RUSSELL-COOKE | SOLICITORS

Enforcing Regulatory Standards in a Liberalised Market

10 May 2012 – Event Summary

Lord Neuberger opened the event, highlighting that regulation has taken centre stage in a fast-changing society and fast-changing profession. He identified a number of factors which have influenced this:

- the increased commercialisation and profit orientated ethos of the profession, which encourages efficiency and frankness but leads to tension in relation to maintaining professional standards
- the increased importance and supremacy of the consumer – there is a difference between the short term benefit for an individual consumer and the long term benefit for society
- the increasingly pervasive concern with process, so that process is sometimes seen as equally important as outcome – partly driven by a desire for quantitative measurement (perhaps this was part of the problem with financial regulation?)
- a fast changing world, with improved communication in particular – change leads to uncertainty and confusion, which means people feel the need for more regulation
- the culture of complaint – if something goes wrong it must be someone's fault

In his view the legal profession stands for the rule of law. A thriving legal profession that commands respect is essential to enable people to enforce their rights. An important feature of commanding respect is effective regulation. Effective regulation means regulation that is transparent, simple, effective and as cheap as possible.

He considers that activity based regulation should not involve more than one regulator regulating the same activity. This leads to either unnecessary duplication or differing standards. Competition among regulators is "a highly questionable and unhelpful concept". In his view it is important that the profession and the regulators regard themselves as being "on the same side" because both want the same thing – an effective, respected legal profession.

David Edmonds gave the keynote speech[1] focusing on standards and quality, and the question of ethics.

David began by reiterating the importance of consumer interests in the legal services market, the importance of the rule of law and the risks of market failure to both consumers and the public interest. He set out his view that the benefits of liberalisation should not just accrue to those who are interested in "new ways of doing things" and/or alternative business structures – but should be capable of being felt more widely across the sector, including to those who wish to retain "traditional" models of delivery, providing those models are capable of being sustained. He noted that legal services providers have always been under competitive pressure – and that many lawyers spend their careers advising other businesses on how to compete.

The two main themes for the speech were: what should we be seeking from a liberalised market? And what can regulation – at both the macro (oversight) and micro (frontline) level – be doing to make sure that standards are not just maintained but improved?

John Wotton responded to David Edmonds. He agreed that the interests of consumers are of central importance in the regulation of the legal sector. The term "consumer" alludes to the economic relationship between the lawyer and the person he serves, while the term "client" refers to the professional relationship. The two terms are not in conflict.

In his view, the regulatory objectives in the Legal Services Act, taken as a whole and in a balanced way, ought to protect the legal profession's mission to serve its client and society at large.

The benefits of liberalisation should accrue to consumers, not providers. The most efficient and responsive practices will survive regardless of structure. Non-lawyer ownership is unlikely to be a magic bullet on its own, but it will allow in established consumer brands which will make parts of the market even more competitive.

He also agreed with David Edmonds that the changes were likely to be evolutionary rather than revolutionary. Elements of supply and demand are likely to remain quite "sticky". Lawyers may be reluctant to move to new entrants, and clients may be unwilling to move from a trusted adviser. Existing firms have in many cases extracted most of the available efficiencies under the competitive pressures that have applied up until now. Innovation will not necessarily be driven by liberalisation, but by demand for legal advice and representation from ordinary people which will not be publicly funded. New entrants may meet some of that need.

He applauded the steps taken by the SRA to deal with ABS licensing, the assigned risks pool, professional indemnity insurance and the Compensation Fund and the rules applying to international practice – although the Law Society does not necessarily agree with every decision. The Society wants the non-lawyer element of the ABS licensing process to be thorough, although it would like a more predictable timetable. All applicants should be entitled to a reasonable standard of service from the regulator.

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[1] The full text of the speech is available on the Legal Services Board website: http://www.legalservicesboard.org.uk/news_publications/speeches_presentations/2012/20120510-david-edmonds-russell_cooke_speech.pdf

It is right that regulation should not be prescriptive as to ABS structures, and that the market should decide. However, he noted that the freedom that regulation offers is the element that our civil law colleagues find most difficult to stomach – one cannot say in advance what will be permitted and what will be prohibited. He is concerned that the reaction of bar organisations in major EU and trans-Atlantic jurisdictions means they will do all that they can to resist UK ABS establishing or remaining on their patch – it will be quite a job to overcome that resistance.

Under the structures we have in the Legal Services Act, the assumption is that the approved regulators rather than the Legal Services Board will be in the driving seat. He agreed that entity based regulation should assume ever greater importance and indeed is essential for ABS.

At this stage, outcomes focused regulation is more attractive in theory than in practice. While David Edmonds highlighted the length of the various professional codes, it could be argued that it is OFR that has led to the increasingly length and complexity of professional rules. If OFR were genuinely liberalising, one would expect firms to welcome it. However, most firms report that they find themselves achieving very high one off costs to achieve compliance and it would be surprising if the on-going costs were not considerably higher than under the previous system.

John agreed with David about the importance of professional ethics and is keen to see it deeply embedded in education and training from the outset, supported by a broadly based legal education and training process and strong professional culture that will enable lawyers to understand ethical issues in a wider context.

