

Legal Services Act: New forms of practice and regulation

Consultation paper 12

Firm-based regulation – fee-raising policy for 2009

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Introduction

1. This paper contains the SRA's proposals in relation to the fees it will charge to firms (recognised bodies and recognised sole practitioners) in 2009. It does not deal with the practising certificate fee. It also contains proposals in relation to the compensation fund contribution to be paid by recognised bodies. The SRA is consulting on what it proposes to recommend to the Law Society Council in relation to such contributions.
2. Our strategic paper published in November 2007¹ suggested that it would be necessary to develop a new system for allocating the cost of regulation among firms and individuals. That paper suggested that little change may be made in 2009, but significant change is likely for 2010. This paper does not deal with the future allocation of costs between firms and individuals that may apply from 2010. Work is continuing between the SRA and the Law Society on preparing a consultation on fee structures for 2010 and beyond but that is not ready yet. This paper therefore only looks at what fees should be payable by recognised bodies in 2009, the first year in which there will be an annual renewal exercise for recognised bodies. It is important that there is clarity on this as soon as possible for both the SRA and the profession. We are proposing very little change from the current fee structure, as we consider that will broadly cover the costs attributable to the recognised body renewal process, which should be borne by firms in private practice, rather than by all practising certificate holders, many of whom are not in private practice.

Background

3. The Legal Services Act 2007 ("the Act") in permitting the Law Society (through the SRA) to regulate new forms of practice (legal disciplinary practices, or LDPs, owned and managed by different kinds of lawyers, with up to 25 per cent non-lawyer managers), changes the statutory powers so that both firms and individuals will be regulated. The Act requires all firms to be recognised bodies, and provides for a renewal process.
4. The SRA believes that firm based regulation is a more effective and efficient method of regulation and is necessary in the context of mixed practices involving, as owners and managers, individuals who are regulated by other professional bodies and those who are not otherwise regulated at all. The Act requires that same regulatory regime must apply to all firms, whether or not firms have taken other kinds of lawyers or non-lawyers as managers.
5. As explained in our strategic paper published in November 2007, the Act enables new forms of practice by amending the statutory powers in the Administration of Justice Act 1985 (AJA) relating to recognised bodies:
 - o by expanding those powers to include unincorporated partnerships;
and

¹ See www.sra.org.uk/sra/consultations/338.article.

- by extending the powers to allow for recognised bodies to be owned and managed by other lawyers as well as solicitors, and/or to have up to 25 per cent of non-lawyers as managers.
6. The SRA has now made, subject to statutory approval processes, the necessary amendments to the SRA's Code of Conduct, and the new SRA Recognised Body Regulations. The Code and Regulations, as made by the SRA Board, can be found at www.sra.org.uk/LSA. We hope that LDPs will be permitted from 1 March 2009, at which point "firm based" regulation will apply to all firms including partnerships. Existing partnerships will be passported into recognition and will not need to make an initial application.
 7. In addition, the Act changes the regulatory position of sole practitioners, who in future will need to seek and renew a "sole solicitor endorsement" in relation to each practising certificate. We refer to such sole practitioners as recognised sole practitioners. The necessary changes to the SRA Code of Conduct and new practising regulations have now been made, subject to statutory approval processes, and can be found at www.sra.org.uk/LSA. We expect that sole practitioners will need recognition from 1 July 2009. Existing sole practitioners will be passported into recognition and will not need to make an initial application.
 8. Currently the SRA conducts regulatory checks and fee collection mainly through the annual practising certificate exercise. The current additional recognised body process applies only to incorporated practices (companies and LLPs), and is "light touch", in that the information requirements are minimal and are checked only every three years. However, the Recognised Body Regulations, reflecting the changes in primary legislation, require recognised bodies, from March 2009, to seek annual renewal of recognition. The necessity for an annual process was discussed in consultation paper 8 - Changes in Regulatory Processes for Individuals and Firms - and the Recognised Body Regulations were drafted and consulted upon the basis that there would be annual renewal of recognition. This means that partnerships that are passported into recognition will need to renew recognition in October 2009, and any new firms setting up after 1 March 2009 will be recognised until that first renewal process.

