

The Office of Immigration Services Commissioner's Response to the Legal Services Board Consultation – Discussion paper on developing a regulatory regime for alternative business structures

Question 1: What are your views on whether the LSB's objective of a mid-2011 start date for ABS licensing is both desirable and achievable?

The Immigration Services Commissioner's concern is for a robust regulatory framework to be in place for ABSs before the first licenses begin to be issued.

The Commissioner understands that the earlier introduction of LDPs was intended to give the LSB and approved regulators the opportunity to learn from that experience and ensure that any necessary further safeguards were in place prior to the introduction of ABSs. She would want to be satisfied that the LSB's proposed timetable allowed sufficient time for this before ABSs were introduced.

Question 2: How do we ensure momentum is maintained across the sector towards opening the market?

No comment.

Question 3: What are your views on whether the LSB should be prepared to license ABSs directly in 2011 if necessary to ensure that consumers have access to new ways of delivering legal services?

It is sensible for the LSB to prepare for direct licensing but, as stated in our response to question 1, it is essential for adequate arrangements to be in place for the effective regulation of ABSs prior to the first licenses being issued. In particular, there must be a transparent process for the handling of complaints relating to ABSs and those employed by them. If, and only if, it has ensured that such arrangements are in place should the LSB consider direct licensing in 2011.

Question 4: How should the LSB comply with the requirement for appropriate organisational and financial separation of its licensing activities from its other activities?

The Commissioner believes this is a matter for the LSB.

Question 5: How do you expect the legal services market to respond and change as a result of opening the market to ABS?

The Commissioner agrees that the predicted developments referred to in the paper are all likely responses to the opening of the market to ABSs. She notes in particular an emerging trend toward on-line and telephone advice which may be further encouraged by the introduction of new management and ownership arrangements.

She believes that the comparison with the response of the optical market to the relaxation of restrictions on the sale of spectacles is a useful one. There are clear parallels with the legal services market, and it is likely that it will respond in a similar way to ABSs.

Accordingly, while she would not expect to see the demise of the high street firm, she would not be surprised to see the market become increasingly dominated by a small number of larger service providers, possibly operating on the “Specsavers” model, where small practices are jointly owned by the practitioners and a larger, non-practitioner company.

At the same time, she considers that many small businesses (for example, solicitors and accountants firms) may need to combine to compete with larger firms, while others will offer more specialized or niche services.

In the long term it is feasible that, while access to services could improve, a lack of competition will develop, which could be detrimental for the consumer.

Question 6: In what ways might consumers of all types – including private individuals, small businesses and large companies – benefit from new providers and ways of delivering legal services?

The Commissioner would expect to see benefits for the consumer in terms of access to firms offering several services under one roof and some price reductions as larger firms are able to pass on cost savings from economies of scale.

It is also likely that there will be greater consumer choice in the short term, though whether this will continue in the long term is less clear as mentioned in our reply to question 5. The analogy with the optical market indicates that it may not. In the long term the lack of competition could result in prices rising.

Question 7: What opportunities and challenges might arise for law firms, individual lawyers, in-house lawyers and non-lawyer employees of law firms as a result of ABS?

Non-lawyer employees may see opportunities for career development within firms rather than starting their own (e.g. an OISC regulated immigration advice

firm). However, the OISC has found that many people who presently leave law firms to start OISC firms do so because they want to practise immigration law, so the impact of ABSs on this particular sector respect may be more limited.

Question 8: What impact do you think ABS could have on the diversity of the legal profession?

No comment

Question 9: What are the educational and developmental implications of ABS and what actions need to be taken to address them?

In future, the training of lawyers will need to prepare them for working closely with different types of lawyer and non-legal professionals. It will need to develop an awareness of the regulations governing other legal and non-legal professionals and deal with the ethical and practical issues that may arise, for example, with regard to maintaining client confidentiality and dealing with conflicts of interest.

Some lawyers (e.g. barristers), because of the way they have traditionally operated, tend to have little experience of business or dealing directly with clients and may lack basic skills in relation to business and client care.

This may not be a disadvantage in some firms, where such matters can be left to others with greater experience, but, overall, such lawyers would probably benefit from some basic training in these respects to equip them for working in other types of firm and generally to prevent them relying completely on others.

Training may need to include issues such as governance, accountability and complaint handling

Question 10: Could fewer restrictions on the management, ownership and financing of legal firms change the impact upon the legal services sector of future economic downturns?

