Report on responses to SRA consultation: Indicative Fining Guidance

Introduction

1. This report follows the SRA's consultation on indicative guidance on financial penalties, and includes the SRA's responses to the substantive issues raised by respondents.

2. We are grateful to respondents for their input and received some very constructive and helpful comments.

3. The consultation paper explained our thinking on how the guidance should be approached, and closed on 19 April 2013. The consultation contained 14 specific questions, and invited the respondents to comment on a range of issues. Relevant comments are summarised below.

Responses received

4. There were 7 responses to the consultation. The most detailed responses received were from:

   - the Law Society;
   - the City of London Law Society; and
   - the Solicitors Disciplinary Tribunal.

5. A full list of the respondents appears at the end of this report.

Overview of responses to individual questions

Responses to Question 1

"Do you agree that the SRA should adopt some form of guidance or guidelines to assist decision makers in determining an appropriate sum for financial penalties? Or do you feel that the existing Financial Penalty Criteria are sufficient?"

6. The majority of respondents, including a number of local law societies, were supportive of the SRA adopting such guidance.

7. Two respondents had concerns:

   - the Solicitors Disciplinary Tribunal (SDT) felt that the existing regulatory arrangements (in particular the Financial Penalty Criteria) were sufficient, save that in respect of criterion 2(d) which the SDT did not feel to be appropriate. The SDT commented that it does not seek to eliminate financial gain or other benefits obtained as a direct or indirect consequence of the misconduct in determining the level of fine;

   - the Law Society felt it was desirable to have guidance in relation to ABSs, but questioned the precise timing of implementation given the SRA's lack of experience at present in regulating such bodies.

SRA response:

8. We are encouraged that the majority of respondents were in favour of adopting indicative fining guidance.

9. While the Financial Penalty Criteria is helpful in setting the overarching and high level principles for arriving at an appropriate sum to a fine a regulated person, we feel that fining guidelines will assist decision makers to determine specific figures.

10. The SRA has previously consulted upon and adopted Financial Penalty Criteria which provide that, as far as practicable, a financial penalty should remove any benefit or gain which would otherwise arise from the conduct in question. This approach is consistent with good regulatory practice and in particular the penalty principles set out by Professor Richard B Macrory in his 2006 report to the government entitled 'Regulatory Justice: Making Sanctions Effective' (PDF 133 pages, 463K). While we note the SDT's comments on the approach it adopts in this respect in matters where the SRA is not the first instance decision maker the SRA does not agree with this. Ultimately the point may need to be tested in the Courts, though we consider that the position is clear for decisions and appeals made where the SRA is the first instance decision maker because the SRA Disciplinary Procedure Rules specifically address the issue.

11. We note the concerns raised by the Law Society as to timing but do not agree with the assertions made. We feel that if guidance is needed by decision makers then it should be available when disciplinary decisions start being taken. Most respondents agreed with this approach.

12. The draft guidance has been informed by the work and experiences of other regulators and will now be developed following consideration of the responses to our consultation. However we shall continue to review the ongoing impact of the guidance in relation to its implementation.

Responses to Question 2

"Do you agree that the guidance should be broad rather than attempting to categorise every type of misconduct which could occur in a law firm?"

13. There was strong support amongst the respondents that the guidance should adopt a flexible approach.

Responses to Question 3

"Do you agree that a staged process for assessing penalties, by which a basic penalty is arrived at and then adjusted for relevant factors such as mitigation, is sensible? Or do you favour an alternative approach (if so, please tell us about it)?"

14. Broadly speaking the responses we received from the respondents were positive, and supported the SRA's staged approach for assessing penalties.

15. Some respondents however did raise concerns. One of the local law societies agreed in principle to the three step process but was apprehensive about whether sufficient emphasis was given to the nature of the relevant conduct.

16. The SDT felt that the guidance may give decision makers too much discretion to achieve the consistency sought.

17. In addition, the SDT suggested that the staged process had not taken into account how decision makers should approach a case where there are multiple allegations of misconduct. Under such circumstances the SDT was concerned that there was a danger that where some (or all) of the allegations are found proved a disproportionate and unjust sanction could be imposed for each allegation rather than taking the 'case' as a whole.

