Consultation Paper

Proposal to increase the SRA's internal fining powers

1. The Solicitors Regulation Authority (SRA) is the independent regulatory body of the Law Society of England and Wales. We protect the public by regulating law firms and individuals who provide legal services.

2. As part of this role, the SRA has responsibility for investigating failures to meet the regulatory standards set out in our Handbook. The SRA's effective, consistent and proportionate use of its enforcement powers, including imposing fines, plays a vital role in ensuring a credible deterrence against unacceptable behaviours and furthers the regulatory objectives and professional principles in the Legal Services Act 2007 (LSA).

3. This consultation paper invites views on our proposal to increase the current level of our fining powers for 'traditional' law firms from their current level of £2,000. The purpose of this consultation is to obtain your feedback on our proposed approach. Your input will assist us to assess views upon our proposals and how they can be taken forward.

Current fining powers

4. Since December 2011, we have been responsible for regulating two types of law firms:

   - 'traditional' law firms, which are generally owned and managed by solicitors; and
   - Alterative Business Structures (ABSs), which are law firms that are authorised to have investment by non lawyers and non legal businesses.

5. Our regulatory and disciplinary powers and procedures vary dependent upon whether the firm is a traditional law firm or an ABS.

6. At present, s44D of the Solicitors Act 1974 (SA) limits our 'in - house' fining powers for solicitors and traditional law firms for misconduct or breaches of regulatory requirements to £2,000. If we consider that a greater fine is appropriate then a referral must be made to the Solicitors Disciplinary Tribunal (SDT). The SDT is an independent tribunal that has had, since 2009, unlimited fining powers.

7. In contrast to the limit on our powers to fine traditional law firms only up to £2,000, we can under the LSA 2007 regime:

   - fine a manager or an employee of an ABS up to £50 million;
   - fine the ABS itself up to £250 million.

   These limits were set by the overarching regulator for legal services, the Legal Services Board (LSB), after consultation and apply to all of the Approved Regulators.

8. Prior to the increased fining powers for ABSs coming into force, we comprehensively reviewed our approach to how we would impose financial penalties in-house. The rules we brought in as a result (the SRA Disciplinary Proceedings Rules 2011) provide guidelines as to when a fine should be imposed for both ABSs and for traditional law firms (up to the current fining limit of £2,000). We have also recently consulted upon, and have now published, detailed Indicative Fining Guidance which guides decision makers to penalty bands within which to levy a fine (see http://www.sra.org.uk/financialpenalties).

9. We have three main concerns about the current position:

- there is a risk of perceived absurdity and unfairness in the lack of consistency between how traditional law firms are disciplined following a prosecution before the SDT and how potentially very similar firms (ABSs) are disciplined internally by the SRA;

- we are considerably limited in the scope of matters which can be dealt with without a prosecution before the SDT;

- the current regime fails to take advantage of the fact that a considerably quicker, cheaper and more proportionate regime for levying fines against law firms is already in place for ABSs. Applying the ABS fining regime more widely could save considerable time, stress and cost for regulated persons as well as result in efficiency and cost savings for the SRA and therefore for the profession which ultimately funds us.

Our initial proposals to increase fining powers

10. In 2010, we therefore sought stakeholder views on the proposal that we should have the same level of fining powers for traditional law firms as we would have for ABSs. Those responding to the consultation were broadly supportive of the proposal and there was overwhelming support in general for our having harmonised powers and processes.

11. Subsequently we proposed to the Ministry of Justice (MoJ), the Law Society, the LSB and the SDT that the SRA should have fining powers of up to £250 million for firms and £50 million for individuals in all types of law firm we regulate, not just ABSs.

12. In summary, the LSB supports our proposal for an increase to a commensurate level, the SDT does not and the Law Society has indicated that it may not object to some degree of increase. More information about the range of views held by the stakeholders we have already discussed this issue with is provided below.

13. The MoJ concluded that changes to primary legislation would be required to increase the fining levels to a commensurate level as it is such a significant sum. However, it has indicated that, with an appropriate business case, a more modest increase to the fining powers would be possible[1].

Our current proposal to increase fining powers

14. While we firmly remain of the view that our having commensurate fining powers would be the best outcome, we are interested in seeking stakeholder views on more conservative changes, the benefits of which could hopefully be obtained much more quickly.

