Government Response to the Report by the Joint Committee on the Draft Legal Services Bill, Session 2005-06

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Foreword

I would like to thank the Joint Committee for their report on the draft Legal Services Bill. I am very grateful to the Committee for their swift consideration of the issues despite a challenging timetable.

In their Report, the Committee made over 50 recommendations. The Government has considered these very carefully over the last two months, and in a few cases that consideration in ongoing.

The proposals which form the basis of the draft Legal Services Bill have already been the subject of lengthy and detailed analysis. They have also been the subject of several wide-ranging public consultation exercises. The process essentially began in 2001 following a report from the Office of Fair Trading (OFT)[1] which indicated there were a number of potentially unjustified restrictions to competition in the legal services sector. As part of its response to the OFT Report, the then Lord Chancellor's Department carried out a public consultation exercise[2].

In its report following consultation[3], the Government concluded that the current regulatory framework in England and Wales was *"outdated, inflexible, over-complex and insufficiently accountable or transparent"*. The Government also concluded that a thorough and independent investigation without reservation was needed. Sir David Clementi was appointed to conduct that Review and in December 2004[4], following his own public consultation in March of that year[5], Sir

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[1] "Competition in Professions", Office of Fair Trading, March 2001

[2] "In the Public Interest", Lord Chancellor's Department, July 2002

[3] "Government's conclusions to In the Public Interest", Department for Constitutional Affairs, July 2003

[4] "Report of the Review of the Regulatory Framework for Legal Services in England and Wales", Sir David Clementi, December 2004

David published his report. Details of the consultation papers are all available on the Department for Constitutional Affairs website.

If there has been a single key theme emerging from the long and detailed process of developing our policy, it has been that the interests of the consumer must come first - whether it is from the perspective of the Office of Fair Trading: "*The aim of the Office of Fair Trading is to make sure that markets work well - for the ultimate benefit of the consumer*"[6]; the views of the Independent Reviewer: "*In a number of ways, in particular through the LSB as a regulator which counts consumer protection amongst its statutory objectives, and through the OLC as a single complaints body independent of the existing professional bodies, the new system should better service both the public and consumer interest*"[7]; or the Government's own White Paper: "*Our vision is of a legal services market where excellence continues to be delivered; and a market that is responsive, flexible, and puts the consumer first*"[8]

The pre-legislative scrutiny undertaken by the Joint Committee has been a final, important step in ensuring that any legislation the Government introduces to Parliament takes proper account of a range of vital considerations such as ensuring that the legal professions remain properly independent, but without losing sight of the primary objective of putting the consumer first.

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[5] "Consultation Paper on the Review of the Regulatory Framework for England and Wales", Sir David Clementi, March 2004.

[6] "Competition in Professions", Office of Fair Trading, March 2001

[7] "Report of the Review of the Regulatory Framework for Legal Services in England and Wales", Sir David Clementi, December 2004

[8] The Future of Legal Services: Putting Consumers First, DCA, October 2005

Summary of proposals in the draft Bill

The Legal Services Bill was published in draft and introduced to Parliament on the 24 May 2006. The draft Bill seeks to establish a new regulatory framework that will put the interests of consumers first. The main provisions outlined in the draft Bill propose:

- The establishment of a Legal Services Board (LSB) as a single oversight body, independent from both Government and approved regulators, to provide a more consistent and coherent framework of regulation.

- The establishment of an independent Office for Legal Complaints (OLC) as a body with statutory power to handle complaints concerning providers of legal services, and to award redress to consumers in appropriate circumstances. It will address concerns about the quality, independence, and consistency of complaints handling by the legal professions.

- Alternative Business Structures (ABS), which will enable lawyers and non-lawyers to work together on an equal footing to deliver legal and other services in ways that better meet the needs of consumers. External investment will be possible, and new business structures will give legal providers greater flexibility to respond to market demands. Licences will be conferred by licensing authorities and safeguards will be put in place.

Response to Recommendations

In the following passages, the paragraph numbers used by the Joint Committee at Chapter 1 of their Report have been used as a basis for setting out each of the recommendations made by the Joint Committee and the Government's response.

Chapter 2: Introduction and Background

Recommendation 1

Given the significant impact of the Bill's provisions - it is the first attempt to draw the entire legal services market within one regulatory framework - and the complexity of some of the issues involved, we believe that the priority should have been to ensure that the Committee had sufficient time to scrutinise the draft Bill effectively. It is in the interests of both the executive and the legislature that the provisions of the Bill are right. The timetable for our inquiry has not allowed us or the Government to realise the full potential of the pre-legislative scrutiny process. We reiterate the recommendation of the Joint Committee on the draft Charities Bill that any future Committee should have at least 12 sitting weeks in which to consider and report on a draft Bill and we specifically draw this recommendation to the attention of the Leaders of both Houses and the Commons Liaison and Modernisation Committees.

Government Response

The Government always tries to give maximum time for scrutiny, and as the Guide to Legislative Procedures sets out, "Generally a committee will need a least three to four months to take evidence and report (not including long recesses)". While this amount of time will not always be needed, it does remain the Government's policy to work on this basis wherever possible. With regard to the draft Legal Services Bill, while it was in the event published a little later than originally intended, there had been much public consultation and public scrutiny of the proposals, and one of the Government's aspirations is that consumers should see real benefits from these important reforms as quickly as possible. However, the Government also recognises that the legislation is complex and that there is a tension between early delivery and proper scrutiny.

The Government did take steps to ensure that the Joint Committee was in place before the draft Bill was published, so that no further time was lost and the Committee could begin work as soon as possible. The Department for

Constitutional Affairs also took steps to brief Committee staff before the members were appointed. In doing this I believe the Government has, in the circumstances, struck a sensible balance between early delivery and proper scrutiny.

Chapter 3: The Objectives of Regulation

Recommendation 2

We note the shift in emphasis in the Government's approach to reform of the legal profession - the change in focus from the public interest to the consumer interest - reflected in regulatory objective (c). The public interest and the consumer interest do not always equate to the same thing, particularly in matters of law, and we are concerned that the necessity for a public interest criterion has been lost as the reforms have developed. We therefore recommend that objective (c) should be redrafted to read "(c) Protecting and promoting the public interest and the interests of consumers".

Government Response

The wording in the Bill follows that recommended by Sir David Clementi in his 2004 report, which stated that there should be an objective to protect and promote the consumer interest. On the public interest the Government considers that, taken as a whole, the seven objectives set out at Clause 1 of the draft Bill will protect and promote the wider public interest, not only the interests of consumers of legal services. For example, all partners in the regulatory framework will be under a duty to act with independence and integrity. It is right that the consumer is at the heart of these reforms and that their needs are central to the provision of high quality, effective legal services. The Government believes that it is in the public interest to do this.

