

# LAW SOCIETY SUBMISSION

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## **Section 118 Legal Services Regulation Act 2015 – Legal Partnerships**

LEGAL SERVICES REGULATORY AUTHORITY

20 July 2017

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#### ABOUT THE LAW SOCIETY OF IRELAND

The Law Society of Ireland is the educational, representative and regulatory body of the solicitors' profession in Ireland.

The Law Society exercises statutory functions under the Solicitors Acts 1954 to 2011 in relation to the education, admission, enrolment, discipline and regulation of the solicitors' profession. It is the professional body for its solicitor members, to whom it also provides services and support.

The headquarters of the organisation are in Blackhall Place, Dublin 7.

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## 1. Introduction

- 1.1. The purpose of this second submission from the Law Society of Ireland (“the Society”) is to issue a response to the report (“the report”) from the Legal Services Regulatory Authority (“the Authority”) to the Minister for Justice dated 31 March 2017. The report was written having regard to the submissions made to the Authority in relation to the regulation, monitoring and operation of legal partnerships as part of their initial public consultation in accordance with section 118 of the Legal Services Regulation Act 2015 (“the Act”). The report was subsequently laid before the Houses of the Oireachtas by the Minister for Justice on 28 April 2017.
- 1.2. As the Society is the representative and regulatory body for solicitors in Ireland, the Society’s comments in this submission will be limited to solicitor-barrister legal partnerships. As such, all references to “legal partnerships” in this submission should be read as a reference only to solicitor-barrister legal partnerships, not barrister-barrister legal partnerships.
- 1.3. The Society limits this second submission to addressing certain matters that arise in the report from the Authority which have led to some concerns regarding the possible introduction of ‘light touch’ regulation for solicitor-barrister legal partnerships.

## 2. Executive summary

- 2.1. The following submission sets out the Society's views in relation to the report on legal partnerships submitted by the Authority to the Minister for Justice dated 31 March 2017.
- 2.2. This submission proposes to address the issue of the regulation of legal partnerships and the possibility of differing standards of regulation being applied to legal partnerships as suggested in the initial report from the Authority.
- 2.3. While the Society recognises that legal partnerships will be commenced in Ireland under the Act, the Authority should be aware of the potential risks in implementing the establishment of these structures without ensuring they are regulated to the same high standard as currently applies to solicitor firms.
- 2.4. Chapter 3 of this submission considers the Authority's report and the Society's concerns about the suggestion that lower regulatory standards might be applied to legal partnerships. The Society notes the importance of changes in the provision of legal services as provided for in the Act but expresses its concern about the standard of regulation of the delivery of those services through legal partnerships.
- 2.5. Chapter 4 sets out the regulatory powers of the Authority and the Society in relation to solicitors, different levels of regulation of solicitors depending on how they practise, and the need for harmonisation of regulatory standards.
- 2.6. Chapter 5 considers possible risks to the solicitors' profession if lower standards of regulation are introduced in relation to legal partnerships, including the creation of a two-tier profession, risks to the Society's Compensation Fund, education and training, and matters relating to professional indemnity insurance.
- 2.7. Chapter 6 considers possible consequential public protection risks associated with the introduction of lower regulatory standards for legal partnerships, including the exploitation of legal partnership structures by the minority of solicitors who might take advantage of this weakness, two-tier protection for clients, and effects on client fees.
- 2.8. Chapter 7 considers the risks associated with 'light touch' regulation, the reputation of legal partnerships, and the Authority's required objectives under the Act.
- 2.9. It is the recommendation of the Society that solicitors in legal partnerships be subjected to the same regulatory standards as solicitors practising outside of legal partnerships in the interests of protection of the public and the profession, the reputation of the regulatory system, protection of the Society's Compensation Fund, and the confidence of the public in legal partnerships as a structure.