15. This consultation therefore seeks stakeholders' views on two proposals:

a) to increase our fining powers for traditional law firms either:

[1] By order of the Lord Chancellor, under section 44D(10) of the Solicitors Act 1974.

i. from £2,000 to a new limit of £10,000;
ii. from £2,000 to a new limit of £50,000; or
iii. from £2,000 to a new limit of £100,000; or
iv. on a different limit to that proposed; and

b) to enable the SRA to agree (rather than impose) fines of a more significant amount with the regulated person concerned under our existing policy of agreeing the outcome of an investigation under our Regulatory Settlement Agreements policy.

Why increase our fining powers for the 'traditional' regime?

Efficiency and proportionality

16. We estimate that disciplinary matters which involve a fine being imposed or agreed to by the SRA rather than by the SDT would generally:

a) be resolved approximately 10 months quicker[2]; and
b) result in the regulated person paying legal costs which are cheaper by a sum in the region of £8,000, and often much more[3].

17. As well as saving on time, stress and legal costs for the regulated person, applying the ABS regime would also be considerably more efficient (for example, in the amounts of unrecovered legal costs we have to bear) and result in a costs saving for the wider legal services market in terms of the fees paid to the regulator.

18. The table below sets out an analysis, based on our records, of the number of matters referred to the SDT that resulted in fines being levied by the SDT in the years 2010, 2011 and 2012 :-

Fine bands	**2010**	**2011**	**2012**
£0 - £2,000	20	25	22
£2,001 - £10,000	66	65	60
£10,001 upwards	40	18	12
Total	**126**	**108**	**94**

19. In 2012, 87% of the fines imposed in the SDT were for £10,000 or less compared with a mode average costs order in favour of the SRA of £10,589 (the median average was £7,500). It is reasonable to assume that in most cases the individual or firm concerned also incurred significant legal costs in defending the matter at the SDT. While costs orders are made where a fine is imposed internally by the SRA under our current Cost of Investigations Regulations, the time and expense involved is considerably less and would therefore represent a more proportionate means of resolving the matter.

20. According to our analysis of our data, to 30 July 2013, fines were imposed in 41 cases before the SDT:-

[2] The average length of a SDT prosecution in 2012 was a little over 10 months whereas under the ABS regime the SRA would make the decision in house.
[3] In 2011, the median average costs order made by the SDT where a fine was imposed by the SDT was £8,500 (the mean was £11,139) and in 2012, the median was £7,500 (the mean was £10,589).

Fine bands	To 30 July 2013	Total amount of fines per bracket	Total associated costs ordered by the SDT	Average costs awarded per band
£0 - £2,000	14	£24,000	£ 44,500	£3,179
£2,001 - £10,000	22	£64,000	£190,433	£8,656
£10,001 - £20,000	4	£60,000	£107,050	£26,762
£20,001 plus	1	£40,000[4]	£35, 000	£35,000
Total	41	£184,000	£336,983	

21 In 12 of the 41 cases referred to above, orders were made by the SDT for the costs orders not be enforced without the SDT's leave, totalling £109,756 or 32.5% of all costs orders made. There is also often a significant difference between the costs we actually incur in the prosecution and the amount awarded in our favour and the costs awarded and the costs we actually recover.

22. A more detailed example to illustrate to stakeholders how the difference may result in differences in costs and efficiency is set out in **Appendix 1**. While this is a hypothetical example, it has been based on the data available as to the average time and costs spent in disciplinary matters involving a fine.

Consistency and fairness

23. We are conscious that some stakeholders will consider it very unfair that disciplinary matters involving an ABS can be brought to a conclusion more quickly and with less legal costs being incurred than would be the case for disciplinary matters involving traditional law firms, particularly where both the nature of the firm and the misconduct in question are very similar. When an alternative system exists for more efficient resolution of disciplinary matters, stakeholders will inevitably question why hundreds of thousands of pounds should be spent each year on pursuing firms through a separate, more costly regime.

24. We are also conscious that there may be a perception of inconsistency between decisions on potentially very similar facts between the SDT and the SRA, particularly owing to the inherent differences between the two regimes such as the consideration of oral evidence at the SDT (which is rare in SRA matters). A summary of the main differences are set out in **Appendix 2**.

25. We believe that increasing our ability to impose fines will increase the consistency of decision-making and mitigate against the risk of stakeholder concern about the differences between the two regimes.

Regulatory arbitrage

26. We also have concerns that important decisions about business models may be influenced by perceptions of whether the traditional or ABS regulatory regime is preferable. This is known as regulatory arbitrage and is highly undesirable. The risk of regulatory arbitrage could be mitigated against significantly by more closely aligning the fining regimes between traditional law firms and ABSs.