He emphasised that he is a strong advocate of the continuation of regulation by approved regulators, independent of government and quangos and accountable to those they regulate for their performance and use of resources, while at the same time being accountable for performing their duties under the Legal Services Act. The SRA have questioned whether it is in the public interest to retain the Legal Services Act model of a set of approved regulators based on the pre-existing professional bodies. One of the key issues with that model is the risk of regulatory competition leading to a “race to the bottom” in terms of costs and standards. However, there is no sign of that yet. The SRA code and its standards of enforcement remain rigorous and there is no sign of a mass flight to other regulators. He acknowledged the need to avoid inconsistency and confusion for clients where more than one regulator regulates the same activity and suggested common codes are the right way to address this, particularly in relation to conveyancing where the rules of the Council for Licensed Conveyancers are in his view “indefensible”. Solicitors do lots of different types of work – there would be regulatory mayhem if a practitioner had to move from one regulatory framework to another during the course of a working day. The siren call for a single regulator for each activity is workable only if a large part of the flexibility and career development we currently enjoy in the legal sector were to be lost.

The Law Society welcomes the recommendation by the LSB to make will writing and estate administration a reserved activity. There should be a common standard for all providers. Any competent organisation offering will writing and estate administration ought to be able to meet the current criteria set by the SRA for ABS. They could operate perfectly well under the current rule book.

Maura McGowan QC began by asking “Who regulates the regulators”? The Bar welcomes effective and efficient regulation, but like any other profession it can only be effectively regulated by a body that understands what barristers do and why they do what they do. Regulation has to fit its purpose. It cannot be right to reform the legal profession to fit in with “pre-formed” regulation. It is essential that the relationship between the profession and the regulator is properly defined, and it was by statute.

She highlighted the regulatory objectives include protection the public interest, and separately protecting the interests of consumers. Also, fundamentally, they included upholding the constitutional principle of the rule of law and maintaining professional principles. She challenged the notion that earlier days of self-regulation were based solely or primarily on self-interest.

She highlighted section 4 of the Legal Services Act, which says that the LSB should assist in the maintenance and development of standards of regulation and standards of education and training. It is difficult to reconcile that statutory objective with the stated desire of the LSB to reform and modernise the legal services marketplace. It is a moot point whether it needs modernising or reforming, but it is a different question whether it is the role of the LSB under the current legislation to do so.

The LSB’s desire to reform is particularly evident in relation to education and training, where she maintained that the Bar has an impressive history of self-regulation.

The Bar continues to seek to regulate its own standards, but accept entirely that this is not solely within their grasp any more, and accept and welcome the assistance that is offered. The Bar Council sets out to improve.

She highlighted the scheme of advocacy standards developed by the Bar Council. This was not easy, but was made all the more difficult by the imposition of unrealistic deadlines by the Legal Services Board and ultimately a refusal to protect the public, the courts and consumers by permitting the accreditation of advocates in the Crown Court who do not even consider themselves competent to conduct a trial.

The LSB has caused a fundamental review of legal education and training from university onwards. It is an enormous task which will take a long time and cost a small fortune. It seems a long way from “assisting” an approved regulator. The LSB has said that the current system is not fit for purpose but has not given the detail of why, so not much assistance there. It appears to want to bring about change because it can, rather than observe its statutory duty to assist the profession and maintain and develop standards.

The Bar accepts regulation, originally from within and now from outside. But that regulation must comply with the law itself, and not be so onerous as to prevent barristers from practising with independence and integrity. It might be said that it is the liberalisation of regulation that is required. The “market place mentality” should play no real part in the administration of justice.

She emphasised that professional practice is centred around the rule of law – rules matter to lawyers, and the letter and spirit of the rules matters equally. The spirit of the rules only emerges after a rigorous study and analysis of the letter itself. It is the process of law that matters, and matters more than the outcome.

In her view, those who regulate the profession now must understand that lawyers are not creators or producers of anything, not even the outcomes. An outcomes focused system of regulation does not make sense in a profession which has duties to the court, the rule of law, the public, the client – all of which are inter-related but no one of which has supremacy. How realistically does one judge an outcome?

She agreed that the profession must run itself efficiently. It has a moral duty to account for the money paid to it, particularly from public funds. That duty to account does not make practitioners a business or commercial organisation in the true sense. Advising people how to compete legitimately is not the same as advising them how to compete. It is difficult to find a parallel in the world of commerce – like health and education, law ranks above purely commercial considerations. Law is fundamental to the health of the nation state.

She emphasised that the Bar invites proper regulation. For example, if a patient goes to a GP and is referred to a consultant, the client believes that the GP is applying professional judgment and integrity in selecting the best person for the job. How would the patient feel if they were told that the consultant had paid 25% of his fee back to the GP and that they were entrusted to that consultant only because he was willing to buy the case? How would we as taxpayers feel if we found out that of the £100 that was claimed as a fee, £25 was in fact spent buying a case. The Bar have always regulated against that and look to the LSB to support and assist them in that. However, the LSB say that apparently there isn't a problem, they don't see the harm. That is not in the public interest, and is not enforcing a regulatory standard. It is not in the interest of the profession and not in the interests of the administration of justice. Many lawyers have developed an international anti-bribery and corruption practice in recent years, spreading the word that the giving of a gift or money in exchange for a contract or job is wrong. She asked for the assistance of the LSB to put this into practice.

