

**EXPLANATORY MEMORANDUM TO  
THE LEGAL SERVICES ACT 2007 (COMMENCEMENT NO.1 AND  
TRANSITORY PROVISIONS) ORDER 2008**

**2008 No. 222 (C. 6)**

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

**2. Description**

2.1. The instrument commences a range of provisions in the Legal Services Act 2007 ('the 2007 Act') which, among other things, establish the Legal Services Board ('the Board') and allow the Board to make appointments to the Office for Legal Complaints ('OLC').

2.2. It also commences transitional provision in Schedule 22 of the 2007 Act which allows the Lord Chancellor to modify the functions of existing legal services regulators (e.g. the Council for Licensed Conveyancers) pending the establishment of the Board. Parallel provisions in the 2007 Act which operate once the Board is established have been modified to enable an order to be made by the Lord Chancellor to modify the functions of the Solicitors Disciplinary Tribunal ('SDT') and bodies that will be "approved regulators" under the new framework. The modification prevents a gap arising between the transitional provision lapsing and the introduction of the new regulatory regime in full (expected in 2010).

2.3. The instrument also makes transitory provision to enable the Lord Chancellor to pay members of the Board and the OLC until the Chief Executive of the Board is appointed. At that time the Board will be fully constituted and financial responsibility would transfer from the sponsoring department to the Board. In addition, there a number of minor provisions streamlining the legislation which apply to Solicitors and Licensed Conveyancers and other minor and consequential amendments.

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

3.1 None.

**4. Legislative Background**

4.1. This instrument commences provisions of the 2007 Act which received Royal Assent on 30 October 2007. This is the first commencement order and the first order made under sections 208 (2) and (4) and 211, which enable the Lord Chancellor to make any "transitory, transitional or saving provision" or "adaptations of provisions of this Act brought into force". The 2007 Act introduces a completely new regime for the regulation of "reserved legal services" and sets up a new structure for the supervision of bodies which regulate lawyers. It also makes a large number of amendments to the legislation which governs certain legal services regulators who are governed by statute. This includes amendments to the Solicitors Act 1974, the Administration of Justice Act 1985, the Courts and Legal Services Act 1990 and the Compensation Act 2006.

**5. Extent**

5.1. This instrument relates to provisions which apply to England and Wales.

## **6. European Convention on Human Rights**

6.1. The Parliamentary Under Secretary of State, Bridget Prentice, has made the following statement in relation to the provisions of this Order which modify the 2007 Act:

In my view the provisions of the Legal Services Act 2007 (Commencement No.1 and Transitory Provisions) Order 2008 are compatible with the Convention rights.

## **7. Policy Background**

7.1. The 2007 Act reforms the way in which legal services are regulated in England & Wales. The 2007 Act establishes an oversight regulator; the Legal Services Board, and an independent complaints handling body; the Office for Legal Complaints. It also provides for alternative business structures ('ABS'), which will enable firms to explore new ways of organising their business. In addition, the 2007 Act also establishes a single set of regulatory objectives (section 1) which will apply to the Board, the OLC and approved regulators (e.g. the Law Society, Bar Council).

7.2. A key aim of the legislation is to simplify the existing regulatory framework, which has a number of oversight regulators, including the Master of the Rolls, the Secretary of State of Justice and the Archbishop of Canterbury. The Board, as oversight regulator, will be able to ensure greater consistency of standards across the legal sector, while approved regulators will be responsible for day-to-day regulation. Another driver for change was the need to improve the way in which complaints are dealt with and to improve consumer confidence. The OLC will be an independent body that will administer an ombudsman scheme which will deal with consumer complaints about legal services providers. The scheme will be able to provide quick and fair redress. Furthermore, the Act facilitates ABS which offers greater choice for the legal profession and consumers about the way that services are provided, including permitting different kinds of lawyers and non-lawyers to work together, and allowing for external investment.