[4] The fine of £40,000 and associated costs were an agreed outcome between us and the respondent that the SDT consented to (see paragraph 36 below)

Question 1 - Do you agree with our analysis of the benefits that would flow from an increase in our in-house fining powers around the areas of efficiency and proportionality, consistency and fairness and regulatory arbitrage?

What are the risks of increasing fining powers?

Independence of the disciplinary decision-maker

27. When discussing with stakeholders the prospect of our having commensurate fining powers, some stakeholders have raised concerns about 'due process'. In particular, a concern has been raised about whether we can objectively make fair and impartial disciplinary decisions in respect of investigations which we have both instigated and led.

28. While we acknowledge the concern, it is important to note that any decisions to fine in-house are made by our adjudication function, which is functionally separate from our investigative units. Adjudicators work to a published decision-making framework, underpinned by transparent decision-making criteria. All decisions to fine also carry an internal right of appeal from the decision-maker - in the case of fines - by an Adjudicator to an Adjudication Panel, comprising normally 3 SRA internal and external adjudicators, both legally qualified and lay. In addition and most importantly, regulated persons would retain the ability to refer the matter to the SDT for review on appeal. All fines imposed by the SRA under both regimes (ABS and traditional) are fully appealable to the SDT. If the regulated person considers that the time and cost should be incurred for the matter to be heard by the SDT, then that can be achieved on appeal. What our current proposals would allow, however, is for many other cases to be dealt with much more efficiently and at a significant cost saving. In case there is any doubt, we confirm that any fines we recover are required by statute to be paid by us to the Government.

29. It is also relevant that much more significant fining powers amongst regulators is very common in other regimes, such as the Financial Conduct Authority. The other Approved Regulators under the LSA are another example so:-

- section 26(1)(e) of the Administration of Justice Act 1985 allows the Council of Licensed Conveyancers (CLC) to set their own limit for fining recognised bodies (the equivalent to traditional law firms) they regulate which is currently set at £1 million. The CLC also recently consulted on increasing this amount to the same level as they have for ABSs ie £250 million. They received 27 responses and 71% of the respondents agreed to the proposal that the maximum penalty should be increased to £250m that is, to the same as the maximum penalty which can be awarded against an ABS regulated by the CLC.
- the Bar Standards Board (BSB) has the power to impose fines of up to £15,000;
- The Disciplinary Tribunal of ILEX Professional Standards (IPS) has the power to impose a fine although this is currently limited to £3,000.

30. The Legal Ombudsman also has the power to order payments in respect of inadequate professional services of up to £50,000.

31. We do not suggest that we would wish to exercise the wide range of other powers that the SDT has, in particular its powers to strike off or suspend solicitors from the Roll or to make orders under s 43 of the SA in appropriate cases. We are only concerned here with financial penalties. As stated above in all cases, the relevant individual would have both an internal and an external right of appeal in full to the SDT.

ABSs requiring higher penalties

32. One point that has been made to us by some stakeholders in the context of our proposal to seek commensurate fining powers is that higher penalties are necessary within the ABS regime because ABSs are of higher means or may be less deterred from misconduct by the prospect of being removed from future legal practice than a solicitor would.

33. We do have significant concerns with this analysis. A number of traditional law firms in England and Wales have global turnovers in excess of one billion pounds. In contrast, many ABSs we license are of comparatively low means, more closely resembling traditional law firms in structure, with 2 or 3 partners, rather than the model of a substantial corporate ABS. If financial means is a relevant consideration in a particular case then our rules provide that this will be taken into account by the decision-maker in question – regardless of the structure of the law firm.

34. Our view therefore is that ABSs do not require higher penalties than traditional law firms but we would be interested in views upon this suggestion.

Question 2 - Do you have any other views about the issues or risks that might flow from an increase in our in-house fining powers?

What level should our fining powers be increased to?

35. We would be interested in stakeholders' views about what is the right amount to suggest our fining powers are increased to, if some increase were to occur.

36. For example, using some straightforward banding as possible options:-

Possible option 1 - an increase from £2,000 of up to £10,000. In terms of our overall enforcement powers, this may be regarded by some stakeholders as a modest increase in our ability to fine. We note, however, that according to our data, the impact on the number of cases that might be referred to the SDT as a result is likely to be quite substantial, as it would (at its simplest analysis) have allowed us to impose fines in 90 cases in 2011, 82 cases in 2012 and to 30 July 2013, 36 out of 41 cases.

Possible option 2 - an increase from £2,000 of up to £50,000. In terms of our overall enforcement powers, this may be regarded as significant, and in our view would represent a meaningful increase in our powers. The impact on the number of cases referred to the SDT is likely to be very significant – there were an additional 11 cases in this bracket in 2011 and 9 cases in 2012.

