

CILEX response to request from members under Bye-Law 27

Resolution One

(1) That the Chair and Members of the Group Board, Members of the Professional Board, including Sub-Committees, and Chief Executive Officer be called upon to account to and provide the Members of The Institute with a full and detailed explanation of the following matters:

a. Explain why The Institute failed to undertake correct accounting and reconciliation in regard to Practising Certificate Fees paid by Members between the period 2017 -2021.

The CILEX auditors both in their audit report and in communication sent to the LSB as part of its investigation confirmed that the accounts were correct and accurate with no mis-statements. Funds received and paid to CRL were correctly stated in all sets of accounts. In all years CRL received its full budget (amount stated in PCF submission and Practising Certificate Fee notice) from CILEX in full compliance with the PCF Rules. These facts are not disputed by CRL. Furthermore, CRL's auditors also declared in their audit reports that the accounts were a true and correct statement.

The dispute with CRL related to the distribution of PCF funds between CILEX and CRL in specific circumstances where the number of Fellows paying for a Practising Certificate fluctuated from the number forecast in the PCF submission.

Prior to the dispute in 2022, CILEX held and managed the PCF Balance (the credit or deficit in funds arising from any fluctuation in practicing Fellow numbers). This arrangement (which had been in place since the incorporation of CRL) meant CILEX protected CRL against the risk of a deficit in funds having been received and its regulatory budget therefore being reduced. Any funds received above budgeted amounts were held in the reserve and used to offset deficits in PCF balances carried forward from previous years in which Fellow numbers were below projections and to allow regulatory costs to be funded without disruption arising from debtors (those individuals or organisations who failed to pay the fees on time or utilised payment plans). Essentially, under this arrangement CILEX not CRL bore the risk to its budget.

In 2022, following CILEX having informed CRL of its intention to consider a change in delegation, CRL requested that this arrangement cease and a reconciliation exercise be undertaken of all fees collected between 2017-2022 with a redistribution of funds held in the regulatory reserve. CILEX conducted this exercise and shared its calculations and accounting records with CRL. CRL disputed the figures and the matter was referred to the LSB.

In its findings, the LSB concluded that it was a matter that should be resolved via CILEX and CRL's auditors but required that a reconciliation exercise related to PCF funds received versus those budgeted for be conducted each year going forward. CILEX voluntarily agreed, noting it had not been a requirement during the period in question (2017-21) with new LSB PCF rules having only come into effect in 2021. This arrangement has subsequently been implemented in collaboration with CRL.

b. Explain why The Institute failed to account to the Members of the Institute in regard to the safeguarding of Members funds during the period 2017 - 2021.

No funds were at risk or were mis-used and were allocated in accordance with those activities specified in the PCF application approved by the LSB and subject to independent audit. The audited accounts were published in full at each AGM, thereby satisfying CILEX's obligations to its membership. CILEX and CRL also provided data to the LSB on an annual basis with regard to the number of Fellows with practicing certificates, the allocation and use of PCF funds and the reserves held by each organisation.

The dispute by CRL was on the basis it wanted to take direct control of the regulatory reserves (both PCF reserve and contingency reserve) held by CILEX, allowing it the freedom to use the money without any visibility to CILEX or CILEX Board oversight governance regarding use within the permitted purposes for which it was held.

CILEX has a duty under Section 28 of the Legal Services and Rule 3 of the LSB Internal Governance Rules, to assure itself that its delegated regulator, currently CRL, is complying with Section 28 of the Act.

Section 28 and LSB IGR Rule 3 place CRL under a duty to provide sufficient information as requested by the Approved Regulator to be assured. CILEX therefore wrote to CRL seeking assurance that it would only use the funds for purposes for which the funds were collected (those activities specified within the PCF submission) and the specific ring-fenced pots held within the contingency reserve (compensation fund claims, appeals and ability to maintain 6 months operating costs in circumstances where PCF fee approval was delayed).

Sufficient assurance was not provided by CRL. Specifically, the CRL Board did not provide assurance it would not mis-use the funds on unwarranted legal action against either CILEX or the Legal Services Board or that it would remain compliant with the CILEX Group Reserves Policy applicable to all CILEX Subsidiary Companies.

c. Explain why The Institute withheld the contingency reserve and Practising Certificate Fees knowing that this would impact upon the regulatory functions of CRL impacting upon its ability to meet its regulatory functions in the interests of the public to ensure public confidence in the members of The Institute.

CILEX did not withhold access to any funds from CRL required for the discharge of its delegated functions. CRL has received its full budget every year, as is evidenced in CRL accounts. Furthermore, CILEX has provided additional funding to CRL by way of underwriting the Compensation Funds to the value of £250k and an additional sum of £50k to allow CRL to implement retention bonus's to retain its staff, in response to requests made by the regulator.

CILEX has at all times, facilitated CRL's access to regulatory reserves held by CILEX for use for legitimate purpose – i.e. the permitted uses of the funds as stated in the Reserves Policy.