Nevertheless, we **agree** that the public interest should be protected and promoted, and that this should be reflected in the Bill. However, as the Joint Committee has highlighted, the public interest and the interests of consumers are not always the same, so we do not think it appropriate that the two should sit within the same objective. We believe that the matters listed in clause 1 do reflect the need of the Board to have regard to the public interest and we will ensure that it is more obviously brought out.

Recommendation 3

We recommend that the professional principles set out in clause 1(3) of the Bill should be amended to include the duty to the court explicitly in the professional principles.

Government Response

The Government **agrees** with the Committee that the duty to the court is vital and we are giving careful consideration as to how the duties presently set out under clause 141 can be made more prominent.

Recommendation 4

We recommend that the independence of the profession should be included explicitly in the regulatory objectives and that objective (e) should be redrafted to read "(e) Encouraging an independent, strong, diverse and effective legal profession."

Government Response

The Government **agrees** with the Committee that independence of the profession is a vital element. While we consider that this is already achieved under the professional principles at (g), we see the benefit in terms of clarity of placing an explicit objective on the face of the Bill.

Recommendation 5

We note the Government's approach that the regulatory objectives are not explicitly ranked in order of importance in the draft Bill. However we are concerned that this has the potential to create uncertainty and confusion in how they will be applied and we note in particular the approach taken by the OFT in evidence. If it is not made explicit on the face of the Bill that they are not ranked in any particular order, it is inevitable that they will be seen as listed in order of priority. We therefore recommend that the Explanatory Notes to the Legal Services Act should make it explicit that the objectives are not listed in order of importance.

Government Response

The Government agrees the need for clarity in the application of regulatory objectives. While the Explanatory Notes to the draft Bill already state that regulatory objectives are not listed in any particular order, the Government **agrees** that they should make this more explicit. The Notes will be revised to reflect this.

Recommendation 6

We agree that the Legal Services Board (LSB) should seek to identify and disseminate information about best practice to help drive up standards. We would like to see the LSB taking on an educative function within the resources planned for it under the draft Bill.

Government Response

The Government **agrees** that the LSB should take on an educative function, and considers that such a function should relate both to members of the public and the legal profession. We envisage that the LSB will carry this forward by encouraging consumer awareness programmes to continue best regulatory practice amongst

authorised bodies whilst also maintaining and developing the standards in education, training and conduct of persons authorised to carry out reserved legal activities.

Chapter 4 - The New Regulatory Framework

Recommendation 7

We recommend that the draft Bill should be amended to require approved regulators to separate fully their regulatory and representative functions. This separation should require all regulatory decisions to be taken by an independent regulatory arm; that arrangements must be made to ensure the regulatory arm has the resources it reasonably requires; and that the regulatory arm should be entitled to seek the intervention of the LSB should it feel that any action or inaction on the part of the relevant professional body is damaging to its independence or effectiveness.

Government Response

The separation of a professional body's regulatory and representative functions is a central feature of the regulatory model proposed by Sir David Clementi (his Model B+) and adopted by the Government. This will ensure transparency in the way regulatory and representative functions are discharged, and lead to greater consumer confidence. While the Bill effectively "passports" existing regulators into the new framework, clause 25(1)(d) provides a power for the Legal Services Board (LSB) to take action where it determines that an approved regulator has failed to adequately separate its regulatory and representative functions. While it is important that the LSB should have the ability to exercise discretion in reaching judgements about the nature of any separation of these functions (e.g. it may not be practicable to require smaller approved regulators to operate the same degree of division as the larger ones) this remains a key aspect of the Government's proposals. The Government therefore **agrees** that the separation of these functions is a central feature and is exploring how the existing provisions might be revised to make greater provision for ensuring that the LSB is satisfied with the regulatory and representative arrangements for all existing and future authorised regulators before they become authorised.

Recommendation 8

We attach importance to the continuing independence of the legal profession and we are concerned to ensure that the constitutional significance of independence is recognised. Public confidence in the integrity of the profession will not be sustained, nor will its international significance continue, if there is the perception that its independence is jeopardised in any way. We wish to ensure that the framework proposed by the draft Bill will not damage the independence of our legal profession. We cover some aspects in more detail below.

Government Response

Not only are legal services crucial to people's ability to gain access to justice; the international success of our legal profession contributes significantly to the UK's economy. While the Government wants to see continued improvements in quality and international competitiveness, it **agrees** with the Committee's view of the need for the profession's continued independence.

Recommendation 9

Adherence to the Nolan principles should underpin all Government appointments. In the case of the chairman of the Legal Services Board - the person in charge of regulating the legal profession - we would like to build on that foundation in order to maintain the independence of the profession.

We recommend that the draft Bill be amended to reflect the recommendations of the Clementi Report so that the first chairman, Chief Executive and members of the Legal Services Board should be appointed by the Secretary of State but only after full consultation with the Lord Chief Justice.

We also recommend that the appointment of the chairman of the LSB is scrutinised by the House of Commons Constitutional Affairs Committee in line with the core tasks for Select Committees, and that it reports its conclusion to the House of Commons.

Government Response

In 1995, the Nolan Committee made a series of recommendations intended to increase public confidence in the way in which appointments to public bodies are made. Following that Report, the Office of the Commissioner for Public Appointments was created by Order of Her Majesty under an Order in Council on 23 November 1995. The role of the Commissioner is to set the standards for recruiting and to regulate the recruitment process for appointments in public bodies. The Commissioner has since established a Code of Practice, which is used to govern Ministerial appointments to public bodies, and to monitor the process to ensure that those appointments are made on merit after fair and open competition. The Government therefore **agrees** that all appointments made by the Secretary of State under the draft Bill should and will be subject to the Commissioner's code and thus in accordance with Nolan principles.

Once it is accepted, as it is, that the chairman's appointment will be made in accordance with Nolan principles, the Government does not consider it necessary or appropriate to make it an explicit requirement on the face of the Bill to consult the Lord Chief Justice. Propriety will be assured by following the Nolan principles. Any further requirements would not be appropriate because responsibility and accountability to Parliament for the appointment lies with the Secretary of State. He may well wish to consult the Lord Chief Justice, and he may wish to consult

others - but how he does has to be a decision for him. This accountability should not be diluted.

Scrutiny of the appointment of the chairman would of course already be subject to the oversight of the Commissioner for Public Appointments, who produces an annual report that provides detailed information on the appointments process, as well as summaries of the auditors' findings and complaints made, and highlights of the main issues that arose during the year. The Commissioner's Code also sets out important safeguards which ensure that the procedure for every Ministerial appointment is independent and transparent. For example, the Code includes a mandatory requirement that an independent assessor is involved in each appointment process. However, the Government recognises that there are opportunities for post-hoc scrutiny of appointments by Select Committees. The Constitutional Affairs Select Committee will obviously be free to take advantage of the powers that all Select Committees have to consider, and if appropriate report on, major appointments by a Secretary of State or other senior Ministers, should they think it necessary.

Recommendation 10

The draft Bill should also make provision for the LSB to establish a nominations committee in line with the Combined Code to make all future appointments as Chief Executive and ordinary members of the Board. The Chairman of the Board should continue to be appointed by the Secretary of State after full consultation with the Lord Chief Justice.