The Commissioner believes that it is too early to predict the long-term economic effects of the introduction of ABSs with any certainty. The experience of the recently introduced LDPs seem to suggest that the effect may not be that dramatic. In any case, it is not clear how reliable that experience will be as a guide to the impact of ABSs. It may be that too many start up in good times to make a quick profit and be unsustainable when times get tough. What would happen to their clients?

Question 11: What are the key risks to the regulatory objectives associated with opening the market to ABS and how are they best mitigated?

One key risk of the introduction of ABSs is that it may increase confusion over regulatory responsibility and thereby inhibit effective regulation. This is a threat to the regulatory objectives of protecting the public interest, protecting the rights of consumers, and increasing public understanding of the legal rights and duties of citizens.

One of the key challenges to the effective regulation of immigration advice has been practitioners thwarting investigations and regulatory action by moving between businesses and regulators. For example, an OISC regulated adviser whose firm is under investigation, by the OISC, may “close” their business and join a firm of solicitors, either in an advisory or administrative capacity and thus come out of OISC regulation.

There is a risk that the introduction of ABSs will muddy the regulatory waters further.

Another common issue is a lack of clarity in the drafting of regulations. For example, in a recent case, the prosecution of an unregulated, non-practising barrister who had appeared at immigration tribunals failed because the judge found that he might reasonably have believed he was entitled to do so due to an ambiguity in the Bar Code of Conduct relating to non-practising barristers.

The introduction of ABSs in which a firm may have a choice of regulator while most of the individual lawyers within it may be responsible to different lawyers and where non-lawyer managers are also permitted, will make it even more difficult to determine lines of regulatory responsibility and whether a particular practitioner is acting lawfully or not.

These issues could be mitigated by:

- (i) Regulations being made as clear as possible;
- (ii) Approved regulators working together to draft clear guidance on determining responsibility;
- (iii) Regulators working closely together on investigating misconduct across regulatory boundaries and ensuring that they have established effective arrangements for sharing information.

As discussed in the paper, the introduction of ABSs may also present a risk to the “access to justice” objective. The Commissioner is particularly concerned at the possibility ABSs resulting in the closure of small practices in more remote areas reducing the accessibility of face to face advice for asylum-seekers and other immigrants.

There also needs to be clear separation between the management policy and the duty of the individual legal advisers to clients.

Question 12: Are there particular types of business structure or model which you consider to present a particular risk to the regulatory objectives?

The Commissioner considers as high risk any ABSs combining legal services with any of the following other types of business or institution:

- Private educational institutions;
- Firms acting as agencies for the above;
- Employment agencies;
- Security firms;
- Private nursing agencies;
- Catering firms, hotels or restaurants;
- Firms employing seasonal workers;
- Small charities (i.e. those with a turnover of less than 10k p.a.

This is because of the risk of such businesses being used for the facilitation of immigrants. These businesses will offer legal advice or have links to someone that does. If such a firm was involved in an ABS firm, there would be a risk that the lawyers would also be involved.

The Commissioner would also consider any ABSs in which non-lawyer managers had a controlling interest as being high risk because of the increased risk of commercial interests prevailing over professional principles.

Question 13: What conflicts of interest do you think might arise in relation to ABS and how should they be managed?

The duty of a solicitor to give his client objective advice on the merits of their case may conflict with the commercial imperatives of the firm as a whole. For example, a client may seek immigration advice from a firm that specializes in providing a package of services to overseas students or business applicants and the solicitor may consider that an application on such a basis is not the most appropriate one for the client. The solicitor may, however be under pressure to “sell” the client a package. This would be in conflict with their responsibility to ensure they act in the client’s best interests.

The introduction of a Head of Legal Practice, (HOLP) in each firm with responsibility for ensuring that its lawyers all comply with their professional obligations may help to manage such conflicts, but if non-lawyers have a controlling interest in the firm, the HoLP’s independence may be compromised. Even if their interest falls short of this level, the HoLP may be subjected to considerable pressure.

This may be a case for limiting the interest of non-lawyers. At the very least, regulators need to make clear to firms from the outset which interests take precedence and have in place a robust auditing system to ensure compliance. There may also be a need to have strict penalties for non-compliance, as otherwise firms may see the threat of regulatory action as an acceptable risk.

Question 14 - How should licensing authorities approach entity-based regulation and what are the main differences from the traditional focus on regulating individuals?