7.3. It is anticipated that the Board and the OLC will not be fully operational until 2010 and therefore this instrument deals with the establishment and constitution of those bodies rather than the Board's oversight functions (for example, its powers of direction and target setting in relation to approved regulators), or the OLC's complaints handling functions. Neither does the instrument commence provisions relating to ABS at this time. In particular, this instrument commences provisions which confer powers on the Lord Chancellor to make appointments to the Board, after consultation with the Lord Chief Justice, and other provisions which relate to the constitution of the Board (e.g. the requirement for there to be a lay majority, and the power for the Board to appoint the Chief Executive). The establishment of the OLC, and appointment of its members by the Board, is also dealt with in this instrument under the transitional powers in schedule 22 to the 2007 Act. This provision was brought forward to enable the ordinary members of the Board to appoint the members of the OLC, without the Chief Executive being appointed, to prevent a delay in the implementation timetable.

7.4. It should be noted that financial responsibility will only transfer from the sponsoring Government department to the Board once it is fully constituted (i.e. once the Chief Executive is appointed). As a result of this policy, a transitional power has been put in place to clarify that the Lord Chancellor can remunerate members of the Board and the

OLC until the Chief Executive of the Board is appointed, and the Board assumes financial responsibility.

7.5. Sections 69, 70 and 180 are intended to prevent statutory regulators, for example the Law Society and the Council for Licensed Conveyancers, being at a significant disadvantage when compared to non-statutory regulators. For example, the Law Society would require amendments to the Administration of Justice Act 1985 to confer the necessary vires to regulate ABS, should it be designated as a licensing authority. Any amendments would need to be carried out by primary legislation. It is the Government's view that it would be impractical to return to Parliament every time new vires or powers were required and would be unnecessarily time intensive. In contrast, a non-statutory body would only require changes to its rules, following designation as a licensing authority. This would not create a level playing field for regulators, and would instead confer an unfair advantage to certain types of body.

7.6. The Government recognises that there may be instances, prior to the Board being fully constituted, when bodies that will be approved regulators under the future framework, may need to have their functions modified by order (for example, to update the regulatory powers of the Law Society in the Solicitors Act 1974, to enable them to prepare for their role as an approved regulator). Paragraphs 1 to 4 of Schedule 22 ensure that there will be transitional provisions in place and allow bodies authorised to provide reserved legal activities under the Courts and Legal Services Act 1990, to be brought into the new regulatory framework before the commencement of paragraph 1 of Schedule 4 to the Act, without having to reapply to the Board for authorisation.

7.7. However, the powers in schedule 22 paragraphs 1 to 4 (Transitory power to modify the functions of bodies) do not apply once the Chief Executive of the Board is appointed. Therefore, in order to prevent a gap in the provision, we have modified sections 69, 70 and 180 to enable the Lord Chancellor to make an order on the recommendation of the Board before bodies in the list at paragraph 1 of schedule 4 become approved regulators. This will help maintain the level playing field between statutory and non-statutory bodies during the various stages of implementation.

### *Consultation and Guidance*

7.8. The 2007 Act is the result of extensive consultation both before and during the Parliamentary process. The key groups that were consulted were consumer organisations, regulatory bodies, other professional representative bodies and other key stakeholders, such as the Offices of the Legal Services Ombudsman and Legal Services Complaints Commissioner. In particular, the Government consulted following the 2001 report on competition in the professions by the Office of Fair Trading<sup>1</sup>, and published a report into competition and regulation in the legal services market.<sup>2</sup> Further to that, in 2003, Sir David Clementi was appointed by the Government to conduct an independent review of the regulation of legal services<sup>3</sup>, which was the basis for the proposals set out in the

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<sup>1</sup> Office of Fair Trading, 2001, *Competition in the Professions – A Report by the Director General of Fair Trading*

<sup>2</sup> Department for Constitutional Affairs, 2003, *Competition and Regulation in the Legal Services Market – A Report Following the Consultation “In the Public Interest?”*

<sup>3</sup> Clementi, Sir David, 2004, *Review of the Regulatory Framework for Legal Services in England and Wales – Final Report*

Government's White Paper, *The Future of Legal Services: Putting Consumers First*, published in October 2005. A summary of the responses to the White Paper are included in chapter 2 ("consultation") of the Regulatory Impact Assessment ('RIA'). Extracts of the full RIA are attached to this memorandum (Annex A: Regulatory Impact Assessment and Supplementary Memorandum).