Questions

The following topics were raised in the question and answer session:

- What are the key lessons for regulation in other sectors – particularly financial services?
    - DE emphasised that it is important to move away from ticking boxes and look instead at outcomes; also to ensure accountability for decision making.
    - JW felt it was important to remember that it is still possible to enter the legal profession on a small scale and expand if ideas are successful. Financial services regulation is more suited to large organisations which can support a complex compliance function. We need to avoid a burden of regulation that is incompatible with small scale practice.
    - MM felt that what is required to avoid "one size fits all" is greater flexibility in regulation which can be adapted to different structures. That does not mean that the process and procedure does not matter. A balance between flexibility and certainty is required.

- How can the success of outcome based regulation be measured?

    - DE said he could not predict the world in 10 years time. A range of measures could be looked at, including numbers of complaints, referrals by SRA to the SDT, whether there is a proliferation of different businesses offering innovative services to the public, whether large crises such as the Miners' Compensation Scheme are avoided.

    - JW felt it was right to challenge how far outcome measures can be used in the legal sector in contrast to, for example, health. Clients should be fully informed at the outset what advice they will receive and at what cost – that is likely to lead to fewer complaints.

    - MM questioned whether that was right in an age of consumer complaints (which has become an industry in itself). In crime, there is always a dissatisfied party, but that is not necessarily a reflection on the practitioner and does not accurately or fairly represent the professional or ethical standards of the individual.

    - The Chair of the Legal Ombudsman commented that she would be concerned if the number of complaints was used as a measure – the appropriate measure is those cases in which a remedy is required. Legal professionals should not be scared of referrals to the Ombudsman. It may mean that their judgment is endorsed. ADR mechanisms used by ombudsmen are positive. Sometimes the best firms have more complaints because they are better at signposting and are not afraid of the Ombudsman.

- What is meant by "consumer interests" – in a global sense this might mean the rule of law, at an individual level it might be price?

    - MM felt that the "consumer interest" is difficult to define, and was beyond the draughtsman of the Act. The word does not make a great deal of sense in the legal sector.

    - JW said that the "consumer interest" is the desire that the legal sector should deliver as much as possible of the demand for legal services in the most efficient way. There is nothing in the legal sector to suggest a disconnect between the interests of the individual consumer and society as a whole.

    - DE asked what was wrong with commoditisation if people can have access to services and a cheaper price (and quality can be maintained)? Lots of citizens find law off putting and unaffordable. His Consumer Panel speaks to consumers. They looked at referral fees and found no detriment in terms of the consumer or public interest in many areas. The public wants the highest standards and the rule of law. On many occasions, consumers want a service cheaply and efficiently delivered.

    - MM suggested that the Consumer Panel might not be asked the right questions. How is buying a case in the consumer or public interest? Commoditisation may work in some areas, but not all.

    - JW emphasised that the Law Society remains opposed to referral fees. There is a concern about the sustainability of the supplier base in some areas where

public funding is being withdrawn. Interventions will be required to meet this demand and enable people to enforce their democratic rights.

- A Financial Ombudsman Service representative agreed that numbers of complaints is not a good measure. Debates about the meaning of "consumer" are also prevalent in financial services. More focus on ADR is required – perhaps we need less lawyer involvement?

- Why does the Legal Services Board reject the suggestion that there should only be one regulator of advocacy?

    - DE said that he was clear that regulators should get together and create a mechanism whereby consistent standards are applied, which he feels should be achievable.

- What should a regulator be doing – for example on education and training are they straying beyond their remit?

    - MM acknowledged that the LSB has a role to play, but suggested that approved regulators need more specifics in relation to why the current system is regarded as "not fit for purpose". The LSB should be assisting not simply calling for a root and branch review without any direction.

    - JW felt that it is time for a thorough-going review, but that it should not be rushed as things are changing rapidly. The division between the branches of the profession probably diverges too early on.

DE said that when he regulated of telecommunications, he coined the phrase "walking backwards slowly" to refer to one resistant part of that sector. He felt that a significant part of MM's comments could fall into that category. The Bar in a number of areas has gone back to futile arguments about what the legislation says. The education review came out extensive discussion with professional bodies and regulators. He had made a speech 18 months ago suggesting review but never said that the existing system is "not fit for purpose" – we don't know, that's why a review is needed. The LSB is not doing the review. This is being done independently under supervision of two Chairs – one appointed by the BSB and one by the SRA. The LSB has assisted by organising seminars to get wider views. He was proud of the work the LSB had done on education and training, and of the work on ABS and increasing diversity in particular. He felt that the LSB has a good understanding of the Bar and the legal system, and that everyone is given an opportunity to provide their views.

For further information, please contact:

Michael Stacey
Trainee
+44 (0)20 7440 4828
Michael.Stacey@russell-cooke.co.uk