The OISC's regulation has been primarily "firm-based" since its inception. However, this is just a matter of emphasis. The OISC regulates individuals within firms too, but does not grant individuals a licence that can take from firm to firm.

The Commissioner considers that, in order to be effective, regulation has to embrace both firms and individuals. Indeed, a stress on firms rather than individuals can mean that individuals often slip through the net, as explained in our response to question 11.

It is also very useful for regulators to have clear guidance to help them identify when they are dealing with a firm that has changed over time, and when they are dealing with a completely new entity. Similarly, when there is one entity to be regulated and when there may be several.

Question 15: Do you agree with our view that licensing authorities should take a risk-based approach to regulation of ABS, and if so, how might this work in practice?

The OISC takes a risk based approach to its regulation in accordance with Better Regulation principles.

The Commissioner agrees that there is a need for regulators to develop a greater understanding of corporate structures and how businesses are run. They also need new technology to ensure that they are able to adequately collect and analyse data.

The Commissioner is not sure that it is appropriate to use as the starting-point for the risk-based approach to the regulation of ABSs the framework, which the Act sets out for the lighter regulation of special bodies.

"Special bodies" are by definition the exception to the rule, and it does not seem sensible to use a framework intended for them as the starting-point for establishing a style of regulation for regular ABSs.

The Commissioner also suggests that the initial assessment of the risks of a particular firm at the point of licensing will need to be regularly reviewed in the

light of complaints and intelligence received and, where appropriate, audit findings.

Question 16: What is your preferred balance in regulating ABS between a focus on high-level principles and outcomes and a more prescriptive approach?

There is a risk with principle-based regulation that it may not be sufficiently clear to regulated persons or firms when they are in breach of professional regulations and therefore they may prove difficult to enforce. The OISC has expressed its concern to the SRA about the latter's regulations regarding the supervision of non-solicitors for precisely this reason.

Issuing detailed guidance may help, though there may still be a problem as such guidance does not of itself have any regulatory force. The OISC's own regulations are a mixture of the specific and general complimented by guidance.

For example, the OISC's regulations relating to the maintenance of client records and professional indemnity insurance are quite prescriptive, while the other of its Codes cover more general issues such as acting in the client's best interests, acting in accordance with the law or abusing immigration or asylum procedures.

Question 17: What are the advantages and disadvantages of a requirement on ABS to have a majority of lawyer managers?

While requiring ABSs to have a majority of lawyer managers may restrict possible business structures and limit the opening up of the market; this may be necessary from a regulatory point of view. As individual regulators are likely to be best placed to make this judgment, it is important that they have the freedom to do so.

A clear disadvantage of permitting a legal business to be controlled by non-lawyer managers is that they may exert pressure on the firm's lawyers to set aside ethical and professional considerations in favour of commercial ones.

Question 18: What are your views about how licensing authorities should determine whether a person is a "fit and proper person" to carry out their duties as a HoLP or a HoFA?

The OISC agrees with the SRA that non-lawyer managers of ABSs should be subject to the same general tests in terms of character and suitability as lawyers. We also agree that there can be some "passporting" of non-lawyers who have been through "fit and proper" tests laid down by other regulators

and professional bodies, provided that the tests they have passed are of a similar or greater standard than that for lawyers.

Timing may be important. If CRB checks are undertaken every 3 years, a person with a new conviction could 'jump' to a non-lawyer post with a valid CRB prior to it all being recorded.

If non-lawyer managers are allowed to have a controlling interest in the firm, or to be HoLPs or HoFAs, we would also suggest that the individuals be made to undertake some training in the ethics of the profession of the organisation's regulator and the relevant regulations to ensure that they are familiar with them.

We further suggest that they should be made to commit to taking a share of the responsibility for ensuring that the organisation abides by the relevant regulations, and that, consequently, they should also share accountability for serious breaches that could result in them facing being dis-barred.

There may need to be a central database accessible to all regulators involved in the regulation of ABSs.

Question 19: What is the right balance between rejecting "higher-risk" licensing applications and developing systems to monitor compliance by higher-risk licensed bodies?

The OISC operates on the basis that it will only register a firm if it considers it to be fit and competent. This is decided on the basis of their application and their supporting documentation and of any background checks. If there is any doubt about this, a pre-regulation audit is carried out. While a firm may be admitted to the OISC, the range of services permitted or the level at which it may operate can also be limited.