Government Response

The Board appoints the Chief Executive. The draft Bill already provides for the LSB to be able to establish committees and the LSB could do so in relation to the Chief Executive although such an approach might lead to unnecessary bureaucracy and cost. Ordinary members are appointed by the Secretary of State; to place an obligation on the face of the Bill requiring the LSB to establish specific committees for their appointment would be inappropriate for appointments by the Secretary of State. The Government consequently **does not agree** with this recommendation.

Recommendation 11

In line with our recommendations on appointments, we recommend that the draft Bill be amended to provide that the Secretary of State may remove the chairman of the Board only after full consultation with the Lord Chief Justice. Responsibility for the removal of other members - in line with the criteria set out in the draft Bill - should lie with the nominations committee of the Board.

Government Response

Unlike the position in respect of appointments by the Secretary of State (where these are subject to regulation and oversight by the Commissioner for Public Appointments) there is no similar arrangement that provides for supervision of the removal of the chairman of the LSB by the Secretary of State. Nonetheless, the draft Bill sets out specific circumstances in which the chairman can be removed, and that will be buttressed by his or her having recourse to judicial review if necessary. In addition, the Secretary of State can consult the Lord Chief Justice, and we would expect him to do so where appropriate. The Government therefore **does not agree** with the Committee's recommendation. The same applies to the removal of other Board members.

Recommendation 12

We share some of the concerns that have been expressed about the scope of the ongoing powers of the Secretary of State that are proposed in the draft Bill which appear to go significantly beyond the recommendations of Sir David Clementi. We therefore recommend that the Government reconsiders whether each of the powers proposed for the Secretary of State in the draft Bill is necessary, identifying those powers that could be removed or transferred. It would be wrong to create a perception that the Government is seeking in any way to exert long-term day-to-day control over the legal profession, or in any sense annex it. In saying this, we are in effect urging the Government to adhere to the recommendations of Sir David Clementi, which were that that the involvement of the Secretary of State should be restricted to important points of public policy where it could be demonstrated that Government involvement was absolutely necessary.

Government Response

The Government **accepts** that it should reconsider whether each of the powers proposed for the Secretary of State in the draft Bill is necessary, and we are currently working with stakeholders to review this. In considering these powers, however, we consider it important to emphasise that many of the functions of the LSB affect the rights and privileges of providers of legal services. Consequently, in preparing the draft Bill, we took the view that there should be proper Parliamentary accountability for the exercise of such important powers. The Bill provides for this by requiring that in exercising its more significant powers, the LSB should do so through Statutory Instruments laid by the Secretary of State. It is also important to emphasise that in most cases the Secretary of State may only exercise powers on the recommendation of the LSB.

The Government is currently reviewing these powers and will transfer responsibility away from the Secretary of State where it is appropriate.

Recommendation 13

Recruitment by Nolan processes for all LSB appointments should be included explicitly on the face of the draft Bill.

Government Response

As set out in the response to Recommendation 9 above, the Government is committed to an appointment process based on Nolan principles, and the Bill has been drafted in such a way as to be compatible with OCPA principles. However, we would not want to specify the appointments process on the face of the Bill, as that could prevent the Board from making appointments in accordance with future best practice and consequently the Government **does not accept** this recommendation.

Recommendation 14

We support the requirement in the draft Bill that the first - but only the first - chairman of the LSB must be a lay person. This should serve to get the new regulatory framework off to a positive start, increase public confidence in the new system and overcome the perception among some that it is a "closed shop". For subsequent appointments to the chairman of the LSB, we believe it is in the public interest that the best person for the job is appointed, following Nolan principles, whether or not they are or have ever been an authorised person. We would not like to see a situation, for example, where a person is excluded from consideration because they are a practising solicitor or because early in their career they qualified as a solicitor or a barrister.

Government Response

The Government notes the general support of the Committee, and **accepts** its view that for the second and subsequent appointments to the chairman of the LSB, the best person for the job is appointed, following Nolan principles, whether or not they are or have ever been an authorised person.

Recommendation 15

We recognise that the Financial Services Authority is a Model A regulator unlike the LSB. However, we recommend that the draft Bill be amended to reflect the provisions set out in section 2 of the Financial Services and Markets Act 2000.

Government Response

The Government **accepts** that some of the regulatory principles at section 2 of FSMA may be relevant to the LSB when exercising its functions under the Bill.

However, we are still considering the implications of each duty in relation to the existing duties of the LSB set out under part 2 of the Bill. Where it is appropriate for the Bill to reflect any provisions in section 2 of FSMA, it will do so.

Recommendation 16

We recommend that the Government should give further consideration to the criteria for the use of each of the powers of the LSB. The draft Bill should ensure that consistent with the Government's policy that lead responsibility should rest with the approved regulators the Legal Services Board acts in partnership with the approved regulators, seeking to resolve differences by agreement wherever possible. Objective thresholds should be set for the exercise of each of the powers in clauses 24 to 40 of the draft Bill. The LSB should be allowed to intervene to take over the functions of an approved regulator if, and only if, there is clear evidence that serious damage might otherwise be caused to the regulatory objectives.

Government Response

The Government **agrees** that the intention of the LSB should be to work in partnership with authorised regulators, leaving them with the responsibility for day to day regulation. The LSB should exercise its powers only where approved regulators are clearly failing. While the LSB will need to establish detailed rules providing for the use of each of its powers, the Government is considering the extent to which the Bill might increase the thresholds before some of the powers can be used.

Recommendation 17

We believe it is in the public interest that the LSB should establish and consult a Practitioner Panel alongside the Consumer Panel. We recommend that the draft Bill be amended to require the LSB to establish a Practitioner Panel, which should include representation of legal academics.

Government Response

One of the benefits of the Government's proposals is that, provided they have made appropriate arrangements for the separation of their regulatory and representative functions (see also the response to Recommendation 7), approved regulators can use their experience and knowledge of working with practitioners to inform regulatory policy. In addition to this, as part of its consideration of applications from approved regulators and other bodies, it will be open to the LSB to consult such persons or organisations as it considers appropriate. The Government therefore considers that to require the LSB to establish a practitioner panel could represent an unnecessary and disproportionate burden on its resources and might restrict its ability to consult other practitioners in carrying out its functions. Accordingly, the Government **does not accept** this recommendation.

Recommendation 18

We support the recommendation of the House of Lords Select Committee on the Constitution on the issue of appeals and we recommend that the draft Bill be amended to include a right of appeal to the High Court against regulatory decisions by the Legal Services Board. In line with existing practice, this right to appeal to the High Court should require the permission of a judge. This would help overcome fears expressed that a right of appeal would lead to ongoing court battles between the LSB and approved regulators.