18. The Law Society felt that it was unable to provide any comments on the staged process, as it felt that the "***SRA has provided limited information on which to base any decision***", including on how other regulators approached this issue.

SRA response:

19. We recognise the concerns raised by the SDT on the issue of whether the process is able to apply to multiple allegations of misconduct. There is existing guidance on the SRA website which sets out its approach under the Disciplinary Procedure Rules. This clarifies that the SRA will where appropriate (in accordance with the guidance) group allegations together and levy a fine in the 'case' as a whole rather than, for example, each breach of a rule or regulation. It is proposed that the draft guidance should be amended to include a link to the relevant information on the website has been inserted into the draft indicative fining guidance.

20. We accept that there is a significant degree of discretion which remains with the decision maker. This is however intentional. It should be remembered that the consultation does relate to guidance rather than revisiting the rules on imposing penalties. We feel that the balance in our revised guidance between guiding decision makes on a consistent approach and allowing sufficient discretion to achieve the aims of the Financial Penalty Criteria is at the right level. We plan to review the operation of the guidance however in due course to reassess how this has operated in practice.

Responses to Question 4

"Do you favour categorising conduct as a list of characteristics or do you agree that it is sensible to distinguish between the nature of the conduct and the harm caused as proposed in our guidance?"

21. There were a number of substantive responses to this question which in broad terms were positive and supportive of the SRA approach.

22. The City of London Law Society (CLLS) was concerned however that the proposed approach to assessing "harm" focused too heavily on the financial loss caused, which it felt was in contrast to the SDT's approach of having regard to harm caused to the profession as a whole.

23. The Law Society felt that it was unable to provide any substantive comments on the basis that "***the SRA have not provided no information on what the list of characteristics might*** be".

SRA response:

24. We are generally encouraged by the responses received, which broadly appear to support the approach proposed.

25. Having considered the comments made about the term 'harm' some changes are proposed to the draft guidance to provide decision makers with more guidance on what to consider in this context.

Responses to Question 5

"Do you feel that the method for assessing the seriousness of the misconduct is clearly set out in the illustration at Annex 1? Do you have any suggestions on how this might be improved?"

26. There was broad consensus from a number of respondents to the methodology that has been proposed in assessing seriousness of misconduct.

27. The concerns raised about what is relevant to the 'harm' caused by a regulated person has been discussed above.

28. The Law Society observed that "***sanction should reflect the level of fault, rather than the measure of loss given that redress is essentially a matter for the Legal Ombudsman"***.

29. The Law Society and the CLLS felt that mitigating factors should be considered in step 1 rather than as a 'secondary consideration' in step 2.

30. The SDT was concerned with the inconsistency of the use of words such as "other gain", "benefit" and "financial gain or benefit" interchangeably, as they are not defined.

SRA response:

31. We welcome the range of views and comments we have received from respondents on the proposed approach to assessing the seriousness of misconduct.

32. The SRA has previously consulted upon and adopted Financial Penalty Criteria which provide that the harm caused by the conduct of a regulated person will be a key consideration. We consider that that is the correct approach. Similarly, we feel that aggravating factors such as a failure to co-operate with the SRA's investigation is a relevant and important consideration.

33. In terms of when mitigating factors should be considered, the aim of the guidance is to encourage decision makers to follow a consistent and transparent process for assessing a financial penalty which meets the requirements of the Financial Penalty Criteria. It may be possible for decision makers to assess more factors or all relevant factors at once. However, the seriousness of the conduct, the aggravating factors, the mitigating factors, the means of the regulated person and whether the regulated person has benefited from the conduct will all need to be considered and a penalty which meets the Financial Penalty Criteria will be arrived at. The benefit of encouraging decision makers to do this as part of a step-by-step approach however is the transparency of the process and the opportunity to maximise consistency in the imposition of penalties. We are therefore proposing to retain this approach.

34. Amendments have been proposed to the guidance to improve the consistency of the language used in respect of the removal of benefits arising from the misconduct.

