

**Written Evidence of the Office of Fair Trading ('OFT') to the Justice Committee of the Scottish Parliament on the Legal Services (Scotland) Bill**

**1 December 2009**

**1 INTRODUCTION**

1 We welcome the Scottish Government's Legal Services (Scotland) Bill ('the Bill') and the opportunity to comment thereon. We strongly support the introduction of Alternative Business Structures ('ABS'.) We believe it will allow those legal service providers who wish to adapt their businesses to the most efficient model that meets their customers' needs. This will consequently allow the market to work better for consumers.

2 In our view, ABS are likely to produce consumer benefits, such as more choice, higher quality services and lower costs. Their introduction in Scotland is likely to contribute positively to competition in the supply of legal services throughout Scotland and thereby benefit the Scottish economy and the public as a whole.

3 We welcome the removal of restrictions on solicitors entering into business relationships with non-solicitors, allowing investment by non-solicitors and external ownership.

4 Our key recommendations set out in our response to a consultation paper<sup>1</sup> produced by the Scottish Government ('the SG') on the regulation of legal services in Scotland ('Consultation Response')<sup>2</sup> were that:

- The Bill and its regulatory objectives should apply not only to ABS but to traditional forms of practice and to all legal professionals including advocates.
- Both the Law Society of Scotland and the Faculty of Advocates should separate their regulatory functions from their representational functions with a lay majority voting on regulatory and non-membership issues.
- Scottish Ministers should exercise their oversight function with the assistance of a consumer advisory panel.

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<sup>1</sup> Wider choice and better protection: A consultation paper on the regulation of legal services in Scotland, Scottish Government, 7 January 2009, available at [www.scotland.gov.uk/Resource/Doc/1097/0076097.pdf](http://www.scotland.gov.uk/Resource/Doc/1097/0076097.pdf)

<sup>2</sup> Wider choice and better protection: A consultation paper on the regulation of legal services in Scotland - Response from the Office of Fair Trading, OFT 1076, April 2009, available at [www.oft.gov.uk/shared\\_oftr/reports/oft\\_response\\_to\\_consultations/oft1076.pdf](http://www.oft.gov.uk/shared_oftr/reports/oft_response_to_consultations/oft1076.pdf)

- The Faculty of Advocates blanket restrictions on members forming partnerships and joining ABS should be lifted.
- The SG should consider a review of the QC appointments process.

5 We also set out the competition scrutiny role we envisage will be the most effective and most valuable<sup>3</sup> to the Scottish Ministers ('SM') when determining competition issues and meeting the competition regulatory objectives in the Bill. This should ensure a more competitive legal services market in Scotland providing lower fees and increased choice for consumers, providing benefits to the Scottish economy as a whole and also serve the wider public interest.

## 2 THE COMPETITION SCRUTINY ROLE OF THE OFT

6 The Bill<sup>4</sup> places a responsibility on SM to provide external oversight over professional or other bodies known as Approved Regulators which are seeking to license ABS. In England and Wales this oversight role is undertaken by an independent body, the Legal Services Board ('the LSB'). The SG does not favour the creation of such a body.

7 The establishment of an oversight regulator has the effect of substantially removing professional rules within its remit from the scope of both UK and EC competition enforcement provisions namely the Competition Act 1998 and Articles 101 and 102 of the Treaty on the Functioning of the European Union (formerly Articles 81 and 82 of the EC Treaty). This is because SM are unlikely to be considered 'undertakings' under these provisions (as SM are not engaged in economic activity). As such rules made by SM are not rules made by an undertaking and do not fall to be considered under these provisions. Alternative scrutiny arrangements are therefore required.

8 We would favour a mechanism whereby the OFT would be consulted by SM, on competition issues. Such a provision appears to exist in section 61, although the section is not entirely clear (see paragraph 15 below).

9 We would also wish to be able to bring to the attention of SM such competition issues that may from time to time arise in relation to the

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<sup>3</sup> OFT 1076, April 2009, page 12

<sup>4</sup> Section 4

regulation of legal services. As a corollary, the Bill should provide an obligation on SM to respond to competition issues raised.