Government Response

To provide a right of appeal to the High Court against regulatory decisions by the Legal Services Board has the potential for every decision to be appealed. Even if this were to be subject to the permission of a judge, there remains the potential for a high number of challenges, with matters being progressed from the High Court to the Court of Appeal and even the House of Lords. This could lead to increased costs and a weakening of the LSB's authority as an oversight regulator. The Government considers that the Bill provides sufficient safeguards, including consultation, in respect of the making of its regulatory decisions and consequently **does not agree** there is a need to provide for such an appeal mechanism. The option of judicial review will be available where it is appropriate, to challenge an LSB decision.

Recommendation 19

We recommend that the Government gives further consideration to the powers and duties of the Consumer Panel to ensure that they are in line with consumer panels in existing regulatory structures and makes any necessary amendments to the draft Bill.

Government Response

The Government notes some of the helpful points which emerged during the Committee's evidence sessions and **agrees** that it should review the powers and duties of the Consumer Panel to ensure that they are in line with consumer panels. For example, the Government considers that the Panel should be able to determine its own procedures and to establish sub-committees where appropriate.

Recommendation 20

We recommend that the Government considers how the draft Bill could be amended to reflect a direct relationship between the regulatory arm of the relevant approved regulators named in Schedule 5 and the LSB.

Government Response

The Government **accepts** that, in general, regulatory arms should be clearly separated. The relationship between the regulatory arms of approved regulators, and the direct relationship between regulatory arms and the LSB, are currently being considered as part of our review of the strengthening of the requirement for the separation of regulatory and representative functions dealt with under Recommendation 7.

Recommendation 21

We are not convinced of the justification put forward for the continued involvement of the Archbishop of Canterbury in a modern regulatory framework. We recommend that the Government looks at this issue again.

Government Response

The Master of the Court of Faculties is appointed by the Archbishop of Canterbury and has two important functions. First, to act as regulator of the notaries' profession in England and Wales; and second, to perform a number of ecclesiastical functions on behalf of the Archbishop of Canterbury. In recognition of the need to provide for oversight regulation by the LSB, the Archbishop of Canterbury has agreed to cede to the LSB his responsibility for oversight of the regulation of notaries through the Master of the Court of Faculties. However, given the ecclesiastical functions that the Master will continue to perform, the Archbishop is concerned that he should continue to appoint the Master. In addition to this, the Archbishop has expressed a concern that any change to the current arrangements beyond those provided for in the Bill could adversely affect the recognition of English notaries by other Latin notary states.

The Government considers that the provisions in the Bill reflect an appropriate compromise and after further consideration it **does not accept** the argument for a change in the proposed position.

Recommendation 22

We note that the offences in clauses 11 and 12 will apply to a range of situations where consumers may need protection, from the impostor on the high street to the risk that unauthorised persons may seek to become involved in the conduct of multi-million pound litigation in an ABS firm. We note that there is a clear disparity with the penalties proposed in the Compensation Bill. We find it difficult to reconcile Government policy which considers the offence of pretending to be entitled to provide claims management services more serious than pretending to be entitled to provide any of the reserved legal services covered by the draft Bill. We recommend that the draft Bill be amended to ensure that the penalties proposed for offences of pretending to be an authorised person are proportionate to the risks

which they seek to address and that any disparity with Compensation Bill penalties for pretending to be an authorised person is justified. In particular, we recommend that clause 12(2)(b) be amended to increase the maximum penalty to two years' imprisonment.

Government Response

Before the Compensation Act 2006, the essentially unregulated claims management industry resulted in a large number of cases where consumers suffered significant detriment. In many cases this was the result of 'touting' for business in shopping centres, or seeking out potential claimants in hospital accident and emergency departments. The Compensation Act provides for significant penalties in order to act as a deterrent, particularly to individuals who prey on vulnerable people, with the maximum penalty most likely to be used in respect of persistent offenders. The Government **agrees** that, where appropriate, penalties provided for in the draft Bill should be consistent with those provided for by the Compensation Act. We are currently considering where amendments are necessary and will do so where appropriate.

Recommendation 23

We recommend that will writing for fee, gain or reward should be included within the new regulatory framework. The draft Bill should be amended to provide for regulation subject to any exemptions necessary in the consumer interest. We note that there is currently no existing regulatory framework for will-writing and no existing professional body with responsibility for will-writing activities. We note that these hurdles have been overcome in respect of the claims management sector, in the context of the Compensation Bill, and urge the Government to consider whether will-writers might be brought within the scope of the regulatory framework in a similar manner.

Government Response

The Government's White Paper, "The Future of Legal Services: Putting the Consumer First", confirmed that (after working closely with consumer bodies and the legal professions) there did not appear to be a compelling argument for the statutory regulation of will writing. That remains the Government's position, and consequently we **do not agree** with this recommendation. However, once it has been established, the Government would expect the LSB to consider whether there is a regulatory failure in respect of will writing services, or any other legal activity, and whether the activity should be brought under its regulatory control under the provisions of Clause 19 of the Bill.

Recommendation 24

We do not support mediation being included in the list of reserved legal activities but we support its promotion as a means of dealing with legal disputes.

Government Response

The Government **agrees** and the draft Bill already makes it clear that judicial or quasi-judicial activities (including mediation) are not reserved legal activities.

Recommendation 25

By the time of the publication of this report, the Compensation Bill will have received Royal Assent. We recommend that the Government clarifies its position on the regulation of claims management and amends the draft Bill to reflect provisions in the Compensation Act 2006.

Government Response

We **agree** with the Committee's views. An announcement was made during the Commons Committee stage of the Compensation Act, confirming that the Secretary of State would act as regulator of claims management services in the short term. A Head of Regulation, Mark Boleat, has been appointed to undertake day-to-day regulation on the Secretary of State's behalf and Staffordshire County Council Trading Standards Department will undertake the monitoring and compliance role. DCA expects to invite applications for authorisation to provide a regulated claims management service from late November and the Act will be fully commenced by April 2007. The Bill will be amended to transfer the Secretary of State's oversight role to the Legal Services Board to allow for the smooth transfer of the regulatory function.

Recommendation 26

We are concerned that the provisions of clause 18 could have the effect of creating two classes of lawyers in terms of their regulation - those that are exempt and those that are not. This would not be in either the consumer or the public interest. We recommend that the draft Bill be amended to reduce the scope of clause 18 to what is absolutely necessary.

Government Response

Clause 18 is intended to provide transitional protection for not-for-profit (NfP) bodies. At the moment, NfP bodies themselves are not regulated (although lawyers working within them are) nor do they have the ability to raise revenues to the same extent as commercial law firms. Clause 18 preserves this position until

the regulatory regime established in the Bill is operational. In the longer term, our intention is that NfP bodies should be regulated, but only to the extent that is necessitated by the risks they present (see for example clause 88 of the draft Bill). This is not intended to create differences in the way that individual lawyers are regulated, but it will reduce the regulatory burden on NfP bodies to the minimum necessary. Further consideration will be given to the regulatory treatment of NfPs.