Responses to Question 6

"What do you think is the best way to determine financial penalties:

- **as fixed monetary sums;**
- **as a percentage of income or turnover;**
- **a mixture of the two as described above; or**
- **some other way (please provide details)."**

35. The SDT was not in favour of any one particular methodology, as it felt that each case should be assessed on its own facts and merits. The Law Society expressed a similar view.

36. Broadly however there was strong support from many of the respondents for introducing a mixed model for assessing financial penalties. One of the local law societies mentioned that adopting a rigid approach of either a fixed monetary sum or a penalty by reference to percentage of income or turnover may result in a disproportionate sanction.

SRA response:

37. We are encouraged by the broad support for the proposals made in this respect and propose to adopt the proposals made in the consultation in this respect.

Responses to Question 7

"Do you agree that a distinction should be made between firms of greater means and other firms? If so, what level of domestic turnover do you think should be used to distinguish firms of greater means from other firms? Or do you think that there should be different categories which taper the percentage applied?"

38. Broadly speaking respondents were in favour of the proposed approach. The CLLS however did raise concerns about applying any form of distinction between firms based on turnover.

39. In the SDT's view each case should be reviewed on the specific facts. The SDT commented that their judicial experience of hearing cases would draw out the necessary distinction between firms of greater means and other firms.

SRA response:

40. We are encouraged by the responses received but note the concerns raised by the CLLS.

41. We remain of the view that in order to achieve credible deterrence it is important that regulated persons of greater means can be fined sums proportionate to their means. The SRA will already have firm turnover information available to it and we consider this to be a sufficiently reliable indicator of financial means. Decision makers will however retain broad discretion in seeking to achieve the objectives of the Financial Penalty Criteria and some guidance is provided to decision makers in this respect within the draft document.

Responses to Question 8

"Do you agree that one approach to fines should be adopted for firms and individuals?"

42. There was a strong consensus amongst the respondents that one approach should be taken for both firms and individuals.

43. One of the respondents, a law firm, commented that determining the means of individuals would be a complex and time consuming exercise, making the acute observation that 'Step 1(c)' enables the decision makers to take account of the means of the paying party.

44. We are encouraged by the responses received in this respect.

Responses to Question 9

"Do you agree with the proposal that individuals such as solicitors should not usually be fined a percentage of their income?"

45. There was unanimous agreement from the substantive responses we received in favour of individuals not being fined a percentage of their income.

Responses to Question 10

"What do you feel is the appropriate range within which the SRA should impose fines on regulated persons taking into account the SRA's three objectives in this respect?"

46. The question of at what level to set the parameters for deciding the starting point of the fine ('the basic penalty') received less attention in consultation responses than we had anticipated.

47. One of the respondents, a law firm, suggested a range from £0 to £50,000. One of the local law societies agreed with the various penalty ranges as a 'starting point' but felt that consideration should be given to whether a form of cap (or similar) should be included.

48. The CLLS was concerned that a fine as high as 10% of turnover may threaten a firm's ability to continue trading. The CLLS felt that if a cap is not set at an appropriate level then it was suggested "***that the maximum percentage needs to be significantly reduced, perhaps to 2.5%.***".

49. Other than the response submitted by the CLLS there was not significant support for capping or tapering the basic penalties with one respondent commenting that tapering would make the process overly complex.

50. The SDT was not convinced that it was right to have a range of fines, as each case should be assessed on its own merits. As indicated earlier in this report the SDT considered the existing Financial Penalty Criteria is sufficient, which

does not include any range of fines.

SRA response:

51. We believe that setting an appropriate level of penalties within indicative fining guidance is an important part of our enforcement strategy and in particular to delivering a credible deterrence against conduct which poses a risk to clients and others.

52. Having reviewed our objectives for setting the parameters for the basic penalty and the responses received to the consultation, we feel that 0-£50,000 is an appropriate band to guide decision makers towards as a basic monetary penalty.

53. In terms of fines for firms of greater means, while we are conscious of the need for fines to act as a credible deterrent for all firms, we note and appreciate the concerns raised about the higher percentages consulted upon and the potentially unnecessary complexities of tapering and capping fines. Overall, we consider that fines of up to 2.5% of domestic turnover could represent a credible deterrent for firms of greater means. For example, for a firm with a turnover of £10 million a 2.5% fine would be £250,000 and for a firm with a turnover of £50 million it would be £1.25 million.