- 10 Existing provisions for effective competition scrutiny which bear consideration are found in the provision in section 57 of the Legal Services Act 2007 ('the LSA 2007'). These provide OFT with an ongoing power to scrutinise regulatory arrangements and report to the LSB and a duty on the LSB to respond to competition concerns raised by OFT. In this capacity, OFT has investigation powers under sections 174 (3) to (5) of the Enterprise Act 2002 ('the EA 2002').
- 11 These provisions allow OFT to be active, not merely passive, about competition concerns and to ensure that the LSB responds to these when raised.
- 12 We wish to draw to the Justice Committee's attention that the Bill imposes no duty on SM to respond to OFT's concerns. We feel that the effect of such an omission is that Scottish consumers may not benefit from similar competition scrutiny arrangements as consumers in England and Wales.

#### **Competition scrutiny powers under LSA 2007**

- 13 The LSA 2007 defines five areas where the OFT has been given a specific role.
- A. Section 57 (as referred to in paragraph 11 above) provides the OFT with the power to investigate if it perceives the behaviour of any approved regulator to be anti-competitive.
  - B. Schedule 10 commits the LSB to seeking advice from the OFT on applications from regulators to become ABS licensing authorities.
  - C. Advising on the recognition of new approved regulators in Schedule 4.
  - D. Advising on additions, amendments and subtractions from the list of reserved activities in the terms set out under section 24 and 26, with the procedure defined in Schedule 6.
  - E. Commenting on any proposals for the LSB itself to become an approved regulator defined in section 66.
- 14 The Bill does not include provisions A, D and E. Section 6 of the Bill commits SM to consult the OFT before deciding whether to approve an applicant as an approved regulator which is similar to the OFT's role under B and C above.

- 15 There are provisions in the Bill such as in section 11 giving approved regulators discretion to consult the OFT where it believes that the granting of a licence may prevent or significantly restrict or distort competition. A similar test exists in section 61 though is unclear in which circumstances this would apply. The guidance notes suggest that this in relation to all competition matters but this is not reflected in the provision and we would suggest that this is clarified in the section.

**Competition scrutiny powers under the Bill**

- 16 The role of the OFT under the Bill is set out in the following sections.

- The OFT must be consulted by SM before deciding whether or not to approve an applicant as an approved regulator (section 6(3)).
- In respect of licensing rules, the OFT must be consulted where the Approved Regulator believes the granting of the licence application may have the effect of preventing competition within the legal services market or significantly restricting or distorting such competition (section 11(2)).
- In respect of the regulation of licensed legal services, section 61 concerns the occasions when SM and Approved Regulators consult with the OFT in relation to competition matters and what they must do. SM and the approved regulators must take into consideration any advice given by the OFT (section 61).
- In respect of confirmation services, the OFT must be consulted by SM before deciding whether or not to certify an applicant as an approved body. In consulting SM must send the OFT a copy of the application and may send a copy of any revised application (section 74(3) and (4)). There is an obligation on SM to take account of any advice given by the OFT within the relevant timescale when they consult the OFT (section 82).
- In respect of advocates, SM must consult the OFT and approve a change in any professional practice, conduct or disciplinary rule which prevents advocates from forming partnerships, before such a rule can have effect (section 89). It supersedes a similar rule in section 31 of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1990.
- SM have the power to make directions in relation to an approved regulator. Where SM consider that the proposed direction may have the effect of preventing competition within the legal services market or significantly restricting or

distorting such competition, the OFT must be consulted (Schedule 2(4) (3)).

- SM must send the OFT a copy of a notice of intention to rescind the authorisation of an approved regulator and consult the OFT accordingly (Schedule 6(4) (2)).
- SM must send the OFT a copy of a notice an approved regulators notice if surrender of authorisation and consult the OFT accordingly (Schedule 7(3) (1)).

