

Legal Services Board (LSB) Consultation: Proposed Internal Governance Rules

**A response by
The Chartered Institute of Legal Executives (CILEx)**

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1. Introduction

- 1.1. The Chartered Institute of Legal Executives (CILEx) is the professional association and governing body for Chartered Legal Executive lawyers, other legal practitioners and paralegals. CILEx represents around 20,000 members, which includes approximately 7,500 fully qualified Chartered Legal Executive lawyers.
- 1.2. CILEx is the Approved Regulator (AR) under the Legal Service Act 2007. These regulatory powers are delegated to the independent regulator CILEx Regulation Ltd.
- 1.3. CILEx benefits from a positive relationship with the LSB and believes that amendments to the internal governance rules (IGRs) will make them more effective than the existing set, and create an environment enabling further incremental improvements towards ensuring true regulatory independence.
- 1.4. CILEx fully supports the principles set out in the consultation paper, enshrined in the revised IGRs. We believe our recent governance reforms have already put us in alignment with the IGRs and therefore can say that we are not just committed to achieving compliance with the new rules; we are also committed to achieving the greatest possible level of regulatory independence permissible under the current legislative framework. CILEx therefore sees the application of the new rules as a further step towards achieving that ultimate aim.
- 1.5. In order to achieve this, we believe that there are some elements of the rules and guidance that would benefit from some further clarity. This is particularly the case in relation to the residual role of the AR which could be clearer.

2. Responses to specific questions

Question 1: Do you agree that the proposed rules would enhance the independence of regulatory functions and improve clarity leading to fewer disputes and more straightforward compliance/enforcement? If not, why not?

And

Question 2: Does the proposed guidance provide sufficient detail to help you to interpret and comply with the proposed IGR? Please provide specific comments on any areas of the guidance where further information would improve clarity.

- 2.1. CILEx agrees that overall the proposed rules will enhance the independence of regulatory functions through greater clarity regarding the lines of separation and the terms of the relationship between ARs and their Regulatory Bodies. This

should in itself reduce the number of scenarios which could result in dispute and the complexity of compliance/enforcement issues.

- 2.2. In particular, CILEx welcomes those amendments which seek to remove outdated or confusing terminology within the current rules. We also support the principle of removal of subjective language and anchoring the rules more firmly to the parameters of the legislation. We do however, think that some of the language contained within the draft rules is still subjective and therefore at risk of alternative interpretations or the source of dispute between ARs and their RBs and we would urge consideration of how such terms could be better defined.
- 2.3. The most significant example is the continued reference to resources 'reasonably required'. Although the consultation paper and the guidance talk about reasonableness not being subjective but, for example, applied 'in the objective legal sense' or reflecting 'the better regulation principles of proportionality and targeting action only at cases where action is needed', there is little specific to guide the AR as to what might be reasonable or not. Indeed, the guidance suggests that this is not a view the AR should or is required to take in case, stating that for 'an AR who has delegated its regulatory functions, this assessment will be carried out by the regulatory body'¹. If reasonableness is what the RB says it is, this seems less of an objective application than the IGRs intend.
- 2.4. Outlined below are those other aspects of the rules and guidance which CILEx considers require further clarity to enhance understanding and promote consistent application of the rules, ensuring compliance and reducing possible disputes arising out of differences in interpretation:

Independence²

- 2.5. There could be greater clarity in the guidance (and possibly Rule 1 itself) in relation how the AR ensures that its representative functions do not 'influence' the regulatory functions delegated to the Regulatory Body (RB). On one reading, 'influence' could be construed as meaning any instance in which the AR communicates with the RB with a view to providing feedback / bringing to their attention issues that require addressing relating to a proposed or actual regulatory arrangement, for example, it is not delivering the outcome it was intended to or it is no longer related to the reality of practice. The AR is uniquely placed to offer the insights and perspective of practitioners; whilst it is of course entirely the business of the RB whether and how it uses that information,

¹ Guidance, page 27

² Rule 1 The Overarching Duty

offering it should not be construed as trying to ‘influence’ the RB negatively and therefore non-compliant with the new IGRs.

- 2.6. The Act³ talks in terms of ‘prejudice’ rather than ‘influence’; perhaps reference to and anchoring more thoroughly in the language of the Act might ensure consistency whilst also creating the clarity needed. CILEx is confident⁴ that the rule and guidance was not written in a way that would unreasonably inhibit the AR in such a core representative role, but it would be better if that clarification could be in the drafting itself.