### 3. The Authority's report

- 3.1 The initial report from the Authority to the Minister for Justice dated 31 March 2017 took into account the views of eight different parties through their respective submissions. The report has also considered comparative aspects of the regulation of solicitors and barristers in England and Wales.
- 3.2 The Society acknowledges that the Authority is seeking to augment the provision of legal services through the introduction of different legal structures including legal partnerships. The Society notes that the Authority is of the view that these structures should not be commenced until the necessary consultations have been conducted and an appropriate framework is in place.
- 3.3 Nevertheless, the Society wishes to express its apprehension with regard to some of the matters expressed in the Authority's report.
- 3.4 Paragraph 21 of the report states as follows:

*"If it is decided to merely extend the concept of solicitor regulation to legal partnerships, it may not succeed in widening the variety of offerings of legal services in Ireland. If, on the other hand, the introduction of legal partnerships is used as a mechanism for introducing different types of regulation for differing categories of lawyers working collectively under different practice requirements, then these legal partnerships may add value to the market. In other words, simply regulating legal partnerships as regulated solicitor-owned law firms, may add nothing to the market. Creating partnerships which have different scopes of practice authorisations, may facilitate the regulation of these entities in new ways."*

- 3.5 The Society is concerned that this may be interpreted that the Authority is considering applying lower regulatory standards to legal partnerships than are currently applied to solicitor firms.
- 3.6 The Society recognises the importance of innovation in the provision of legal services, but this should not come at the possible expense of public protection. While novel methods of regulation are worth considering, lower standards of regulation should not be accepted.
- 3.7 The Society sees the application of lower regulatory standards to legal partnerships as unnecessary, inappropriate and with the potential to damage public confidence in the legal professions, as well as damaging the professions themselves. Regulatory standards should be universal across the solicitors' profession and should not be conditional on the basis of the entity through which a legal practitioner provides legal services unless such differences in standards are reasonable, proportionate and do not constitute an increased risk to public protection.
- 3.8 It is unclear from the report what lower standards are being referred to, how these standards would be applied, and whether such standards would only be applied to barrister-barrister legal partnerships or to all types of legal partnerships. The centrepiece of the Authority's powers, once enacted, relate to processing complaints against solicitors and barristers. The

view could be taken from the report that the threshold for legitimate complaints against legal practitioners in a legal partnership could therefore be higher than complaints against other legal practitioners.

## 4. Regulatory powers

### **Society's regulatory powers**

- 4.1 Notwithstanding the powers of the Authority when additional parts of the Act are commenced, the Society will retain a number of key regulatory powers in relation to solicitors including issuing practising certificates, professional indemnity insurance, financial regulation, anti-money laundering obligations and powers of inspection. The Society also maintains and controls the statutory Compensation Fund which administers grants to clients who suffer financial loss through the dishonest actions of solicitors in the provision of legal services.
- 4.2 In the interests of protecting the Society's Compensation Fund and the public, the Society will continue to inspect practices, require solicitors to submit annual accountants' reports and a closing accountants' report and will prosecute breaches of the Solicitors Accounts Regulations 2014 (S.I. No. 516 of 2014).
- 4.3 The Society has developed a risk-based system for choosing firms for financial investigations rather than using a purely cyclical basis. This means that firms are chosen for inspection based upon a number of matters including complaints made against solicitors in any given firm. Any reduced standard of regulation that would not alert the Society to potential risks could distort the Society's risk assessment system, and constitute a risk to the Society's Compensation Fund.

### **Current differing levels of regulation**

- 4.4 There are differing levels of regulation that currently apply to different subsets of solicitors depending on the nature of their practice. These differences are reasonable and proportionate as they do not put the public or the reputation of the profession at increased risk. Such different levels apply to solicitors firms that do not hold client monies, in-house solicitors in relation to professional indemnity insurance, and non-practising solicitors in relation to requirement to hold a practising certificate and insurance.
- 4.5 The Society allows a different level of financial regulation for firms that do not receive, hold or control client monies. The compliance partner or sole practitioner of a firm may make a statutory declaration to the Society confirming that the firm does not receive, hold, control or pay client monies and this would mean that a firm does not have to provide an annual accounting report to the Society nor are they normally subject to inspections from the Society's investigating accountants. However, the Society reserves the right to inspect such firms and does so from time to time. This declaration is made to the Society on an annual basis and it is professional misconduct to make a false declaration to the Society representing that a firm does not receive, hold, control or pay client monies.
- 4.6 As at 19 June 2017, there are 62 firms out of 2,302 firms in Ireland that have filed statutory declarations that they do not hold client monies and are therefore not subject to further



regulatory requirements pertaining to the handling of client monies unless the Society has reason to inquire into those declarations.