17 As noted in paragraph 10 above the Bill provisions do not seem to provide a role for the OFT where it can provide symmetry of advice in both jurisdictions. This may result in a less effective competition scrutiny in Scotland.

18 We appreciate that powers exist under the EA 2002 which would allow the OFT to investigate and or refer any concerns by way of a market investigation reference to the Competition Commission.<sup>5</sup> However we anticipate that the use of these powers could be seen to be disproportionate. They arise where OFT sees that there are features of a market which prevent, restrict or distort competition and must decide whether to make a market investigation reference (or accept undertakings instead). These provisions were not specifically designed to provide competition scrutiny over an oversight body. It would be preferable for the Bill to place a duty upon SM to respond to competition concerns.

19 We also observe the absence of the powers of investigation under sections 174 (3) to (5) of the EA 2002 which may be due to issues of devolved competence. The effect is that the OFT would be unable to compel the production of evidence when considering whether the regulatory arrangements of an approved regulator (or any part of them) prevent, restrict or distort competition within the market for reserved legal services to any significant extent. This would therefore inhibit information gathering powers and could limit the effectiveness of any competition assessment.

20 We also note that the Bill omits a provision that SM may seek the advice of the OFT in relation to any additions, amendments and subtractions from the list of reserved activities and the OFT can choose to respond. We appreciate changes to the current reservations are not currently contemplated. However, we anticipate

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<sup>5</sup> Market investigation references: Guidance about the making of references under Part 4 of the Enterprise Act, OFT, March 2006, available at [www.offt.gov.uk/shared\\_offt/business\\_leaflets/enterprise\\_act/oft511.pdf](http://www.offt.gov.uk/shared_offt/business_leaflets/enterprise_act/oft511.pdf)

that it would be useful to provide for the future assessment of any such changes.

- 21 It would also be helpful if OFT could be invited to comment on any proposals for SM to become a temporary approved regulator as contemplated in section 35. (Such a provision exists under section 66 of the LSA 2007.)

**3 THE FACULTY OF ADVOCATES (THE 'FOA') AND ABS**

- 22 We are disappointed that the FOA will not permit the participation of advocates in ABS. As stated in our Consultation Response<sup>6</sup> we have identified the prohibition on advocates forming partnerships with other advocates or with other professionals as amongst the most restrictive of competition.

- 23 Allowing partnerships between advocates and others has the potential to increase the availability of advocates, by attracting practitioners to new areas of practice and would pave the way for young barristers to gain varied legal experience. We do not consider that the operation of the 'cab rank' rule justifies this restriction. We have questioned whether the 'cab rank' rule does in fact ensure the right of representation since advocates may already decline a brief on the grounds of work load and have some scope therefore to balance their workload and types of cases. We also queried the suggestion that removal of the existing rule would cause some clients to be significantly hampered in securing Counsel of the appropriate skill and experience.<sup>7</sup>

- 24 The ability of advocates to transfer to the solicitor advocate branch in order to participate in ABS does not alleviate the competition concerns of the OFT. We believe that the current arrangements for transfer lack transparency and appear to incur costs of time and loss of perceived status. There does not appear to be reciprocity for advocates who have become solicitor advocates to rejoin the

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<sup>6</sup> OFT 1076, April 2009, pages 17 - 18. See also: OFT Report in Professions, March 2001 paragraph 50;

Consultation on the future regulatory framework for legal services in England and Wales, OFT 722, June 2004, paragraph 3.2;

Report by the Research Working Group on the Legal Services Market in Scotland, 2006, paragraphs 8.8- 8.11, 8.23,8.24 and 8.42; and

OFT Response to Which? Super-complaint: Restrictions on business structures and direct access in the Scottish legal profession, OFT 946, July 2007, Chapters 3 and 4

<sup>7</sup> OFT 1076, April 2009, page 18

advocate branch. The status of solicitor advocates as a relatively new branch of the profession is still being developed. Given the historical dominance of FOA members in advocacy in the Higher Courts, there are questions about whether transfer from this prestigious branch, losing a badge which appears to carry weight both with clients and with the courts, imposes a significant professional cost to practitioners.

