has been fixed following consultation, it may not change for a number of years, in which case perhaps the only further consultation required would be to alert the profession to increases or decreases of the AFR. Again, in some circumstances, the consultation may be required to publicise any likely increases or decreases to allow the regulated community to plan their own budgets. However, in some cases where a budget increase is due to a decision to undertake a new regulatory activity or permitted purpose, then consultation on

whether or not the activity should be undertaken may be required.

16. Again, consultation should take place as soon as the issue which requires this consultation has been recognised, rather than leaving it until the time when the approved regulator is about to seek final approval of the level of the practising fee under section 51.

17. The rationale for representative bodies consulting on providing public interest activities within the permitted purposes through the representative arm is more interesting. There is an argument that the regulated community should be able to influence the extent to which practising fees are used by the representative arm to support such public interest activities. It would also be possible for the LSB to seek views from the regulatory arms on what public interest activities should be provided by representative arms and whether any proposed activities, in their view, are in the public interest.

Maximising transparencies

Question 15

What degree of detail would be most appropriate to require when seeking to maximise transparency but be proportionate in terms of bureaucracy? Have we got the balance right?

18. We agree that there should be transparency and that balance is required. We think that the balance set out in paragraph 4.21 looks about right, although we consider that approved regulators with shared services should be encouraged as far as possible to allocate the cost of shared services to the regulatory and representative arm, and so that the amount that cannot be so categorised is as low as possible. That way, transparency is maximised.

Question 16

Are there any issues in respect of practising fees that you think we should consider as part of this consultation exercise?

19. We refer back to the point we made in paragraph 2 [#part-2] . Given the fact that practising fees raised cover the costs of a number of activities, can the LSB confirm whether it considers that it is more appropriate for any final decision setting the level of fees to be made by the regulatory arm of an approved regulator (as appears to be contemplated by

section 51); or that such fees should be subject to final decision by an elected representative body of an approved regulator?