7.9. The draft Legal Services Bill was published in May 2006 and was subject to pre-legislative scrutiny by a Joint Committee of both Houses of Parliament. The Joint Committee reported in July 2006, and the Government published its response to this in September of the same year.

7.10. A Consumer Panel was also established in 2005 to advise in the development of the 2007 Act, and it continues to advise on the implementation of the legislation. In addition, the Government continues to consult with relevant stakeholders during the commencement of the legislation and has set up the Implementation Working Group (established in April 2006) which includes representatives from existing legal regulators and consumer groups, amongst others.

## **8. Impact**

8.1. A full RIA was prepared for the Legal Services Bill in November 2006, and a supplementary memorandum was published in June 2007. A further RIA has not been prepared for this instrument, although the full RIA and supplementary memorandum which relate to the provisions commenced in this instrument. For convenience, we have annexed the relevant chapters from the RIA to this memorandum (Annex A: Regulatory Impact Assessment and Supplementary Memorandum). Those chapters are: chapter 2, chapter 4, chapter 6, paragraphs 9.13 and 9.14 of chapter 9, chapter 12 and chapter 13 including the summary of expected benefits and costs tables relating to the LSB and the OLC. The full RIA includes sections which examine the options considered and our reasoning for the final recommendations which were brought forward in the Act. The full RIA can be found at <http://www.dca.gov.uk/risk/ria-legal-services.pdf>

8.2. The forecasts for implementation and running costs of the Board and the OLC are set out in the supplementary memorandum (attached in full at Annex A: Regulatory Impact Assessment and Supplementary Memorandum). The implementation costs are forecast to be £32.1 million (in 2007-08 current prices), of which £19.9 Million would be recovered through the levy on approved regulators, £9.8 million would fall directly on the Law Society and £2.4 million would fall to the Ministry of Justice. The running costs will also be met through the levy and at current 2007-08 prices, are £4.0 million for the Board and £19.9 million for the OLC.

## **9. Contact**

9.1. Any enquiries about the contents of this Memorandum should be addressed to:

Kerri Phillips  
Legal Services Regulation  
Ministry of Justice

## **Annex A: Regulatory Impact Assessment and Supplementary Memorandum**

### **2. Consultation**

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#### **Engagement with stakeholders**

2.1. Throughout the development of its proposals, the Government has held discussions with key stakeholders. These include:

- **Consumer organisations:** such as Which?, Citizens Advice, National Consumer Council, the Federation of Small Businesses, the Equality Commission, Complaints Against Solicitors Independent Adjudication (CASIA), and Reform Of Complaints Against Solicitors (ROCAS).
- **Regulatory bodies:** including the Law Society, the General Council of the Bar, the Institute of Legal Executives, the Institute of Trade Mark Attorneys, the Chartered Institute of Patent Agents, the Council for Licensed Conveyancers, the Court of Faculties, the Council of the Inns of Court, and the Association of Law Costs Draftsmen.
- **Other professional representative bodies:** such as City of London Law Society, Association of Personal Injury Lawyers, Resolution, and Legal Aid Practitioners Group.

- **Others include:** Office of the Legal Services Ombudsman, Office of the Legal Services Complaints Commissioner, British Bankers Association, Legal Action Group, Law Centres Federation, and Amicus.