25 One such cost may be, as described to the OFT, the perception that a solicitor advocate is less likely to earn the QC title than an advocate. In our Consultation Response,<sup>8</sup> we revisited the discussions of the Research Working Group on the Legal Services Market in Scotland<sup>9</sup> and the proposal that the award of QC status should be examined further, as recorded by the Group's report. The arrangements are of relevance to the question of comparability of status between solicitor advocates and advocates as well as in the wider context of consumer information. We believe there is a need to consider how this title is awarded, whether it is in the interests of consumers and whether it distorts competition. In general, the OFT considers for the QC appointments process to function effectively:

- appointments should be made on an objective basis;
- the appointment process should be fair and transparent and performed by a selection panel composed of professional and lay interests;
- entry should be subject only to candidates meeting a standard without influence of any kind of quota; and
- awards should be revalidated from time to time, and be capable of being withdrawn.

26 We note that the appointment process is still performed by a senior judge and selection is at his discretion, in light of views sought from other senior judges and senior members of professional bodies. This does not appear to meet the criteria the OFT has sought and we would propose that the SG should take this opportunity to review and develop the process.

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<sup>8</sup> OFT 1076, April 2009, pages 19 - 20

<sup>9</sup> Report by the Research Working Group on the Legal Services Market in Scotland, Scottish Executive, May 2006, at paragraphs 11.13 and 11.16, available at [www.scotland.gov.uk/Resource/Doc/111789/0027239.pdf](http://www.scotland.gov.uk/Resource/Doc/111789/0027239.pdf)

**4            OVERSIGHT OF THE APPROVED REGULATORS**

27            In our Consultation Response, we reiterated our strong preference for the oversight function to be performed by a new independent public body, such as the LSB in England and Wales. However, in the absence of such a body, we suggested that the oversight function of the approved regulators should be exercised by SM together with an advisory panel, subject to competition scrutiny by the OFT.<sup>10</sup>

28            We have expressed concerns that requiring the Lord President's agreement would be seen to introduce a possible conflict of interest, given his position as a judicial officer and a member of the profession. Regulatory independence of the oversight body is crucial to the credibility of the legislation with consumers and the general public.

**5            TIME LIMITS FOR AUTHORISATION OF APPROVED REGULATORS**

29            We are disappointed with the inclusion of section 7(4)(a)(i), which allows authorisation to act as an approved regulator to be awarded without limit of time. We consider it necessary to have in place a robust procedure to review the authorisation of approved regulators, including reviewing how their regulatory scheme adheres to and applies the regulatory objectives and obligations. We therefore would wish to see the removal of section 7(4)(a)(i) so as to ensure that authorisation to be given only on a time-limited basis.

**6            'FIT TO OWN' TEST**

30            We have supported the introduction of the 'fit to own' test for ownership of a licensed legal service provider. We assume that the presumption in the Bill that an outside investor will be fit to own if qualified to practise as a solicitor is because a solicitor's fitness to own is dealt with by the regulation of the individual solicitor.

31            This however deviates from the current proposals in England and Wales where the LSB has proposed that there should be one test for all owners of an ABS, whether they are lawyers or non lawyers. The objective of this provision is to ensure consistency across all licensed authorities so that ABS regulated by one licensed authority are not

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<sup>10</sup> OFT 1076, April 2009, page 11

perceived to be riskier than those regulated by another licensed authority.<sup>11</sup>

32 The LSB has also proposed that there will be an obligation to notify the appropriate regulator of any change of circumstances that is relevant to the test.<sup>12</sup> We assume that rules placing such an obligation on ABS owners in Scotland would be a requirement of an approved regulator's regulatory scheme, to ensure that if an outside investor, including a qualified solicitor, was no longer deemed fit to own, the regulator must be informed.

**7 SEPARATION OF REGULATORY AND REPRESENTATIONAL ROLES**

33 The OFT considers that it should be a pre-condition of the continuing regulatory involvement of the Law Society of Scotland (the LSS) and the FOA that they separate their regulatory and representative functions and do so to the satisfaction of the oversight body. We consider this critical to ensuring that regulation is in the public and consumer interest.