The fact that an organisation is "high-risk" will not in itself prevent the firm being OISC regulated, though it may cause the admission to be conditional. For example, the period of regulation may be limited and an early audit may be scheduled. All high-risk organisations are, in any case, scheduled for audit within the first year of operation.

The Commissioner believes that a similar approach may be appropriate for ABS firms. She shares Lord Hunt's concerns regarding the robustness of internal governance arrangements, and notes that these can only properly be assessed when the firm is up and running as what happens in practice may be different to what is set out on paper.

Question 20: How should regulators ensure a level playing-field between regulated legal practices and licensed bodies?

The Commissioner agrees that different approaches should be based, as far as possible, on evidence about the risks associated with different types of firms and the practicalities of auditing them, rather than basing these on

assumptions about ABSs being inherently risky. She also agrees that some ABS firms may be of a lower risk than other types of firms.

At the same time, the Commissioner recognises that evidence will not be available in many cases because the structures of the firms are new. In such cases, she feels that regulators must be free to make reasonable inferences about the risks posed by those structures.

Question 21: How should licensing authorities approach the access to justice condition, and do you agree that it is unlikely that many licences should be rejected on the basis of the condition?

While the Commissioner agrees that it may be difficult to determine the likely impact of a single licensed body application on access to justice, she considers that it should be possible to make a risk assessment in consultation with key stakeholders.

She further believes that there should be some opportunity for interested parties to make their views known and have them considered by the licensing authority, as the case, for example, with planning applications.

While the Commissioner would not wish to see any unnecessary restrictions on market entry, she believes that reducing access to justice is such a serious matter that there should be a presumption in favour of refusing applications where it is deemed, after a full and balanced consideration of all the relevant factors, that there is a real risk of such an outcome.

The Commissioner is concerned that, if the LSB or licensing authorities proceed on the assumption that there will only be a minority of cases, there is a risk that this may become a self-fulfilling prophecy.

The Commissioner agrees that the LSB and licensing authorities need to monitor the impact of opening up the market to ABSs on access to justice, and suggests that the results of such monitoring activity should, in turn, inform future licensing decisions. This process needs to start with the monitoring of the impact of LDPs.

Question 22: How should licensing authorities give effect to indemnification and compensation arrangements for ABS?

The Commissioner considers that the key consideration is that the arrangements in place ensure that clients are protected. There may be a number of different ways of doing this, with some more appropriate to a particular regulatory body than others. The Commissioner feels that bodies should be free to adopt the arrangements best suited to them, provided they give adequate protection to the consumer.

Regarding the assigned risks pool, the Commissioner recognises that ABS firms may be less likely to have recourse to it, but she does not believe it is sensible to proceed on the basis that it will not be relevant to them at all. The more prudent course would be to wait and see. As ever, the protection of the consumer is paramount.

The Commissioner agrees that it is not appropriate or practicable for licensing authorities to attempt to regulate the capital adequacy of new entrants, though recourse to arrangements such as the Assigned Risk Pool (ARP) should continue to be limited. Firms that cannot obtain their own cover cannot be permitted to continue indefinitely, effectively underwritten by the licensing authority.

Regarding compensation, the Commissioner agrees that the key principles for ABSs should be that the consumer receives compensation as soon as possible after the collapse of an ABS and that there is minimal disruption to the processing of the consumer's legal matter. She is particularly concerned to ensure that client records are properly looked after.

Question 23: How should complaints-handling in relation to legal services provided by ABS be regulated?

The Commissioner does not consider that new complaints-handling systems will be needed for complaints about ABSs. However, regulators will need to ensure that existing systems are sufficiently flexible to cope with investigations that may cut across several regulatory regimes and have both firms and individuals as their subject. Regulators will need to look at protecting evidence, acting promptly to pass cases on and supporting each other.

The Commissioner is cautious about focusing on the "rapid resolution of the consumer grievance" to the detriment of regulatory issues. While the former is clearly of key importance, she considers that a suitable balance must be struck between consumer satisfaction and regulatory action. It is important that any underlying regulatory issues are properly addressed.

The Commissioner is also sceptical about the quality of the internal complaint systems likely to be implemented by ABS firms. While a number may have

sophisticated systems, others may not, and still more may have good systems on paper, but fail to implement them in practice.

Question 24: How should licensing authorities approach the “fit to own” test and how critical is it in mitigating the risk to the regulatory objective of promoting lawyers’ adherence to their professional principles?