Recommendation 27

We recommend that clause 43 of the draft Bill should give the LSB the right to consult on the level and impact of fees for not-for-profit bodies and, if necessary, to set differentiated fees for not-for-profit bodies.

Government Response

The Government **agrees** with the Committee's recommendation that the LSB should have to consult. But fees are a matter for the individual regulators. The Legal Services Board if regulating directly is already under a duty to consult where it makes rules, including rules under clause 43 specifying practising fees that are to be charged by approved regulators. The Board and regulators are also under duties to act in a way that is compatible with the regulatory objectives, which includes improving access to justice. However, we will consider whether any drafting amendments are required to strengthen this ability.

Recommendation 28

Trade unions are distinctive from other organisations and governed by their own legislation. We are concerned that the draft Bill could restrict the ability of trade unions to act in their members' interests especially by placing on a legal footing the means by which trade unions provide advice and representation to members. We therefore recommend that the Government gives further consideration to any necessary exemptions from the draft Bill for trade unions. In doing this, we recommend that the Government also takes note of concerns expressed during the Committee Stage debate on the Compensation Bill in the House of Commons about the provision of legal services by subsidiary companies wholly-owned by trade unions.

Government Response

The Government **accepts** the recommendation. We are currently working with the TUC to ensure that exemptions under the Legal Services Bill take account of the position reached with respect to trades union exemptions under the Compensation Act, and considering whether any further provision is needed in relation to the Bill regime.

Recommendation 29

A few witnesses raised the automatic exemption of Government lawyers from the scope of the regulatory regime. We recommend that the draft Bill be amended to remove this automatic exemption. It is important from the outset that all legal professionals are included in the regulatory framework.

Government Response

The Government understands the argument put forward by the Joint Committee that all lawyers should be appropriately regulated. While we take the view that Government lawyers represent a very different regulatory risk when compared to lawyers working in private practice, we are nevertheless still considering the implications of this proposal.

Recommendation 30

We recognise that the draft Bill strikes a balance between the compensation fund provisions of existing approved regulators and ensuring that new approved regulators establish such funds in the interests of consumer protection; and we have evidence supporting this position. However, we have also heard evidence that a central compensation fund should be established for all existing and future approved regulators. Both positions have some coherence and merit and we have not had sufficient time to come to a determination on one side or the other. We hope that this issue will be the subject of further detailed debate in Parliament once the Bill is introduced.

Government Response

The Government has been continuing to consider the provision of compensation funds since the commencement of the pre-legislative scrutiny process. As the Committee acknowledges, both positions do indeed have some merit and it is crucial to ensure that any arrangements devised satisfy the objectives of consumer protection and fair and proportionate regulation.

To aid in formulating policy, the Government commissioned PricewaterhouseCoopers to consider a number of options for future compensation funds. Their report was published on 20 June. We have since discussed the report's findings with key stakeholders, and there appears to be broad agreement that while there may be potential risks to consumers in the current compensation fund environment, there is little demonstrable evidence of significant consumer detriment arising from these risks.

Creating a central compensation fund would be a significant departure from the current arrangements and, as shown in the PwC report, would have high costs which would inevitably be passed on to consumers of legal services. However, our bottom line is that we cannot risk inadequate consumer protection, so it is clear that the LSB needs to be able to act if the risks to consumers increase over time. It is

our firm view that the LSB has the necessary power to ensure that all regulators maintain appropriate consumer protection and insurance arrangements for the range of services that they provide. The Government **agrees**, however, that it would be beneficial for this issue to be the subject of further debate in Parliament once the Bill is introduced.

Chapter 5: Alternative Business Structures

Recommendation 31

In our opinion, it should be an over-riding consideration in licensing ABS firms that nothing in the proposed ABS structure would have an adverse effect on the quality of legal advice given by the legal professional to the client. Once bad advice has been given, there is a long, complex and difficult course for the client to follow if they wish to seek redress.

Government Response

It is important to recognise that the regulatory objectives in Clause 1 of the Bill, which include maintaining adherence to the professional principles, will bind licensing authorities in exactly the same was as they do the LSB and approved regulators. Each ABS will also be required by Schedule 11, Part 3, paragraph 18(3) to *'at all times have suitable arrangements in place to ensure that it and the persons through whom the body carries on any licensed activity maintain the professional principles'*. Additionally, it will be open to licensing authorities to make rules or impose conditions (or for the LSB to direct them to do so) in relation to any licences they issue to ensure there is no adverse impact on quality. However, the Government **agrees with the principle** that ABS firms should not create an adverse effect on the quality of legal advice and is content to consider drafting amendments to emphasise assurance of quality, although not to the extent that quality is made an *overriding* consideration, or that it should apply to ABS entities only.

Recommendation 32

We urge the Government to re-think its approach to Legal Disciplinary Partnerships (LDPs) and amend the draft Bill to make provision providing the opportunity for LDPs without outside ownership.

Government Response

The Government **accepts** the Committee's recommendation and intends to enable those professional bodies with appropriate regulatory and other arrangements to regulate entities that fall short of the Bill's definition of an ABS entity. This would allow the Law Society, for example, to remove the current restriction that requires a solicitors' firm to be fully owned and managed by solicitors. It could instead provide for the regulation of entities which are managed or owned by different types of lawyers (e.g. a solicitor and a barrister) without the need for the issue of a full ABS licence. This should reduce a potential burden on firms and reduce costs to the consumer, while enabling greater liberalisation in the delivery of services.

Recommendation 33

We were not attracted by the proposal that Multi-disciplinary Partnerships (MDPs) could "ring fence" their legal service provision from other parts of their business - this would undermine any advantages of ABS firms. We recommend that the draft Bill be amended to make it explicit that the LSB and other licensing authorities must have agreements in place with regulators of other relevant professions before licensing ABS MDP firms.

Government Response

The Government **accepts** the principle that licensing authorities seeking to regulate ABS firms should, where those firms provide services regulated by other sectoral regulators such as the Financial Services Authority, make appropriate arrangements with those regulators to address regulatory overlap and potential conflict. The Government agrees that, without such requirements, cross-regulatory conflicts could arise.

A clause requiring consultations can be provided, and the LSB will need to be satisfied that where ABS regulators are seeking to regulate the provision of legal and other services, their proposed licensing rules include adequate provision for managing any foreseeable regulatory overlap. It will be important to ensure that any arrangement does not lead to an unjustified restriction on competition; the Government will work with the Office of Fair Trading to ensure any requirements are compliant with competition legislation.

Recommendation 34

We share concerns expressed about the impact of legal professional privilege on the effectiveness of ABSs and therefore the advice given to the client by an ABS organisation. We recommend that the Government gives further consideration to how legal professional privilege should apply to ABS firms and what legislative provisions are necessary.