Possible option 3 – an increase from £2,000 of up to £100,000. The largest fine imposed by the SDT (since it acquired the ability to impose unlimited fines in 2009) has been £50,000. The effect of any such increase would be that we would have been able to impose all of the fines so far imposed by the SDT in-house although the SDT would retain the power to impose any fines over this amount if it was considered appropriate.

37. Over 87% of all of the fines imposed by the SDT in 2012 were less than £10,000. In 2010 this figure was 68% and in 2011, 83%. An increase in the £2,000 limit to, say, £10,000, would therefore, in our view, have a positive impact upon our ability to improve the speed and efficiency of the imposition of financial penalties as well as substantially reducing the costs borne by both parties. Any such increase would also impact the number of cases dealt with by the SDT at first instance. Greater increases would similarly, in our view, improve efficiency and consistency – it is interesting to note that the average cost order

made in the SRA's favour over the 4 cases in the £10-20,000 bracket (to 30 July 2013) was £26,732. If a firm or individual does in fact wish for the matter to be heard before the SDT, then there is an external right of appeal to the SDT in all cases in order for this to occur. We accept that the costs that may be incurred in pursuing an appeal to the SDT may deter some from doing so but we remain of the view that overall, under our proposals, such matters would be dealt with more quickly and with less cost.

38. It is also worth pointing out that in the more serious disciplinary matters involving an individual where a large fine is likely to be imposed, we might choose to prosecute the matter before the SDT in case the appropriate sanction ordered by the SDT was a period of suspension (which we cannot or do not propose that we should be able to impose). In addition, a number of prosecutions involve multiple entities and individuals, such as several partners and employees in a firm and we may refer those matters to the SDT, even where the lesser culpability of those involved, once tested, may result in a lower fine so that the evidence can be reviewed as a whole.

Question 3- We are keen to hear the views of our stakeholders on possible increases of:

(a) up to £10,000;
(b) up to £50,000;
(c) up to £100,000; or
(d) do you have views on any other potential increase bands?

Imposing higher fines by agreement

39. One of the clearest impacts of the low level of fines available to us is on our ability to enter into proportionate and effective Regulatory Settlement Agreements (RSAs). Since 2008 we have operated a policy under which we can agree the outcome of an investigation in the public interest with those we regulate. We have entered into 111 RSAs with 246 individuals covering a wide range of different issues. The RSAs contain a range of outcomes, including admissions, practising certificate controls and undertakings to repay affected clients monies due to them. They also contain disciplinary sanctions such as rebukes and fines. The vast majority of RSAs have been made public on our website.

40. As we move to a full risk-based approach we are finding that an increasing number of those we regulate would like to reach an outcome with us that involves payment of a fine in excess of our statutory limit of £2,000. Such firms or individuals accept that there has been a breach of our rules and the proper result is a financial penalty to reflect the gravity of the misconduct. However, in the absence of being able to agree a penalty of more than £2,000, we have no option but to prosecute the matter before the SDT. We have recently been exploring with the SDT the most effective way in which we can put before the Tribunal an agreed outcome, covering for example admissions, mitigation and an agreed sanction. In one recent case in 2013 the respondent agreed to a fine of £40,000 and to pay our costs of £35,000.

41. However, the question arises - if the regulated person (which could be a firm or individual) wants to accept a penalty of, say, £30,000 and the regulator feels it is the most appropriate outcome, why should the matter have to be referred to the SDT for consideration and approval with its inevitable attendant delays and costs implications? In our view it is clearly against the public and indeed the regulated person's interest that these matters cannot be agreed at an early stage.

42. If any eventual increase in our fining powers that the MoJ was prepared to recommend is relatively low, to address this risk we could also seek a change to our powers as set out in the Solicitors Act to allow us to impose larger fines by agreement with the regulated person.

We consider this may be achievable without primary legislative change but are seeking the MoJ's views on the best way to approach this.

Question 4 - **Do you agree that we should explore increasing our ability to agree higher fines with those we regulate? Do you have any views on whether this figure should be capped to say, £1 million or should be unlimited?**

Question 5 - Do you have any other views or comments on this consultation that you think we should consider?

Diversity and inclusion

43. We do not anticipate at this stage that an increase in our fining powers would have a negative impact in terms of diversity and inclusion considerations. We feel an increase in our fining powers will assist in providing a consistent and fair fining regime and will not have a negative impact in terms of equality and diversity. However, we are very keen to receive your feedback on the potential impact of the proposed approach and your views or suggestions as to how this might be mitigated.

