EXPLANATORY MEMORANDUM TO

THE LEGAL SERVICES ACT 2007 (THE LAW SOCIETY) (MODIFICATION OF FUNCTIONS) (AMENDMENT) ORDER 2012

2012 No. [DRAFT]

1. This explanatory memorandum has been prepared by the Ministry of Justice and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument amends the Legal Services Act 2007 (The Law Society and the Council for Licensed Conveyancers) (Modification of Functions) Order 2011 (S.I. 2011/1716) ("the 2011 Order") so as to allow the Law Society's compensation arrangements in respect of licensed bodies to continue beyond the end of 31 December 2012.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None

4. Legislative Context

4.1 The Legal Services Act 2007 ("the 2007 Act") sets out a framework for the regulation of legal services in England and Wales. The 2007 Act establishes the Legal Services Board ("the LSB") as the oversight regulator for this new framework. It requires that certain legal services ("reserved legal activities") may only be carried out by those who are authorised to do so or exempt from such authorisation. It also makes provision for the regulation, by approved regulators (such as the Law Society), of those providing such services.

4.2 Part 5 of the 2007 Act sets out arrangements under which licensing authorities (approved regulators which have been designated for this purpose in accordance with Part 1 of Schedule 10 to the 2007 Act) may license firms ("licensed bodies") which are partly or wholly owned or controlled by non-lawyers to provide legal services (or a mixture of legal and non-legal services). The Law Society was designated as a licensing authority on 23 December 2011 by the Legal Services Act 2007 (Designation as a Licensing Authority) (No.2) Order 2011 (S.I. 2011/2866).

4.3 Section 83(5)(e) of the 2007 Act provides that the licensing rules of a licensing authority must contain compensation arrangements. The Law Society has powers under section 36 and 36A of the Solicitors Act 1974 to run a compensation scheme

in relation to sole practitioner solicitors and recognised bodies (traditional solicitors' firms). In anticipation of the Law Society's designation as a licensing authority, its powers to make rules about compensation under the Solicitors Act 1974 were extended by article 5 of, and the Schedule to, the 2011 Order to allow it to make rules about compensation arrangements for licensed bodies. These powers were extended only for a transitional period, which ends on 31 December 2012 (paragraph 1 of the Schedule to the 2011 Order).

4.4 Section 69 of the 2007 Act, under which this instrument is made, provides a route through which changes may be made to the powers of certain bodies. It allows for an Order modifying or making other provisions in relation to the functions of approved regulators for certain purposes, including to allow bodies to be designated as an approved regulator in relation to particular activities, to be designated as a licensing authority, or to allow them to carry out their function as such bodies more effectively and efficiently.

4.5 There is a requirement under section 69(2) of the 2007 Act, that the Lord Chancellor may make an Order under section 69 only if the LSB has made a recommendation that he does so. Under section 70 of the 2007 Act, that recommendation may be made only with the consent of the approved regulator or other body to which it relates. Before making the recommendation, the LSB must publish the proposed recommendation and draft Order and have regard to any representations made.

5. Territorial Extent and Application

5.1 This instrument applies to England and Wales

6. European Convention on Human Rights

6.1 The Minister of State, Damian Green MP, has made the following statement regarding Human Rights:

"In my view the provisions of the Legal Services Act 2007 (The Law Society) (Modification of Functions) (Amendment) Order 2012 are compatible with the Convention rights."

7. Policy background

- ***What is being done and why***

7.1 As noted above, the provisions of the 2011 Order extending the Law Society's power to make compensation arrangements to licensed bodies were drafted so as to operate for a limited period. This Order would remove that limitation.

7.2 The sunset clause in the 2011 Order was included as the Solicitors Regulation Authority ("the SRA"), which is the regulatory arm of the Law Society, had

announced during the drafting stages of the 2011 Order that it was undertaking a review of their compensation fund. However, the SRA only began to license bodies in March 2012 and this resulted in the SRA being unable to gather the information about this developing market required for its review as quickly as it expected. Consequently, it announced that its review would be delayed until it was able to gather robust evidence on the types and scale of claims on the compensation fund that licensed bodies would be likely to cause.

7.3 Articles 4 and 5 of this Order therefore amend the 2011 Order by removing the reference to the transitional period to enable existing compensation arrangements under the 2011 Order to remain in place indefinitely. This will ensure that the Law Society, a statutory body which requires a statutory basis for its compensation fund, can continue to comply with the requirement to have licensing rules about compensation arrangements.

7.4 As discussed below, consideration was given to replacing the transitional period set out in the 2011 Order with a longer period. The SRA is committed to reviewing the current compensation arrangements over the next two years and this may lead to further legislative changes. However the timing of this cannot be predicted ahead of the review and it is therefore felt that it was more appropriate to permit the existing arrangements to continue without any time restriction.

- ***Consolidation***

7.5 There are no issues relating to consolidation.

8. Consultation outcome

8.1 In accordance with section 70 of the 2007 Act, from June to July 2012 the LSB consulted on the proposal to make this Order. There were three responses to the consultation, from: the SRA, Chartered Institute of Legal Executives Professional Standards ("the IPS") and the Law Society. The consultation and responses can be found on the LSB website at: http://www.legalservicesboard.org.uk/what_we_do/consultations/closed/index.htm .

8.2 Both the IPS and the SRA supported the proposal to remove the sunset clause from the 2011 Order. The SRA explained that it needed to delay its review until it was able to obtain a clear picture of the number and size of licensed bodies and the major risk factors which would be likely to lead to compensation claims. The SRA agreed with the drafting of the Order. The LSB supports the SRA's large scale review of its compensation arrangements and expects to see progress against this commitment.

8.3 The Law Society supported the making of a new section 69 Order but would have preferred to see the transitional compensation arrangements extended for a further

two years. This was to ensure that the issue was specifically considered in the future, rather than being left to review at the discretion of the SRA Board. The Law Society did not comment further on the drafting of the Order. The LSB appreciated the Law Society's view, but thought it was important to avoid a situation where there is insufficient information to make sensible long term provision for compensation arrangements within the revised timescale. Therefore, on balance, the LSB considered that the change should not be time bound.

8.4 Taking on board comments from the consultation, the LSB made a recommendation to the Lord Chancellor for an Order to be made.

9. Guidance

9.1 As the oversight regulator for approved regulators, the LSB has issued a statement of policy setting out the circumstances in which the LSB is likely to consider it appropriate to make a recommendation to the Lord Chancellor under section 69(3)(c) of the 2007 Act.

9.2 This statement is available online at http://www.legalservicesboard.org.uk/what_we_do/consultations/closed/pdf/Statement_of_Policy-s69_Orders.pdf

10. Impact

10.1 This statutory instrument has no impact on businesses, charities or voluntary bodies.

10.2 This statutory instrument has no impact on the public sector.

10.3 An Impact Assessment has not been prepared for this instrument, as it is not proposing a policy change or new regulation. An Impact Assessment was prepared and published with the 2011 Order. The Impact Assessment showed that the costs are difficult to quantify fully and did not expect any disproportionate impact on businesses.

11. Regulating small business

11.1 This instrument is not expected to have any disproportionate impact on small firms.

12. Monitoring & review

12.1 The SRA has indicated that it will be conducting a review of the structure of their compensation arrangements over the next two years. The LSB is expecting to see public indications of the SRA's progress against this commitment.

13. Contact

13.1 Please contact Hazra Khanom at the Ministry of Justice (tel: 0203 334 6403 or email: hazra.khanom@justice.gsi.gov.uk) about any queries regarding this instrument.