- 4.7 In-house solicitors are not required to hold professional indemnity insurance as they only provide legal services to their employer. The liability of in-house solicitors is covered by their employment contract and principles of vicarious liability.
- 4.8 Non-practising solicitors (that is solicitors who are not providing legal services of any kind or holding themselves out as a solicitor entitled to practise) are not required to hold a practising certificate nor are they required to hold professional indemnity insurance. They are also not subject to the regulatory requirements concerning the holding of client monies.
- 4.9 In these scenarios, the lower level of regulatory obligations placed on such solicitors is directly proportionate to the reduced risk that such solicitors pose to the public and the Society's Compensation Fund. The Society would not have an issue with similar concessions being granted to legal partnerships, such as in relation to legal partnerships that do not hold client monies.
- 4.10 However, the Society's concern is that lower regulatory requirements for legal partnerships will be put in place merely by virtue of the fact that the legal service is being provided by a legal partnership, rather than by virtue of the fact that the legal partnership poses a lower regulatory risk. It would be difficult to justify why solicitors providing the same legal service through different structures should be subject to different regulatory standards.

### **The Authority's regulatory powers**

- 4.11 The Authority will have regulatory powers over solicitors in legal partnerships and other practice entities in terms of dealing with complaints from members of the public under Part 6 of the Act, once commenced. The Authority will also have the power to make regulations in terms of the operation and management of legal partnerships under section 116 of the Act, once commenced. The Authority will also have competence to make advertising regulations under section 218 of the Act for *inter alia* legal partnerships.
- 4.12 The Authority may make regulations under section 116 (3) providing for:
- (a) *the standards to be observed in the provision by the practice of legal services to clients, including standards relating to:*
    - (i) *the professional and ethical conduct of persons providing legal services to clients;*
    - (ii) *the obligation of such persons to keep the affairs of clients confidential;*
    - (iii) *the provision of information to a client in relation to the duties owed by the practice to him or her,*
  - (b) *the rights, duties and responsibilities of a practice in respect of moneys received from clients,*

*(c) the management and control of the practice so as to ensure that:*

- (i) the standards referred to in paragraph (a) are at all times observed;*
- (ii) it has in place appropriate systems of control, including systems for risk management and financial control;*
- (iii) where, in the provision by it of services, a conflict of interest or potential conflict of interest arises, this is dealt with adequately and in accordance with any relevant code of conduct or professional codes;*
- (iv) its obligations under this Act and regulations made under it are complied with,*

*(d) the maintenance by the practice of records,*

*(e) the regulation of the names that may be used by a practice,*

*(f) the regulation of the advertising by the practice of its services.*

4.13 The Authority would not have the power to set regulatory standards for the following matters in relation to solicitors:

- a) professional indemnity insurance;
- b) the Society's Compensation Fund;
- c) Solicitors Accounts Regulations;
- d) anti-money laundering matters;
- e) issuing of solicitors' practising certificates.

4.14 Solicitors in legal partnerships should be subject to the same rules and requirements as solicitors in other forms of practice in relation to these matters, and regulatory standards between legal partnerships and solicitor firms should be harmonised.

## 5. Risks to the solicitors' profession

- 5.1 There are inherent risks to the solicitors' profession if there is any consideration given to operating a lower regulatory standard for legal partnerships.

### **Two-tier solicitors' profession**

- 5.2 The regulatory standards that currently apply to solicitors have been established over a number of decades through experience and are maintained to protect the public, the Compensation Fund and the reputation of the profession. Regulation does not remain static and must be kept under review to adapt to changes in the market.
- 5.3 Any lowering of those regulatory standards for legal partnerships would grant an immediate and unfair competitive advantage to a defined class of solicitors which would bring about an imbalance by creating a two-tier form of solicitors' profession between those solicitors in legal partnerships and those practising outside legal partnerships.
- 5.4 The application of any lower regulatory standards to legal partnerships would reduce protections to clients and would ultimately be a risk to the public. It may lead to a situation where solicitor firms could employ a single barrister in order to benefit from the lower regulatory standards applied to legal partnerships, to the detriment of the clients.
- 5.5 This could also lead to confusion for members of the public as there would be differing regulatory standards applied to different classes of solicitors. It would be unreasonable for a client accessing a legal service through a solicitors' firm to be offered greater protections than a client accessing the same service through a legal partnership. It would also be unjust to hold certain solicitors to a higher standard by virtue of their practice structure.