Question 6: Do you consider that an increase in our fining powers is likely to have a negative impact upon a specific section of the legal service market and in particular a specific equality strand?

Appendix 1

Hypothetical example

Background facts

In January 2013, the SRA discovers that two firms – Lawyeronly co (a traditional law firm) and ABS2B Co (an ABS of similar size and financial means) – have been involved in the same referral arrangement for new clients in conveyancing transactions. The arrangement is a new but growing scheme. The arrangement involved some inappropriate costs being passed on to the clients of the firms direct in order that the introducer of business may make a profit from the arrangement. The scheme was new and so relatively few clients have been affected by the arrangement.

The SRA investigates the two cases and finds that the relevant facts are essentially the same. Both firms and the introducer make representations that the scheme is compliant with the SRA's regulatory arrangements.

By June 2013, the SRA has concluded its investigations into each firm and refers each matter to a decision maker with a recommendation that ABS2B Co is fined £5,000 and Lawyeronly Co is referred to the SDT.

ABS2B Co

At adjudication a finding of misconduct in respect of ABS2B Co is made. Following consideration of the appropriate criteria and guidance, ABS2B Co is fined £5,000 and ordered to pay fixed costs of £1,350.00. In light of the recommendation made at adjudication stage, ABS2B Co decided not to seek legal representation. The file is closed in July 2013.

The SRA publishes its decision and publication gathers some interest in the legal press. In light of the SRA finding and the publicity surrounding the case having an impact upon the introducer's ability to maintain its panel of solicitors, the introducer revises the problematic aspects of its scheme.

Lawyeronly Co

In July 2013, Lawyeronly Co is referred to the SDT. No findings of fact are made at this stage. The fact of the referral is published on the SRA's website.

Lawyeronly Co seeks legal advice and retain a barrister to defend the proceedings. Proceedings are issued and a hearing date is confirmed for January 2014.

At the hearing in January 2014 a finding of misconduct is made and a fine of £5,000 is imposed . Lawyeronly Co is also ordered to pay the SRA's costs of £10,000. In addition, Lawyeronly Co has incurred £10,000 of costs itself in defending the proceedings.

In March 2014, the findings of the Tribunal are published. Fortunately, a deterrent impact has already arisen from publication of the decision on the ABS2B Co case and the protection afforded to the consumer owing to the scheme in question has already been improved in the time taken to determine the matter at the Tribunal.

Conclusion

The disciplinary proceedings into ABS2B Co are resolved by the SRA's internal adjudication process 6 months prior to the SDT's decision on Lawyeronly Co. Although both resulted in the same sanction – a fine of £5000 - Lawyeronly Co was required to pay or incurred additional legal costs of £18,650.

Appendix 2

	Traditional law firm	ABS
Decision maker for fines over £2000	SDT	SRA
Time taken to conclude the matter following referral for adjudication	11.1 months – average time taken in 2010 11.7 months - average time taken in 2011 10.1 months - average time taken in 2012	Fines will be levied in-house at adjudication stage.
SRA Costs payable	£10,946.98 (was the mean average costs order made in 2010 in favour of the SRA). In 2011, the average costs order in favour of the SRA was £11,094.44 In 2012, the average was £10,589.34.	Fixed costs are currently payable: £300.00, £600.00 or £1,350.00 depending upon time spent. Potentially a further £75 per hour can be charged if time spent exceeds 16 hours[5].
Own costs payable	No data is available but it is reasonable to assume that in most cases similar costs are incurred in defending proceedings as for those in pursuing.	No data is available but it is reasonable to assume that significantly less cost would be incurred for 'in-house' matters.
Standard of proof to be applied	The SDT are of the view that the criminal standard of proof applies in most if not all cases.	Civil.
Financial penalty criteria to be applied	The SDT has issued a guidance note on sanctions in August 2012. Consideration may be given to the financial means of the paying party when assessing both the penalty and level of costs.	SRA Enforcement Strategy, SRA Disciplinary Procedure Rules 2011 (including the Financial Penalty Criteria annex) and detailed Indicative Fining guidance
Oral hearing	Yes.	Rare in the current adjudication processes and likely to be limited to cases involving particularly complicated factual disputes.
Appeal rights	To High Court	(1) To Internal Appeals panel (2) To SDT (3) To High Court
Cross examination of witnesses	Yes.	No.

[5] It should be noted that a review of the costs provisions for internal decision making as part of a wider review of the way that we calculate our fees is proposed for later in 2014/2015.