Regulatory Resources

- 2.7. CILEx supports the principle of regulatory autonomy⁵ enshrined in the new IGRs and appreciates and supports that proper maintenance of that autonomy comes through the RB having the regulatory resources that it says it needs⁶. CILEx welcomes the reinforcement of the related principle that the RB should set its own budget⁷, without interference or influence from the AR, and determine the allocation of its resources.
- 2.8. In fact, in our view, CILEx has already had some success at ensuring the processes and procedures are in place to achieve this now. We have always taken the view that the RB should be managing its financial affairs itself, and in an effective and proper manner, responsibly, efficiently and with probity.
- 2.9. CILEx therefore continues to support the principle that the financial husbandry of the RB should be only the RB’s business and through the PCF it should have access to the resources it demonstrates it needs and should be left to manage them properly. However, the proposed rules and guidance, as drafted, do not appear to either reflect the fact that each AR has a different financial model/relationship with its Regulatory Body. Nor do they adequately address the issue of ARs retaining the financial liability and funding requests from the RB outside of the PCF process without any ability for the AR to satisfy itself that the request has not arisen as a result of the RB having failed to budget or manage its resources effectively.
- 2.10. CILEx acknowledges that there can be situations where unforeseen circumstances arise which may have budgetary repercussions. Such scenarios are problematic to RBs given the accepted principles that RBs should not be

³ S30

⁴ Particularly from the LSB’s comments at the 11 December workshop event

⁵ Rule 4

⁶ Rule 9

⁷ Rule 10

budgeting to make a profit on their regulatory income⁸ and that they should not be encouraged to build up reserves. However, in such scenarios, the IGR guidance should perhaps make it clear that, unless the scenario is of such severity to compromise delivery of the regulatory objectives, it is reasonable to defer and manage it in the next financial year when budgetary provision can be made thereby limiting the circumstances in which as RB has to seek financial assistance from the AR.

- 2.11. We consider the current rules/drafting do not support greater independence in this regard as they are capable of being interpreted as enabling the RB to rely on the ability to the AR in year for more resources. Worse still, we believe this creates an unreasonable and unquantifiable liability on the AR which, depending on the scale, could represent a severe risk to its own activities.
- 2.12. In CILEx's case, the existing mechanism whereby parts of the Group have to bid, with a business case, for funding from a central contingency fund, could be an acceptable model for reference in the guidance. Such a model is not designed to deny funds to the RB but would enable specific analysis and assurance that the discrete funds were required for legitimate reasons and not due to anything going wrong. The arrangement could be enshrined in an appropriate protocol.
- 2.13. Finally, with regard to resources, whilst the draft rules make it clear the RB must manage its financial affairs independently and without oversight or scrutiny by the AR, it fails to make clear where the accountability and assurance around financial probity does lie. To address this, we would suggest consideration needs to be given to more explicit provisions within the LSB's Performance Review Process relating to the RBs management of financial affairs, effective budgeting and efficient operations.

Shared Services

- 2.14. CILEx is grateful for the clarification at the workshop event⁹ that both the RB and the AR must agree to the (exceptional) provision of shared services and that a waiver must be applied for. It must be right that neither party is disadvantaged by having to enter into an arrangement or forced to accept one on unequal terms.
- 2.15. For its part, this is an aspect of the proposed IGRs with which CILEx wishes to go as far as possible, having no dual roles and as few shared services as it practicable. This links to CILEx's overarching objective of achieving full

⁸ ie should budget only to cover regulatory costs reasonably incurred

⁹ 11 December 2018

structural separation/independence in the long term and, in the medium term, achieving the greatest degree of separation/independence as can be achieved under the current regulatory framework.

- 2.16. In moving in this direction, CILEx recognises that an incremental approach is necessary, with a gradual reduction in the numbers of shared services, and that it is also paramount that any related changes should not adversely affect the Practising Certificate Fee (PCF) i.e. should not increase it. CILEx is perhaps more able to take this line because its finance and governance model is distinctive compared to other AR/RB dependencies, and has subsidised aspects of its regulator's budget for some time.
- 2.17. That said, the guidance would benefit with more granular clarification in order to ensure the cost/benefit principle in particular is adhered to and that this too is agreed¹⁰ jointly between the RB and the AR.

Saving provisions/Waivers

- 2.18. The guidance is very light in respect of the process envisaged as part of any system of waivers under the savings provisions¹¹. The clarification at the workshop event was helpful but could have gone further given the challenge of attaining compliance in 6 months. It is likely that, in the early stages, the waiver process will be much used and greater detail on that would therefore be very helpful.

PCF Timetable

- 2.19. Allied to the above point, it has been recognised that the PCF for 2019 has already been set and the 2020 PCF budget will be finalised before the final IGRs are published. However, CILEx believes that the 2020 budget-setting process offers a real opportunity to move towards achieving the greatest extent of independence possible. More explicit guidance about realising that potential as part of that process and the interplay with the waiver system would also be welcome.