Government Response

The Government and recognises the importance of the concerns expressed about how LPP should apply to ABS firms. As a general principle, ABS firms, with guidance from regulators, will need to structure their business communications in order to ensure that LPP and consumer interests are adequately protected. Firms will need to make clear to clients the extent to which their communications are protected by privilege. These arrangements are facilitative; it will be for firms to decide whether they can provide the safeguards that the LSB and regulators will require. Beyond that, the Government agrees with the Committee that there will need to be greater clarity about the extent to which LPP protection for clients is available when services are delivered through ABS firms. We therefore **accept** the Committee's recommendation and are considering whether and to what extent there should be further provision for this in the Bill.

Recommendation 35

In our opinion, LDPs and MDPs with outside ownership may create an undesirable conflict between shareholders and lawyers and the benefits of outside ownership would need to be weighed against the merits. This is reflected in our recommendations on the speed of approach to ABSs in paragraphs 285-291.

Government Response

The Government **accepts** that our proposals will need to adequately provide for the LSB and authorised bodies to maintain appropriate rules to ensure that any conflicts are properly dealt with.

We have proposed that prospective external investors undergo a fitness to own test. Our response to Recommendation 36 confirms that we agree with the Committee that the principal elements of this test should be set out on the face of the Bill. The test will be triggered if the sum to be invested is above a particular threshold set by the Legal Services Board. Regulators will then monitor any changes to the ownership structure of ABS firms on an ongoing basis.

The Bill will set out a clear duty on licensing authorities to satisfy the LSB that its rules on conflicts of interest are fit for purpose.

Recommendation 36

We recommend that the draft Bill should be amended to specify (a) the basis of the fitness to own test on the basis that the Minister suggested - honesty, integrity and reputation, competence and capability and financial soundness; and (b) who is responsible for making the judgement. The LSB should have a right to add additional requirements to the "fitness to own" test in light of experience. The onus should be on the individual or firm to prove that they meet the fitness to own test. We commend the approach taken in the Courts and Legal Services Act 1990 that set up an Advisory Committee to make judgements about "fitness for purpose". The ownership threshold set by the LSB should reflect a significant interest in the ABS firm.

Government Response

The Government **agrees** that it is desirable to set out the fitness to own test on the face of the Bill, which includes most of the provisions mentioned by the Joint Committee, and that it should be clear who makes such a judgement. We are considering what criteria should be included in the determination of who is a fit and proper person.

However, we **do not agree** we should require the LSB to establish a specific advisory committee. The LSB is already able to establish such committees as it considers appropriate. In order to maintain flexibility in primary legislation it would

be preferable to determine detailed provision in rules. Many of our stakeholders support this view.

Recommendation 37

Given the level of uncertainty about the impact of ABS provisions we urge the Government to use "less haste and more care" and follow the Clementi Report in their approach. We recommend that the draft Bill be amended to ensure that the LSB takes a "step-by-step" approach to licensing ABSs. We recommend therefore that the following four stages be licensed in turn as set out in Table 5 in Chapter 5. If necessary, this gradual approach could be adopted by bringing the necessary provisions into force by order at different times.

Government Response

The Government **agrees with the principle** behind the Committee's recommendation but does not believe that a prescribed timetable is necessary or appropriate. It should be for the LSB to make a judgement whether a regulator has the appropriate arrangements in place to regulate and address the risks of various kinds of ABSs, and those ABSs will only emerge once this regulatory framework exists. There is no reason artificially to delay implementation and the benefits to clients.

Recommendation 38

We do not wholly accept the Minister's argument that ABSs do not lend themselves to a pilot scheme and we hope that the LSB will take our approach. In line with our recommendation in paragraph 291, we recommend that the Government instruct the LSB to take a step-by-step approach to ABSs starting with the least controversial model - partnerships of different types of lawyers without outside ownership or management - before going into the deeper waters surrounding more complex forms of ABSs where real issues of conflicts of interest and uncertainty of impact may arise. We do not think that a "pilot scheme" could be suitable for the introduction of ABS licences.

Government Response

The Government too considers that the establishment of a pilot scheme for ABS firms could be unworkable and would be unlikely to deliver much in the way of benefit.

Recommendation 39

We have received no concrete evidence that access to justice will either be improved or reduced under ABS arrangements, but we are persuaded by some of the evidence suggesting that the reforms may reduce geographical availability. We consider that ABSs may reduce the number of access points for legal services and we see this as a potential problem. There is clearly an issue here and the only conclusion we are able to draw is that no-one can be sure how it will work out. We recognise that there may be a trade-off between the quality and accessibility of advice - for example, a small, high street solicitor in a rural area may not be able to provide the specialist advice a client requires. We recommend that the Government amends the draft Bill to ensure that the impact of ABSs on access to justice, particularly in rural areas, informs the decision-making process for licensing an ABS firm.

Government Response

The Government **agrees** with the Committee. As part of the regulatory system ABS licensing will promote access to justice. Clause 1 of the Bill already places the LSB and licensing authorities under a statutory duty to have regard to the regulatory objectives, including the objective of improving access to justice, when exercising their functions in relation to licensed bodies. A licensing authority will also have powers to refuse or attach conditions to licences (for example where it feels that granting a licence to the firm in question could damage access to justice). It will also be possible for licensing authorities to take action to modify the licence terms of firms already in existence.

Recommendation 40

We recommend that the draft Bill be amended to provide explicitly that those bodies who currently have statutory ability to license ABS services (for example, the Council for Licensed Conveyancers) may continue to grant those licences rather than relying on transitional provisions.

Government Response

The Bill aims to create a level playing field between regulators and to ensure that all consumers of services provided through ABS firms are protected by the same statutory safeguards. Transitional provisions are provided for in the Bill to allow existing ABSs to continue under present licensing arrangements during a transitional period. We agree that this is necessary to ensure that the effective regulation of existing structures can continue without regulators or their members being unduly burdened by a sudden change in statutory requirements. However, the Government **does not agree** that such arrangements should be extended indefinitely. To do so would provide certain regulators with an indefinite competitive advantage, and could risk creating inconsistent standards of consumer protection across the legal services market.

Recommendation 41

We are concerned that certain ABS models that could follow Royal Assent to the Bill may be regarded as illegal or unethical in some territories or jurisdictions. If this is the case, this would necessitate a fundamental re-think of this policy. We are also concerned lest the provisions in the draft Bill would move England and Wales out of step with other European countries.

Government Response

The Government **does not agree** and takes the view that it should be left to individual firms, who know their international markets and clients better than Government, to make their own judgements. Our ABS proposals are entirely facilitative and it is open to individual firms to decide whether they wish to seek a licence to operate in that way. It would of course be open to individual firms to establish different structures in other jurisdictions, consistent with what is permitted by the relevant national regulators. Currently Germany, Spain, and a number of states in Australia permit some elements of ABS and a number of European countries are looking at further reforms.

Recommendation 42

We do not support the idea put forward by the Law Society for "ring-fenced" legal provision within ABS firms, which we believe, would undermine any advantages to be gained from ABS firms.