54. The potential for improper benefits arising from the misconduct to be removed in addition would also increase deterrent value and increase public confidence in cases where otherwise there may be concern. For example, where significant profits had been generated by improper conduct the decision maker would give consideration to levying a fine at a level which eliminated such benefits (step 3) in addition to the basic penalty (step 1). In practice it is anticipated that it is this third step of the fining guidance which will result in the highest penalties being imposed rather than fines within the parameters of the basic penalty at step 1 discussed here.

55. We are therefore proposing to suggest to decision makers within the guidance 2.5% of domestic turnover as the upper limit for fines imposed as a percentage of domestic turnover (i.e. for firms of greater means and before the potential adjustments to the penalty envisaged in steps 2 and 3 of the process).

56. In direct contrast to the points raised by the CLLS, the Law Society raised concern about the fairness of the proposals on smaller firms and firms with low turnover potentially being subject to fines representing a greater proportion of their turnover than for larger firms. The Law Society expressed concern about the potential for an impact on BME lawyers. BME lawyers are known to be disproportionately represented in smaller 'traditional' law firms (though there is currently only a small number small law firms which are ABSs).

57. The draft guidance does allow for exceptions to be made for firms of lesser means as well as greater means in keeping with the principles set out in the financial penalty criteria. Regulated persons can make representations to the SRA on financial means for this to be considered and there is a process for the SRA seeking this information set out in the SRA Disciplinary Procedure Rules. We feel that this is the appropriate mechanism to maximise the proportionality

of penalties to the means of the paying party (as well as the other aims of the Financial Penalty Criteria) without undertaking disproportionate financial assessments in every case.

58. The guidance is currently most relevant to ABSs rather than 'traditional' law firms and it is difficult at this stage to anticipate what proportion of firms fined in line with the guidance will represent a particular equality strand. However, we intend to conduct a more detailed equality assessment once we have outcomes and data available on the effects of the guidance in practice.

Responses to Questions 11 & 12

Q.11. "Do you agree that the SRA should discount financial penalties to take account of mitigating factors? In particular, do you agree that the SRA should discount penalties for:

the early reporting and full admission of conduct?
promptly correcting any harm which has been caused?"

Q.12. "Do you consider that the percentages proposed for discounts are set at an appropriate level? Or do you consider that some or all of the percentages set out in the illustration at Annex 1 should be higher or lower?"

59. We have received substantive response from a number of respondents in favour of introducing discounted financial penalties on the basis of mitigating factors.

The key concerns that were raised were around the issue of timing, and whether mitigation and intent should be integrated into the initial assessment of the seriousness of the misconduct at 'step 1'. One respondent felt that in the proposals made mitigating factors were 'marginalised' to a later stage after an initial decision on penalty had been made.

The Law Society was also concerned with reference to the guidance proposed to be given to decision makers about mitigating factors that "***regulated persons should not be put in a position where they believe they must admit all allegations even where they believe some are incorrect.***" The Law Society also questioned why the guidance appeared in their view to be suggesting that reporting matters to the SRA and full admission was necessary to constitute mitigation.

We received a mixed response from respondents on the issue of the level of the proposed discounts (question 12). Some stakeholders raised concern about the proposal to allow up to a 40% discount in respect of a basic penalty. The SDT in particular raised concern about the impact which this may have on the public confidence in the regulation of legal services. However, other stakeholders were more supportive of the proposals and appeared to recognise the need for significant incentives to change behaviour in this area.

SRA response:

60. The aim of the guidance is to encourage decision makers to follow a consistent and transparent process for assessing a financial penalty which meets the requirements of the Financial Penalty Criteria. It may be possible for decision makers to assess more factors or all relevant factors at once. However, the seriousness of the conduct, the aggravating factors, the mitigating factors, the means of the regulated person and whether the regulated person has benefited from the conduct will all need to be considered and a penalty which meets the Financial Penalty Criteria will be arrived at. The benefit of encouraging decision makers to do this as part of a step-by-step approach however is the transparency of the process and the opportunity to maximise consistency in the imposition of penalties. In our view therefore decision makers should be encouraged to determine basic penalties in a methodological way.