34 We believe that securing the independence of the regulatory arm acting with demonstrable independence from representational interests would be best achieved by a completely separate regulatory body. This is the model now in dentistry and in medicine with the British Medical Association and the British Dental Association representing members and the General Medical Council and General Dental Council regulating those professions. However we appreciate that the formation of a new body may not immediately be feasible but it should be a long term objective.

**Governance of the Law Society of Scotland ('the LSS')**

35 We welcome the proposals in the Bill to modernise the governance of the LSS. We welcome the requirement for the LSS's regulatory committee to comprise of at least 50 per cent lay membership with a lay convenor.<sup>13</sup> We agree with Consumer Focus Scotland that there

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<sup>11</sup> Alternative business structures: approaches to licensing, Consultation paper on draft guidance to licensing authorities on the content of licensing rules, Legal Services Board, November 2009, paragraph 88 available at [http://www.legalservicesboard.org.uk/what\\_we\\_do/consultations/2009/pdf/consultation\\_181009.pdf](http://www.legalservicesboard.org.uk/what_we_do/consultations/2009/pdf/consultation_181009.pdf)

<sup>12</sup> Alternative business structures: approaches to licensing, Consultation paper on draft guidance to licensing authorities on the content of licensing rules, Legal Services Board, November 2009, paragraph 71

<sup>13</sup> Section 93(3)

should be a lay majority on the LSS Council as this will enhance public perception that the LSS is fulfilling its public interest role although we remain unconvinced that a representational body can do this effectively. We will be interested to see what steps the LSS will take in order to build public confidence, to make the public and consumers aware that it has a separate regulatory committee.

36 We also consider that the process for appointment of lay members is seen by both the public and the profession to produce qualified and genuinely independent members from a variety of backgrounds well suited to considering the consumer and public interest.

37 We believe the Bill could benefit from greater explanation of what is meant by the 'representative functions' and 'regulatory functions'. We also query how regulatory independence will be safeguarded and suggest the Bill stipulates how and whom would carry out such the review contemplated in section 20(1) (c).

#### **Governance of the FOA**

38 We are also disappointed by the provisions relating to the governance of the FOA.

39 We do not believe the current provisions within the Bill offer sufficient clarity to allay fears about the lack of independent oversight of the FOA. The current provisions<sup>14</sup> allow for the Court of Session to delegate regulatory responsibility to the FOA or Lord President but no further clarification is offered as to how this relationship would function in practice. We note the lack of any codified statement about how consumers or other individuals/organisations may refer regulatory concerns to the Lord President acting in his capacity as oversight regulator of advocates. We therefore remain concerned by the continued lack of clarity of the FOA's regulatory and governance framework and believe the Bill would be strengthened if, as a very minimum, such further provisions clarifying these frameworks were to be added.

40 We consider that the FOA should have regulatory responsibility only where it can demonstrate that this will not conflict with its representational responsibilities. Consumers and the public at large are unlikely to trust any regulatory framework unless and until they are satisfied that it is separate and independent from representative self-interest.

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<sup>14</sup> Sections 87-89

41 The OFT's view is that the FOA should also be regulated by the oversight body and that its representational and regulatory function split. If such amendment or alternation of the FOA's prohibition of members joining ABS is not being pursued, we propose that the legislative framework should provide for the future alteration of the FOA's governance structure without further recourse to primary legislation.

**8 ADVISORY PANEL**

42 In our Consultation Response, we favoured the setting of up an advisory panel which would represent the interests of consumers and to provide advice to SM (similar to the role of the Consumer Advisory Panel established under the LSA 2007 sections 8- 11).<sup>15</sup>

43 We are surprised that the Bill does not include provision for the establishment of an advisory panel to advise SM as this was a strongly favoured provision. The proposals for establishing an advisory panel were supported by more than three quarters of the consultation respondents.<sup>16</sup> Whilst we welcome the intention of the SG, as set out in the Policy Memorandum accompanying the Bill, to use its powers to set up a panel at the implementation stage of the legislation,<sup>17</sup> our preference is still for the advisory panel to be a statutory body to give it legislative backing.