Recognised body fees – the current position

9. Currently only companies and LLPs are required to be recognised bodies. There are about 2,300 recognised bodies. The fee on initial recognition is £900 for three years. That includes a periodic regulation fee of £500 and a compensation fund contribution of £400. Recognised bodies renew recognition every three years on the anniversary of their initial recognition and the combined renewal fee is also £900.
10. The justification for this standard fee was to recognise both the processing costs and the additional regulatory cost of regulating an entity. It was considered inappropriate for those costs to be borne by all practising certificate holders. There was no basis for introducing a graduated fee reflecting risk, the ability to pay or the cost of regulation, so a fixed rate standard fee was the appropriate way forward.

Transitional proposal for 2009 only

11. The Act will require all partnerships to be recognised bodies so there will no longer be an element of choice as to whether to become a recognised body. But the legislation also requires different regulation and administrative regulatory procedures to be applied to recognised bodies, and it is right to reflect those costs in a separate recognition fee for what will be a transitional period.
12. We therefore need to propose a fee to reflect the cost of recognising new firms created after 1 March 2009, and also an annual renewal fee for the first annual renewal exercise which takes place in October 2009. The annual renewal will apply to all recognised bodies, i.e. all partnerships, companies and LLPs, i.e. to about 11,000 firms. Renewal will be for one year only.
13. The SRA proposes that, transitionally, for 2009, a standard fee should continue to be applied to all recognised bodies on renewal – regardless of size and whether or not the recognised body is also an LDP with or without non-lawyer partners. The SRA proposes not to change the current basis for the fee, so that the combined annual fee should be £300 (i.e. £900 ÷ 3) made up of a periodic regulation fee of £180 and a compensation fund contribution of £120.
14. All new partnerships, companies or LLPs setting up after 1 March 2009 will need to make an initial application for recognition. It is proposed that the initial application fee should be the same as the renewal fee, as now – i.e. an annual fee of £300, but that a similar approach to practising certificate applications should be made in that the fee should be reduced according to the time of year the application is made. That would mean that applications made from 1 March 2009 to 30 June 2009 would be charged at a combined fee of £200 and applications from 1 July 2009 to 31 October 2009 would be charged a combined fee of £100.
15. All individual solicitors working in recognised bodies will continue to pay the annual practising certificate fee and compensation fund contributions. Often these fees are paid on behalf of the individuals by the firm in which they work.

Why has so little change been made for 2009?

16. The SRA are aware however that this proposal may be seen by some in the profession to be unfair given the fact that a number of recognised bodies setting up and renewing in 2009 will have non-solicitor managers. We cannot under the statute charge those non-solicitor managers any form of individual fee such as the practising certificate fee. The only way to cover the cost of an LDP in a way which would reflect the different structure would be to charge a different (i.e. higher) recognised body (initial or renewal) fee to recognised bodies if they have some non-solicitor managers. However, at present, our IT and finance systems would not support the ability to recognise different types of recognised body, and so calculate different fees on that basis.
17. The proposals in this paper represent the only realistic option open to the SRA as anything more complicated will involve considerable expense in adapting existing or developing new IT and finance systems to support

anything different. Any such change would be for one year only and so represent a one off, wholly disproportionate cost. The SRA considers that would be a waste of the profession's money. Work on developing a significantly different system for 2010 and for the future is more important and will require a considerable resource commitment by the SRA, supported by the Law Society Group finance and IT teams. The SRA do not believe that resource should be diverted to develop a different system for one year only in 2009. The transitional period during 2009 will provide time to develop new and improved systems for 2010 and beyond.

18. There is an argument that non-solicitor managers should be making a direct contribution. In fact, in the vast majority of cases the firms' owners (which will include any non-solicitor managers) fund the total cost of regulation for all in the firm from its gross profits and so do, in reality, bear the cost. While the proposals may create a small anomaly, the SRA considers that any alternative would lead to wasted costs which would be disproportionate to any benefit that might be gained. Also it must be borne in mind that the current system, in effect, apportions costs among firms on the basis of the number of practising certificate holders in each firm is more anomalous. It is that anomaly that will be addressed in the next consultation on fee structures for 2010 and beyond.

How does this affect existing recognised bodies?