61. In terms of the suggestion that the SRA would be requiring admissions for allegations which are felt to be incorrect, regulated persons would of course remain free to make representations and demonstrate that an allegation is incorrect. We consider it unlikely that a regulated person would admit misconduct in order to receive a discount on a penalty of up to 25% if they considered it likely that a finding of misconduct and a penalty would be avoided altogether. The intention is to encourage early resolution of disciplinary matters in appropriate cases to reduce costs. Models for discounting sanctions in recognition of early admissions are well established in criminal law (where the liberty of the individual is at stake) and in regulation. We are therefore not proposing changes in this respect.

62. In terms of requiring admissions of misconduct generally, the suggested discounts detailed at step 2 of the draft guidance are not an exhaustive list of mitigating factors. They are examples of behaviours which the SRA wishes to highlight as important mitigating factors to encourage behaviours which contribute to effective resolution of conduct matters in the public interest. However, it should be remembered that regulated persons generally do have conduct duties to report misconduct to the SRA. Regulated persons are therefore already required to report matters to the SRA. Reporting and admitting the conduct at an early stage however would go beyond the conduct requirements.

63. In terms of the concerns raised by the SDT, we remain of the view that significant discounts could deliver great benefit in increasing reports of misconduct to the SRA and speeding up the resolution of problems for clients. However, we do recognise that public confidence in the provision of legal services requires a credible deterrent against serious misconduct. We are therefore proposing to expand the section of the guidance which stresses that discounts should not be made to such a level that on the facts the overarching aims are defeated.

Responses to Question 13

"Do you have any comments on our proposed approach to removing profit or gain which has arisen as a result of misconduct?"

64. Though we were not consulting upon the principle of removing benefits arising from misconduct (which has been consulted upon previously and now forms part of the SRA Disciplinary Procedure Rules) we received a number of positive responses from respondents who believed that our proposed approach was clear and fair.

65. Two respondents did raise concern with this principle and reference is made to our response to question 1 above in this respect.

66. The Law Society asked for further clarity on how this approach would work in practice, and consult further before adding any further stages. They observed that if a firm has made a profit while breaching the regulatory requirements it does not follow that all of the profit relates to the breach and therefore should be removed.

SRA response:

67. We are encouraged by the responses received.

68. The SRA's existing Financial Penalty Criteria provide that, as far as practicable, a financial penalty should remove any benefit or gain which would otherwise arise from the conduct in question. This approach is consistent with good regulatory practice.

69. While we consider it important that the guidance remains broad in nature, we are proposing to add to the guidance to assist decision makers further in assessing the benefits arising from misconduct. This would include encouraging caution where there is difficulty in confidently quantifying the benefit arising taking into account completeness and reliability of information available. We do not consider it necessary to have a separate consultation in this respect. The principle is already established and we feel that only small revisions to the guidance consulted upon previously are needed to provide decision makers with the level of guidance necessary to address the concerns raised. In appropriate cases SRA staff will seek information on the financial gain or other benefit arising as part of the investigation.

Responses to Question 14

"Do you consider that guidance of this nature is likely to have a negative impact upon a specific section of the legal service market and in particular a specific equality strand?"

70. A small number of respondents were concerned that large highly resourced firms are likely to be in a better position to promptly investigate and remedy misconduct, and are therefore more likely to benefit from the discounting built into the assessment process than smaller firms, which tend to have a disproportionately high representation of BME. Smaller firms may therefore have proportionally larger fines imposed.

71. Interestingly one respondent took the opposite view and felt that larger firms would be unfairly treated under the proposals made.

SRA response:

72. Reference is made to the comments made in respect of question 10 above. We do not anticipate that the guidance will have a negative impact upon any section of the legal service market though we accept that there is currently limited information available to make a detailed assessment of this. We will keep the policy under review and conduct a more in-depth equality impact assessment once further evidence is to hand in this respect.

List of respondents

- The Law Society
- The City of London Law Society
- Newcastle upon Tyne Law Society
- Cardiff and District Law Society
- Solicitors Disciplinary Tribunal
- Penningtons Solicitors LLP

There was one anonymous response received from a law firm.