Government Response

The Government **agrees** with the Committee's view that ring-fencing legal services within an ABS firm is unlikely to maximise the potential to improve service to the consumer and profitability for firms. However, it will be for the LSB, licensing authorities, and firms to exercise the flexibility which the Government's proposals provide to decide which arrangement they consider most appropriate in individual circumstances.

Chapter 6: Legal Complaints

Recommendation 43

We agree that the draft Bill's current provisions for creating the OLC fail to make clear the respective roles for the OLC and approved regulators in handling different types of complaints. We recommend that the role of the OLC and the approved regulator in handling complaints is clearly demarcated on the face of the Bill.

Government Response

The role of the OLC is to provide redress, essentially by way of restitution and compensation, to consumers of legal services where things go wrong. It can (among other things) order providers to re-do work, refund fees or provide clients with financial redress. However, it has no punitive role and cannot sanction a legal practitioner. It is the role of the approved regulators to regulate and, if necessary, discipline their members. This was the split of functions envisaged by Sir David Clementi and the Government welcomes the Committee's acceptance of this framework.

The Government considers that the respective roles envisaged for the OLC and the approved regulators are already adequately defined, but it may be that those roles do not emerge on the face of the Bill as clearly or immediately as might be possible. The Government therefore **accepts** the Committee's recommendation for greater clarity. We are considering whether there is scope to arrange these provisions to bring out the distinction. Depending on the outcome, we will also consider whether other means should be employed to communicate the different roles of the OLC and the approved regulators.

Recommendation 44

We retain concerns - reflected to us in evidence - that a "one-size-fits-all" approach to complaints handling may not be suitable for all complaints and may not give the client the best outcome. This may particularly be the case for those complaints where issues of conduct and service are effectively inseparable. We therefore recommend that the draft Bill should be amended to give the OLC the power to refer service complaints, as well as conduct complaints, to an approved regulator where it considers it is appropriate to do so. In doing so, the LSB and the OLC must be satisfied that an approved regulator has an approved mechanism to handle service or "hybrid" complaints. The OLC should remain the single access point to which consumers take their complaint.

Government Response

The Government believes that there are clear practical benefits in separating consideration of redress from regulatory action, and notes that a number of witnesses, including the Chief Financial Ombudsman and the Master of the Rolls, concurred in this view in their evidence to the Committee. The great majority of complaints do not require regulatory action and where they do it is not right that the consumer should have to wait for that to be resolved before getting redress.

Whilst the Government appreciates the Committee's concern that this is not necessarily the case for every type of legal services provider, it does not seem defensible from the perspective of consumer confidence to make an exception to this principle in the case of a single type of provider. Allowing different processes for different types of provider would be inconsistent with key objectives such as clarity for consumers and consistency of outcomes. Consumers would be uncertain about who was handling their complaint, or the criteria against which it was being measured. For these reasons, the Government **does not accept** the Committee's recommendation that the OLC should be able to refer complaints of any kind on to approved regulators.

Recommendation 45

We recognise that clause 105(3) of the draft Bill establishes that there will be a two-tier process for complaints handling, but are concerned that this remains unclear to many. We recommend that the Government should ensure that the draft Bill makes this two-stage process clear, in order to avoid potential confusion for consumers and those within the legal services sector.

Government Response

The Government **agrees** entirely with this recommendation. It should be clear to all parties that the OLC will not (except in specified circumstances) consider complaints until the legal services provider has already had a reasonable opportunity to resolve the complaint in-house. We will consider how this might be brought out more clearly on the face of the Bill.

Recommendation 46

We recommend that clause 99(2) and Schedule 13 be amended to allow legal practitioners to hold the post of assistant ombudsmen.

Government Response

The Government **accepts** the Committee's recommendation, subject to the proviso that nobody should be allowed to work as a legal practitioner at the same time as holding the post of assistant ombudsman.

Recommendation 47

We consider that decisions taken by the OLC should also be subject to an appeal based on the merits. This is not provided for by judicial review. We therefore recommend that the draft Bill be amended to include provision for a final internal appeals mechanism within the OLC.

Government Response

The Government **agrees** with the Committee that it is not desirable for parties to a complaint to have no recourse except judicial review if they are dissatisfied with the initial consideration of their complaint. It is envisaged that the OLC will operate some form of internal review mechanism. This might be based on the Financial Ombudsman Service model, where caseworkers make initial recommendations and either party can request that an ombudsman reconsider that recommendation.

This is a *de facto* two-tier process under which the ombudsman's decision is then final. The Government believes that this model strikes an appropriate balance between quick, informal routes to redress and adequate protection of all parties' human rights.

While accepting that there ought to be an internal review mechanism within the OLC, we do not believe that the details of this mechanism ought to be set out in legislation. We believe, following the successful precedent of the Financial Ombudsman Service, that it is important for the OLC to develop its own mechanisms which are appropriate for the particular types of complaints it receives, and that the OLC has the ability to develop those mechanisms over time in line with changing conceptions of best practice. We would therefore expect the OLC to design its internal review mechanism through draft rules, as the Financial Ombudsman Service has done.

Recommendation 48

We recommend that in future, the Government ensures that the full range of information necessary to scrutinise a draft Bill is made available to a pre-legislative scrutiny committee from the start of its inquiry.

Government Response

In relation to this particular draft Bill, while the Government would obviously have preferred to provide the Committee with a full draft of consequential amendments, we took the view that it was not essential for consequential amendments to the Solicitors Act and other related legislation to be published as part of the draft Bill in order to enable appropriate scrutiny of the Government's main policy proposals. To have delayed publication would have increased the risk of a potentially significant delay to the Bill's readiness for introduction, reducing the scope for consumers to see real benefits from these important reforms as quickly as possible.

Nonetheless, the Government acknowledges the Committee's concerns and **agrees in principle** that pre-legislative scrutiny committees should be provided with the fullest possible range of information at the start of their inquiries.

Recommendation 49

We consider that the term "ombudsman" is one that is easily recognised by consumers. We therefore recommend that clause 92(4) of the draft Bill be amended to require the OLC to include the word "ombudsman" in the name under which it operates the scheme.

Government Response

The Government **agrees** that the term "ombudsman" is one that is easily recognised by consumers, and note that such an amendment is in line with the broad thrust of Government policy. We will therefore consider how best to give effect to the Committee's recommendation.

Recommendation 50

We note the evidence we have heard that the £20,000 redress limit may be too low and we recommend that the Government provides further explanation of the rationale for deciding on this amount. We also recommend that the draft Bill be amended to include a requirement that the OLC should consult on the level of the compensation redress limit after a set period of time (for example, after 2 years). Thereafter, the redress limit should be regularly reviewed in order to keep it in line with inflation and any other relevant factors.

Government Response

The Government is concerned that if the OLC were permitted to make an award for an unlimited or very high level of redress, it could have implications for indemnity insurance and lead to increased costs to the consumer. Most consumer complaints involve relatively small amounts. The Law Society's average award for redress in 2004/05 was £405.53; the Bar Council's was £427.78.