The “fit to own” test is a basic precaution, which is necessary from the point of view of public confidence in ABS firms. However, the test is not sufficient to ensure that the risk of lawyers being pressed by unscrupulous non-lawyer

owners into failing to adhere to their professional principles is reduced to an acceptable level.

One possible additional safeguard would be to prevent non-lawyers from obtaining a controlling interest in firms. While the Commissioner appreciates that the LSB does not wish any unnecessary restrictions placed on non-lawyer ownership, she considers that allowing non-lawyers a controlling interest may be incompatible with safeguarding the integrity and independence of lawyers as explained in our response to earlier questions.

While requiring the constitution of an ABS firm to set out a hierarchy of duties to prevent potential conflicts of interest may be a useful measure to some extent, it is not clear how it is possible to ensure that the constitution will be enforced if the firm is controlled by non-lawyers whose interests may conflict with the duties of the firm’s lawyers.

The Commissioner agrees with the remarks at paragraph 7.38 of the consultation paper that there is also a potential problem with the possible installation of individuals with clean records as “front” people for criminal interests or with identifying ownership of firms, which have received investment from abroad.

It is difficult to see what safeguards can be put in place to prevent this from happening, but it clearly something that regulators will need to be aware of and develop mechanisms for dealing with. Effective intelligence systems and legal gateways permitting the transfer of such information are crucial here, as well as links to other enforcement bodies such as the police, HRMC, and FSA.

Question 25: Are there any particular risks to the regulatory objectives that arise from could arise from ABS offering non-reserved legal services?

See our response to question 11.

There may be an issue as to whom handles complaints about non reserve matters.

Question 26: What are the risks to the consumer associated with the delivery of legal services by special bodies and which more general risks are less relevant to these bodies?

The OISC regulates a wide range of not-for-profit organisations providing immigration advice and (in some cases) other legal services. These range from national organisations such as IAS, Refugee Action to small community groups consisting of one or two advisers. The OISC also regulates many law centres and Citizens Advice Bureaux.

The Commissioner agrees that the risk factors identified in the consultation paper apply to these bodies, and that the OISC has considerable experience of the issues highlighted. She believes that at least three important further factors need to be taken into account.

First, that the individual users of these services, tend to be among the more vulnerable members of society, asylum-seekers, people on a low incomes or people whose first language is not English and who may be unfamiliar with the UK legal system.

Second, as these bodies may be community based and will certainly present themselves as focused on helping people, they generate levels of trust among their clients which are not so often found in the commercial sector and which can easily be exploited by unscrupulous individuals.

Third, as the regulation of such bodies tends generally to be relatively light, unscrupulous individuals can abuse the system by setting themselves up as not-for-profit organisations, but actually operate for profit, either directly or by acting as a conduit for a third party.

While the Commissioner agrees that there is generally less risk of these bodies exploiting clients financially, this does happen, and, when it does, the impact can be more severe because of the vulnerability of the individuals concerned.

Question 27: Is it in the consumer interest to require special bodies to seek a licence, and if so, what broad approach should licensing authorities take to their regulation?

The Commissioner considers on balance that it is in the consumer interest for such bodies to seek a licence.

Her experience of regulating not-for-profit organisations has been that they can be as problematic as for profit organisations. From the outset, the OISC has implemented an application process for not for profit organisations which is broadly similar to that applied to the for profit organisations.

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Although not-for-profit organisations are not currently required to apply annually for continued regulation, the risk assessment system the OISC employs in determining the frequency of audits makes no distinction between the two organisation types. Rather, it focuses on other factors such as the level of advice given and the organisation's complaints history using a risk based matrix to determine the level of risk any organisation poses. This is because the Commissioner feels that the quality of advice and service should be consistent across both sectors.

The Commissioner agrees with the approach taken to "group licensing" in paragraph 8.6. While this may be relevant in some cases, careful

consideration needs to be given to the type of cases treated in this way and possible exceptions to the rule. For example, the Commissioner has granted a "block exemption" to Citizens Advice Bureaux to operate at OISC level 1. But CAB offices which want to operate at a high level have to apply separately to do so in the same way as other organisations and are subject to the OISC audit process applied to organisations operating at the higher levels.

Question 28: Are there any other issues that you would like to raise in respect of ABS that has not been covered by previous questions?

The Commissioner wishes to emphasise the importance of monitoring the impact of LDPs and learning from that experience prior to implementing the full ABS regime. Also, the need for close collaboration between regulators.

Suzanne McCarthy
Immigration Services Commissioner

10 August 2009