44 In the absence of a new independent body as oversight regulator we believe an advisory panel would greatly assist SM in the exercise of their oversight role. We suggest that the panel be comprised solely of lay members from a diverse background, though including some with a clear consumer interest. We would strongly advocate including provision for such a panel in the Bill.

**9 REGULATORY OBJECTIVES**

45 We welcome the fact that the regulatory objectives will apply to all regulators of legal services in Scotland. Under section 38(1) (a) of the Bill, licensed legal services providers must have regard to the regulatory objectives. In order to create a level playing field this duty

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<sup>15</sup> OFT1076, April 2009, page 11

<sup>16</sup> Analysis of the Responses to the Consultation on the Regulation of Legal Services in Scotland, Research Findings No.15/2009, page 4

<sup>17</sup> Policy Memorandum on the Legal Services (Scotland) Bill, 30 September 2009, paragraph 133

should be extended to all forms of practice and to all legal professionals including advocates.

- 46      OFT considers that there should be a single set of provisions that apply to the current structures and providers of alternative business structures. We are concerned that the higher standards for ABS might act as a disincentive for firms to move to ABS. It is important that the regulatory principles, which could be passported for some applicant approved regulators, are not seen as an added burden and have the practical effect of limiting the feasibility of some models of ABS, particularly some of the innovative models which may emerge in rural areas.
- 47      The OFT believes, as set out above, that the FOA and its members should similarly be subject to the regulatory arrangements set up under the new regime.
- 48      We welcome the inclusion of the objective of 'encouraging an independent, strong, varied and effective legal profession'. However, we are disappointed at the decision not to include the objective of 'increasing public understanding of the citizen's legal rights and duties' although we welcome the SG's recognition in the Policy Memorandum that this is an important policy aim.<sup>18</sup>
- 49      We are disappointed that complaints about approved regulators are to be made to SM rather than the Scottish Legal Complaints Commission ('the SLCC'). We feel that this will have the effect of removing the single gateway for complaints. Our concern is that this may cause confusion for consumers. Moreover, while we note SM have the authority to delegate the investigation of such a complaint to the SLCC, the decision of whether the complaint is 'frivolous, vexatious or totally without merit' will always rest with SM.
- 50      We believe that consumer confidence in the complaints handling function is crucial and we are not convinced that there shall be such confidence in a complaints process if a decision as to the merit of a complaint lies with SM.
- 51      We are also concerned that there do not appear to be equivalent provisions to those contained in section 65 for approved regulators, for making complaints about how the regulators outlined in section 86 (which includes the LSS and the FOA) exercise their regulatory functions. We believe this requires to be set out in the legislation and we believe an appropriate body to deal with such complaints would be the SLCC.

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<sup>18</sup> Policy Memorandum on the Legal Services (Scotland) Bill, 30 September 2009, paragraph 74

**10            GUARANTEE FUND**

52            We note that the Bill does not include any provisions in relation to the Guarantee Fund. While most claims are against sole practitioners as those who work in partnerships are likely to be covered by the Master Policy and under the Bill licensed providers would be required have an equivalent level of professional indemnity, our preference is for the Guarantee Fund to also apply to licensed providers so that consumers have the same protection irrespective of provider.

**11            PROFESSIONAL INDEMNITY**

53            Section 19 includes a requirement for licensed providers to keep in place sufficient arrangements for profession indemnity and include a provision corresponding to that applying under section 44 of the 1980 Act in relation to incorporated practice. Currently this would be insurance under the 'Master Policy'. We believe that ABS providers should have choices of insurance providers as indicated in our Consultation Response.<sup>19</sup> We are concerned that any provision that might deny access to a range of insurers could inhibit development of ABS.

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<sup>19</sup> OFT 1076, April 2009, page 17