On the advice of its Independent Complaints Commissioner, Sir Stephen Lander, in April 2003, the Law Society has recently accepted that the limit which it applies to redress should be increased from £5,000 to £15,000. This is the highest level of redress in the legal sector. To allow for the fact that the implementation of the proposals in the Bill will take some time, the Government proposes that under the new system, awards made by the OLC should be subject to an upper limit of £20,000.

We **agree** with the Committee that it will be important to keep this redress limit under regular review, and there is provision in the draft Bill allowing for that review.

We intend to maintain that provision, and although we see no specific need to require the OLC in legislation to review this limit after 2 years, we would certainly expect the OLC, the LSB, and the Consumer Panel to review the limit whenever there is evidence to suggest that this is necessary.

Recommendation 51

The Government may wish to reconsider whether or not clause 102(3) should be amended to ensure that third parties in most circumstances should not be able to seek redress from the OLC.

Government Response

The Government notes that there is wide agreement on this point. We therefore **agree** to reconsider this clause in the light of the Committee's recommendation. There are circumstances where a third party is a *de facto* client - for example, a beneficiary of a will - and we would want these circumstances to be reflected in any assessment of who is eligible to seek redress from the OLC. The draft Bill allows the OLC to define categories of persons eligible through scheme rules; we are considering whether there are alternative approaches that might operate more effectively.

Recommendation 52

We consider that applying the "polluter pays" mechanism to those against whom a complaint is made but not upheld is unfair and amounts to making the innocent pay. It may also have unwelcome consequences, by unfairly penalising particular areas of legal work and creating a potential disincentive to act on behalf of certain clients. We therefore recommend that the draft Bill be amended to ensure that the "polluter-pays" mechanism is applied only to those against whom a complaint is upheld.

Government Response

The Government **does not agree** with this recommendation, and notes that it would not be in line with other ombudsman schemes. It is important that suppliers have an incentive to handle complaints effectively in-house, and important that the OLC has an incentive to conciliate complaints where possible. The former incentive is provided by the prospect of a charge from the OLC; and the latter incentive would be compromised by the OLC having to rely only on upheld complaints for funding.

Clearly, there are circumstances where it would be unfair to charge those who are the subject of complaints. The Government would not, for example, expect providers to pay fees for the processing of complaints against them, which were found to be frivolous or vexatious. Nonetheless, a substantial proportion of the

complaints that reach the OLC should be expected to be of some merit - otherwise the provider should have been able to resolve them at in-house level. Where they have not, the Government believes it is surely more reasonable for that provider to contribute to the cost of processing the complaint than it would be to charge all of the costs to the profession as a whole.

The Government has also consistently acknowledged the Committee's concern that case fees might unfairly penalise particular areas of legal work or create a potential disincentive to act on behalf of certain clients. It is plausible (although by no means certain) that a one-size-fits-all approach to setting fees might have this effect. However, it is for this reason that clause 106 of the draft Bill deliberately gives the OLC the flexibility to set different fees for different types of lawyer or different stages of a complaint. Indeed, should it consider it appropriate, the OLC would be able to waive fees altogether.

This flexibility should also be considered in conjunction with the consultation requirement with regard to the setting of fees, and with the regulatory objectives to protect consumers and improve access to justice. We believe that this combination of safeguards should serve to ensure that fees are set in an equitable manner, which does not unfairly penalise any providers or indeed any consumers.

Recommendation 53

We recommend that the Government should ensure that the OLC enter into memoranda of understanding with other complaints or regulatory bodies.

Government Response

We **agree** entirely with the Committee's recommendation, although we do not believe that this needs to be specified in legislation.

Chapter 7: Financial provisions and costs

Recommendation 54

PricewaterhouseCoopers' (PwC) conclusions about the costs of the Legal Services Board are explicitly based on the assumption that the LSB will operate at a level of activity not substantially different from that performed under the current framework. We think some amendments to the draft Bill - suggested elsewhere in this report - are necessary to ensure that is the case.

Government Response

The Government **accepts the principle** set out by the Committee that it is necessary to ensure that the Bill does not require the LSB to do more than necessary. The Bill reflects this principle of proportionate regulation.

Recommendation 55

It is unclear to us how PwC move from the assumption of 15% efficiency savings, to estimating a running cost of almost 40% lower than current costs. We think the Government should revisit that estimate. The possible increase in complaints, which even PwC seem to regard as inevitable, should be reflected in the RIA. Given that some increase in complaints is likely as a result of the establishment of the new system, and given that the new system will no longer rely on the services provided freely (for example by barristers) we think it unlikely that the running costs of the OLC will be any less than the costs of the existing complaints handling systems. The £4.2 million increase in costs that PwC estimate the rise in complaints is likely to represent has an overall impact on the Government's claim about the cost of the new regulatory system being 10% lower than under the existing system. We have received no evidence from the Government to support this claim.

Government Response

Whilst the Government is broadly content with the PwC report we are currently reviewing some of their underlying assumptions and their impact on the projected costings. The Final RIA that will be published alongside the Legal Services Bill will reflect PwC's work and the outcome of any further work undertaken by DCA officials.

Recommendation 56

We recommend that the draft Bill be amended to require the LSB be made to consult when making levy rules and to provide that levy rules must be fair and proportionate.

Government Response

The Government **agrees** with the Committee's view and notes that the LSB is already required under clause 152 to consult when making rules. This already includes levy rules, although we are considering how provision that the rules should be fair and proportionate should be specified more clearly on the face of the Bill.

Recommendation 57

We recommend that the Government give further consideration to funding the start up costs of the new regulatory system. We understand that such assurances have been given in respect of Part 2 of the Compensation Bill which introduces a new regulatory regime for claims management. At the very least the Government should make clear how it sees the set up of the LSB and OLC being funded. If this is to be done through levies and charges on the legal profession, a timescale for collection of these should be set.

Government Response

The Government has made it clear that it proposes that the legal professions should pay the full cost of these reforms. The basic principle is that those being regulated should bear the cost of regulation.

While the Government therefore **does not accept the principle** of the recommendation, we are nevertheless looking at the precise mechanism through which the implementation and start-up costs will be funded. As well as considering the position reached in respect of the Compensation Act, we are keen to ensure that the funding arrangements are in keeping with the principles of better regulation and that they facilitate the timely implementation of the provisions contained within the Bill.

Recommendation 58

We are also concerned at the impact of additional regulatory costs of the new system on not-for-profit bodies, such as Law Centres, which are generally publicly funded and we recommend that the Government considers this issue carefully.

Government Response

Given the reduced risks arising from the absence of a significant commercial interest, and the lower resources of not-for-profit bodies, we expect that the regulatory costs for such bodies under our proposals will be lower than for commercial firms. The Bill provides the LSB or other licensing authorities with flexible powers to waive or modify ABS rules for not for profit bodies where appropriate. However, the Government **accepts** the principle of the recommendation and will consider carefully the impact of regulation costs on not for profit bodies to ensure they are not unduly burdened.

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