The dispute related to a request CILEX received from CRL to take direct control of the regulatory reserves and move it out of the safety of the ring-fencing and under-writing provided by CILEX through its Barclays portfolio into the CRL bank account.

In response to the request CILEX (legitimately as acknowledged in the LSB Investigation Report) sought assurance from the CRL Board that it would only use the funds for legitimate purpose as specified in the PCF Rules and submission and the CILEX Reserves Policy. This assurance was not provided.

The CILEX Board therefore remained concerned that CRL's intention was to use the funds for activities outside the scope of the permitted purposes of the reserves funds, namely legal fees in pursuit of injunctions against CILEX to block CILEX's public announcement of its review of its regulatory delegation and a Judicial Review the LSB determination that CILEX has the right to review and change its delegation. This activity is not in line with the permitted purpose of either the contingency reserve or PCF funds. The CILEX Board has a duty to protect the funds from mis-use and therefore informed CRL and the LSB that it remained unsatisfied.

Despite this, at all times CRL still had access to both its full budget and reserve funds for those purposes specified as legitimate use. There was, therefore, no impact on CRL's ability to conduct its delegated regulatory functions.

d. Explain why the recommendations to be implemented by the LSB in their report of 18 April 2023 have not been published, and rectify the requirement to do so within 21 days of the date of the Special General Meeting.

The response to the LSB Investigation Report, Undertakings and associated action plan agreed by CILEX and CRL was submitted to the LSB and monthly update reports on progress are also provided to the LSB. The decision to publish this material rests with the LSB.

- e. **Explain why The Institute refused to take part in a joint declaratory relief application with CRL to answer the lawfulness of actions taken by The Institute in pursuing deregulation and redelegation to SRA incurring all associated costs so far.**

Based on independent advice, the published position of the LSB and discussions with Government, CILEX is satisfied that it has the legal right to review and, if following consultation it considers it to be in the public interest, amend, its delegation. There is, therefore, no justification to spend what is estimated to be in excess of £250k on an unnecessary legal process.

Furthermore, due to CRL being a subsidiary company of CILEX, CILEX would also carry liability for CRL's incurred legal costs which would double the financial exposure. CILEX does not consider this to be a legitimate use of regulatory funds.

- f. **Itemised breakdown of all sums spent and forecast to be spent by The Institute relating to and in connection with the proposed change of regulator from CRL to the SRA to be published in written form for the benefit of all members.**

This detail was provided to the AGM and is published here: [Annual Report \(cilex.org.uk\)](https://www.cilex.org.uk/annual-report)

- g. **Provide copies of full minutes of the CILEX Board meeting dated 19 July 2023 and the resolution dated 26 July 2023 referred to in footnote 9 of the recent consultation do be published for the benefit of all members.**

All relevant information, including minutes will be published, alongside the consultation outcomes and analysis when CILEX makes its decision and any application to the Legal Services Board.

Resolution Two

- (2) **There be an electronic vote and all members of The Institute shall be eligible to vote in relation to whether re-delegation of regulation is in the public and member interest and should pass from CRL to the SRA. Such a vote shall require a two-thirds majority in order for regulation to pass from CRL to the SRA.**

As the Approved Regulator, CILEX is not permitted under the Legal Services Act 2007 and LSB Internal Governance Rules 2019 to allow member interest to prejudice its decision making with regard to its delegation (or any other regulatory matter). Furthermore, it must keep separate its representative activities (those related to member interest and its role as a professional membership body) from those as an Approved Regulator (LSB IGR Rule 1).

Rule 1(3) of the IGRs places a duty of CILEX, as the Approved Regulator to "periodically review" its delegation arrangements. Each year as part of its declaration of compliance CILEX must confirm that it considers its arrangements to continue to satisfy Section 28 of the Legal Services Act 2007 and to meet the regulatory objectives and public interest. In reviewing its delegation and considering the alternative option of regulation by the SRA, CILEX is discharging this duty.

Therefore, if CILEX were to agree to the proposed resolution and conduct a vote (which is a representative and member interest activity), it would be in breach of its statutory duties and non-compliant with the regulations that govern it. The LSB have advised both CILEX and CRL that 'member preference' is not a valid basis for CILEX, as the Approved Regulator, to make its decision. Conducting a member vote and using the outcome to inform CILEX's decision regarding its delegation would be allowing its representative function and member interest to prejudice discharge of its public interest Approved Regulator role. The proposed resolution is not therefore valid nor permissible.

The CILEX consultation provides the regulated community, alongside all other stakeholders, the opportunity to express their views on both the public interest outcomes and potential impact on individuals, entities, consumers and the wider legal services market. This will enable the decision to be made on the basis of the public interest case and in full compliance with the Legal Services Act 2007, LSB Internal Governance Rules 2019 and associated Change to Regulatory Arrangement Regulations.