19. Recognised bodies that already exist or have received initial recognition before March 2009 will have been recognised on a three-year rolling basis from the date of initial recognition. The Recognised Body Regulations contain transitional provisions (Regulation 8.6) which, when they come into force on 1 March 2009, will replace the current renewal date for bodies who received initial recognition or renewed their recognition on or after 1 November 2006, with a renewal date of 31 October 2009. The Regulation also provides that credit will be given for fees and contributions overpaid if and when such bodies apply for renewal of recognition in 2009. Recognised bodies which have set up or renewed since January 2008 have been warned about this possibility in correspondence. We are currently working on the process which will calculate and provide such credit.

Fees for the recognition of sole practitioners

20. The Solicitors Act 1974, as amended by the Legal Services Act, provides for the firm based regulation of sole practitioners through a process linked to the issue and renewal of practising certificates. It is the SRA's policy to apply the same principles of firm based regulation to sole practitioners as it applies to recognised bodies. The policy is in effect that sole practitioners should not be treated more or less favourably than other firms. However, instead of there being a distinct recognition fee for sole practitioners the statute gives the power to charge a differential practising certificate fee at the same time as renewal of the practising certificate and an additional fee where a solicitor applies for recognition ("endorsement" under the Act) during the currency of an existing practising certificate.

21. Given the policy position taken, the SRA proposes to recommend to the Council of the Law Society that recognised sole practitioners should be charged on the same basis as recognised bodies. This would mean that they would pay an additional combined fee of £300, over and above the normal practising certificate fee and compensation fund contribution, on renewal in 2009. This will affect about 4,500 sole practitioners.
22. It will mean that new sole practitioners setting up in practice between July 2009 and October 2009 would pay a proportion of £300, i.e. £100 for the initial period of that recognition.
23. The justification for charging a differential fee to sole practitioners is that the new process, required by legislation, carries some cost that is not attributable to all practising certificate holders, but only to those operating in sole practice.
24. This proposal is transitional for one year only and the future fee structure for sole practitioners from 2010 and beyond will be subject to further consultation.

Application fees for approval of non-lawyer managers

25. The SRA considers that the application fee for the approval of non-lawyer managers should, in principle, cover the administrative costs of that process, so that those firms who do not take on non-lawyers managers do not bear the cost. We are still working on the amount of the fee, and it is difficult, in the first year of a new application process, to accurately estimate the resource that will be required. The current application fee for admission, when similar checks on character and suitability are required, is £100 with an additional charge to cover an appeal.
26. The number of applications from non-lawyers will be much lower than those for admission, and so there will be fewer economies of scale, and some aspects of the process will require more work to be done. We therefore think that an initial fee of £250 can be justified, although this has to be an estimate. We are also proposing to charge an additional amount on an application for an appeal against a refusal as that is fairer than apportioning the cost of appeals among those applications that are straightforward.

Impact of proposals

27. This paper proposes some additional regulatory fees which will be at a flat rate, but comparatively low, for a transitional period. This fee could impact very small firms. Arguably, a fee which can take into account ability to pay can be fairer, although that is less justifiable, where a fee is intended to cover the cost of processing. The SRA also believes it would be disproportionate to add complexity to the fee calculation during this transitional period. These new processes, required by statute, will involve some additional processing cost. Charging nothing or less will mean that any additional costs are borne by solicitors who are not running their own business in private practice, such as in-house solicitors.

Questions

1. Please let us know if you agree or disagree with the SRA proposals in relation to fees to be charged transitionally in 2009. Please give reasons for your views.
2. In the light of the potential impact on small firms we would be interested in finding out what the impact will be on sole practitioners and small firms. We would, therefore, also like to hear from you about any concerns and views you may have on the equality impact of the fee proposals as set out in this consultation.

How to respond

For information on how to respond, please visit our website.

- Go to www.consultations.sra.org.uk.
- Select **Firm-based regulation – fee-raising policy for 2009**.
- Click **How to respond**.
- Alternatively, go to www.sra.org.uk/sra/consultations/1469.article#respond.

Submission deadline

The deadline for responses is **8 December 2008**.

The SRA Board must set these regulatory fees at its meeting in December 2008 in order that solicitors can be informed of the fees they will be required to pay in 2009. The transitional proposals involve no new change in policy.

As a result, the consultation period—four weeks—is substantially shorter than would otherwise be the case.