### **Parallel regulatory structures**

- 5.6 Any consideration of operating a parallel regulatory scheme for legal partnerships would be an expensive and unnecessary exercise. The costs of establishing and maintaining a regulatory scheme for legal practitioners in legal partnerships would be disproportionate to the aims to be achieved and difficult to justify.

### **Regulatory standards**

- 5.7 There is also a concern that solicitor partners in legal partnerships would be held to a higher regulatory standard than barrister partners. It would be unfair and inappropriate to create a situation where the regulatory burden for legal partnerships rests disproportionately on the shoulders of the solicitor partners. It is the view of the Society that it would be more appropriate that solicitors and barrister partners in legal partnerships be held to the same regulatory standards, and share regulatory responsibilities equally.

## **Education and training standards**

- 5.8 Solicitors are currently trained to a required standard before they can be admitted to the Roll of Solicitors. This requires a trainee solicitor to successfully complete the education and in-office training requirements of the Society. If a trainee solicitor were to complete their in-office training in a legal partnership, they could be at a disadvantage in terms of their understanding of regulatory requirements. The trainee solicitor would be trained to the lower regulatory standard which would not be of a sufficient standard to commence practice in a solicitors' firm.
- 5.9 A newly qualified solicitor who has completed their in-office training in a legal partnership could jeopardise their own career by commencing practice in a solicitors' firm as they would then be held to the higher standard of regulation which they would be unprepared for.

## **Society's Compensation Fund**

- 5.10 Legal partnerships that include practising solicitors will be entitled to hold client monies and as such they will constitute a potential risk to the Society's Compensation Fund. The Society has already made its representations regarding the possible risks to the Compensation Fund in its first submission.
- 5.11 The application of lower standards of regulation to legal partnerships could attract a minority of non-compliant solicitors that seek to exploit those lower standards. This could lead to the scenario whereby dishonest solicitors in legal partnerships could cause an increase in the number of claims made on the Society's Compensation Fund.
- 5.12 If there is a lower regulatory standard for complaints against solicitors within a legal partnership than solicitors in other forms of practice, this could lead to an imbalance in the Society's risk-based assessment system for financial investigations, thereby constituting a risk to the Society's Compensation Fund.
- 5.13 This could put the Society in the invidious position of being liable for an increase in claims made on the Compensation Fund by clients of those solicitors who seek to take advantage of lower regulatory standards in legal partnerships. As the Society would have no power to regulate those standards, this could affect the ability of the Society to secure insurance for the Society's Compensation Fund.
- 5.14 Any increase in grants paid out from the Society's Compensation Fund would likely be reflected in higher practising certificate fees for solicitors. It would be unreasonable for the largely compliant members of the solicitors' profession to suffer due to lower regulatory standards put in place on legal partnerships.

## **Professional indemnity insurance**

- 5.15 Legal partnerships that include solicitors will be subject to the relevant professional indemnity insurance regulations made by the Society.

- 5.16 If there are to be any lower regulatory standards applied to legal partnerships, this is likely to impact the risk profile of these structures in the view of insurers. Any perceived increase in risk by insurers is likely to manifest itself in higher professional indemnity insurance premiums charged to legal partnerships.
- 5.17 Given that professional indemnity insurance is a free market in Ireland, some insurers may not wish to assume the risk of underwriting legal partnerships or only do so at an inflated price. This could have the effect of pushing up premium levels charged by those insurers who would underwrite legal partnerships.