Question 3: Is there any reason that your organisation would not be able to comply with the proposed IGR within six months? Please explain your reasons

- 2.20 CILEx expects to be able to achieve compliance with the new IGRs within the specified six month period providing waiver applications for shared services are able to be considered and receive approval within that time frame, in particular

¹⁰ Perhaps by jointly obtaining quotes for comparable services, as referred to on page 31 of the guidance

¹¹ Rule 16

in relation to premises and IT systems. For this reason, a greater degree of clarity on the issues referred to above is key. This is particularly the case with getting the waiver process right; inevitably some aspects will be more complex and harder to achieve and could result in increased costs if rushed. Having waivers to fall back on if needed will help the management to compliance. Without that, six months would be very ambitious.

- 2.21 The need to recognise flexibility is crucial. Even with the best planning in place, there is always the possibility of unforeseen challenges derailing project timelines in ways that could not be reasonably anticipated. The likely resources required to make the changes necessary changes for compliance is one such area of risk; see below.

Question 4(a): Beyond the usual resources allocated to compliance with the IGR what, if any, additional resource do you anticipate you will need: (i) to assess compliance with the proposed IGR and then to make changes to come into compliance, if any are required; and (ii) to comply with the IGR on an ongoing basis?

- 2.22 CILEx is committed to ensuring any changes should not lead to greater costs either for the organisations themselves or, by extension, by putting pressure on PCF levels. We do anticipate significant staff time being required to fully develop plans to deliver the intended changes including to support waiver applications and to manage the transition away from dual roles and shared services however we are seeking to do this within existing budgets.

- 2.23 We also recognise though that this will be an area which both the RB and AR will have to monitor and manage closely. In some ways, the new IGRs introduce a greater formality to processes which CILEx and CILEx Regulation are already undertaking in relation ensuring regulatory independence is maintained and regulatory resources guaranteed; however, processes and management take time and the greater degree of specificity introduced by the IGRs in relation to anticipated documentation and evidence etc¹² will inevitably take an initial period of bedding in.

CILEx is confident that the IGR-promoted changes will though be manageable and cost-effective on an ongoing basis.

Question 4(b): Do you agree with our assessment that the cost of compliance (which includes the costs of dealing with disputes and disagreements) will reduce under the proposed IGR?

¹² For example, those specified in the last paragraph on page 33 of the guidance

- 2.24 Inevitably, at the early stage, there are likely to be clarifications and differences in interpretation of the new IGRs which will need to be worked through and a significant number of waiver applications given the existing levels of shared services across the regulators. In the medium to long term however, we believe the new IGRs provide a clear and solid framework for ARs and RBs to work within. This is however contingent on attaining the greater level of clarity in the rules and guidance referred to above. Without that, rather than reduce the instances of AR's/RBs going to the LSB with disputes, this risks increasing that likelihood as the rules are capable of different interpretations.

Please provide details of your assessment of the costs and actions associated with the initial assessment of compliance under the transition period and your estimation of the difference in the ongoing cost of compliance with the proposed IGR compared to the existing IGR

- 2.25 CILEx and CILEx Regulation have already begun more detailed financial modelling which is being tested and analysed at our respective Boards with the support of our financial teams. As stated, we anticipate that this will demonstrate that both assessing and then implementing the changes required to achieve and maintain compliance on an ongoing basis will be manageable within existing PCF levels.
- 2.26 The accuracy of those financial estimates will only be properly tested during the transitional period, we therefore intend to share more detailed financial modelling as it is developed and on an ongoing basis though that period should this vary from original estimates.

Question 5: Please provide comments regarding equality issues which, in your view/experience, may arise from implementation of the proposed IGR

- 2.27 CILEx does not expect any specific equality issues to arise as a consequence of changes made to ensure compliance with the new IGRs. As above however, we remain sensitive to the need to keep regulatory costs low and the potential for certain groups to be disadvantaged and will be monitoring and managing this closely.

3. Conclusions

- 3.1. CILEx is committed to and supports the principles enshrined in the proposed new IGRs. Indeed, our Board is committed to achieving the greatest degree of regulatory independence/separation possible with the ultimate goal of achieving complete structural separation of regulatory functions guaranteeing independence.

- 3.2. Greater clarity in the language of the new rules and guidance will enable this; without that clarity, particularly in relation to the residual role of the AR, there could, initially at least, be an increased need for LSB intervention to settle differences in interpretation.
- 3.3. CILEx remains confident that these enhancements to the proposed IGRs can be achieved, would be pleased to assist the LSB in making them and working toward attaining the ultimate goal of true regulatory separation/independence.

For further details

Should you
require any
further
information,
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