## 6. Public protection issues

- 6.1 Any deviation in regulatory standards will impact members of the public in their dealings with legal partnerships. The public expects and deserves high standards from legal practitioners and those standards should be applied consistently.
- 6.2 A reduction in regulatory standards for legal partnerships could have the unintended consequence of attracting solicitors who would use such structures in order to circumvent more rigorous regulatory standards which would apply to other classes of solicitors.
- 6.3 This could in turn lead to a situation whereby a solicitor could enter into a legal partnership with a barrister in a nominal capacity in order to gain the benefit of lower regulatory standards. This could ultimately damage protection of the public, the administration of justice, and the reputation of the profession.

### **Fees**

- 6.4 Any dilution of regulatory standards is unlikely to reduce fees charged by legal partnerships. There is no empirical evidence available to suggest that lower standards of regulation will offer any financial benefits for clients.
- 6.5 Further to this, as noted in paragraph 5.17, any higher premiums charged for professional indemnity insurance to legal partnerships would most likely be reflected in the fees charged by the partnership to their clients.
- 6.6 As such, any reduction in regulatory standards at the expense of public protection would likely not result in any substantive reduction in fee levels.

### **Two-tier protection for clients**

- 6.7 The Society is apprehensive that the purpose of lowering regulatory standards for legal partnerships would be to create a cheaper form of legal provider by reducing client protections and safeguards. Protection of the public is a fundamental tenet of the provision of legal services. The level of protection a client receives from their professional legal provider should not be dependent on the level of fees that the client can afford. The Society is of the opinion that the public has high expectations with regard to standards applied to legal practitioners and that lower regulatory standards can only damage public confidence in the legal system.

## 7. Risks of 'light touch' regulatory framework

- 7.1 A regulatory framework should be consistent with and responsive to the evolution of the profession or industry it seeks to regulate. The framework should be monitored, amended and updated as necessary in order to adjust to changes in the wider environment. Setting poor foundations to a regulatory framework at the outset will almost inevitably lead to collapse and rebuilding can be a costly exercise.
- 7.2 A regulatory system must ensure that it maintains the confidence of the public. Reconstruction of public confidence after the failure of regulatory mechanisms can take a great deal of time.
- 7.3 There have been numerous examples in both Ireland and internationally whereby regulatory malfunction has failed the public interest, in particular as a result of 'light touch' regulation. These include the failure to adequately regulate the insurance industry and failure to adequately regulate banking activities. The fallout from the failure of regulation in these two areas alone has caused widespread financial difficulties and damage to public confidence. Further to this, it has damaged the public perception of the regulators themselves.
- 7.4 While no regulatory framework can possibly envisage all risks, the establishment and maintenance of high standards of regulation should be an aspiration of the Authority in order to secure public confidence in its regulatory role.
- 7.5 The introduction of legal partnerships could be seen unfavourably in the eyes of the public, the professions and the courts if solicitors within legal partnerships were not held to the same high regulatory standards as those solicitors who practise outside such structures. It may result in legal partnerships gaining a reputation as poor quality, under-regulated and second class providers of legal services.
- 7.6 The Act requires the Authority to have regard to the objectives specified under section 13 (4) of the Act. Those objectives are as follows:
- a) *Protecting and promoting the public interest,*
  - b) *Supporting the proper and effective administration of justice,*
  - c) *Protecting and promoting the interests of consumers relating to the provision of legal services,*
  - d) *Promoting competition in the provision of legal services in the State,*
  - e) *Encouraging an independent, strong and effective legal profession, and*
  - f) *Promoting and maintaining the professional principles specified in subsection (5).*

It seems unlikely that lowering regulatory standards would assist the Authority in promoting and vindicating these objectives.

## **Recommendation of the Society**

- 7.6 As such, it is the recommendation of the Society that regulatory standards should be applicable to all solicitors on an equal and unambiguous basis. The application of lower regulatory standards by virtue of the structure within which a solicitor practises would likely reduce public protection, damage the reputation of the solicitors' profession, increase risks for the Society's Compensation Fund, and damage the public perception of legal partnerships as a legal service provider.
- 7.7 Proportionate and reasonable standards for legal partnerships, similar to those in place for solicitors, would be appropriate, such as alternative financial regulatory obligations where legal partnerships do not hold client monies.