### *Responses to the White Paper*

- 2.2. The Legal Services Reform White Paper invited comments on the Government's proposals. The Department for Constitutional Affairs received just over 100 responses. The vast majority accepted and supported the Government's proposals for reform.
- 2.3. Just over half of the responses represented the views of the legal profession, while a quarter were from the consumer organisations or members of the public. The remainder represented other professions, the not-for-profit sector, and other interested parties.
- 2.4. Responses from the larger professional bodies were mixed, but in the main were supportive of the Government's objectives and its main proposals. However, some bodies expressed concerns about the need for careful implementation to ensure, for example, that the Government did not create a large bureaucracy in setting up the Legal Services Board (LSB). Responses consequently raised concerns about the LSB's governance structure maintaining the professions' independence from government, and about the need to limit further the LSB's powers to ensure that it was proportionate and risk-based. They also continued to press the Government to contribute to the cost of reform and were opposed to the profession paying for the full costs. They also raised some concerns about the alternative business structure (ABS) proposals, including issues about access to justice as well as the cost of the reforms.
- 2.5. Responses from the other professional bodies also argued strongly in favour of the Government contributing to the costs of the new arrangements. There were also concerns that the voice of the smaller bodies could be lost in the regulatory framework, and some argued for a professional advisory panel. Other concerns included the added bureaucracy of applying ABS safeguards, a concern that the new Office for Legal Complaints (OLC) should not be essentially the Law Society's Consumer Complaints Services "re-badged", and an argument that the OLC should have the power to delegate complaints handling to those ARs that met minimum service standards. Finally, the smaller bodies wanted to see a central compensation fund established to which all legal service providers would contribute.
- 2.6. The consumer organisations remained extremely supportive of the proposals, as they had been throughout their development. Generally their main concern was that the OLC should have sufficient powers to deal effectively with consumer complaints. The Consumer Advisory Panel, which was established to advise the Government on the implementation of the proposals for legal service reform, has played a key role in the detail and development of these proposals. Membership of the Panel comprises Citizens Advice, Which?, National Consumer Council, Federation of Small Business and the Equal Opportunities Commission (with the OFT assisting).
- 2.7. Responses from the NfP sector were broadly supportive of the prospect of regulation via the ABS framework. Some NfP organisations actively welcome this on the basis that this will provide greater clarity to providers over how regulation applies to them, and more consistent protection for consumers. However, there were also concerns expressed that the new framework will lead to higher costs for charitable organisations and smaller providers, and that there is insufficient recognition of the different objectives of commercial and NfP providers. Some respondents felt that the proposals in the White Paper for LSB discretion did not go far enough in counteracting the threat of greater regulatory burdens, whereas others expressed concerns that these should not mean less scrutiny of NfP practices or the quality of services they offer to consumers.
- 2.8. The Government also received various responses from businesses which were supportive of

the ABS proposals and the possible opportunities that those proposals would enable.

- 2.9. The trade union response was broadly supportive of the proposals for the LSB, OLC and ABS. However, their primary concern was to ensure that the services they provide would not be captured by the definition of legal services and asked for a specific exemption. They also expressed a wish for any individuals affected by the Government’s proposals to be dealt with fairly.

### **Impact of consultation on the proposals**

- 2.10. Public responses to the Government’s White Paper and the results of its stakeholder engagement have resulted in some amendments to the policy proposals set out in the White Paper. The table below identifies the key changes:

	<b>White Paper reference</b>	<b>Change/addition</b>
<b>LSB - Diversity Objective</b>	The White Paper made references to the general increase in diversity of the legal profession, but did not set it as an objective of the LSB.	The Government considers that the objective of the LSB to “encourage a strong, effective legal profession” should be amended to “encourage a strong, effective and diverse legal profession”.
<b>LSB - Consumer Affairs</b>	The White Paper stated that members of the LSB Board and Consumer Panel would between them have experience of “consumer affairs”.	The Government intends that the legislation should require the Consumer Panel to have a fair degree of members representation of all types of consumers, including sophisticated consumers who are using reserved services in connection with businesses carried on by them.
<b>LSB - duty to consider representations of ARs and representative bodies</b>	The White Paper did not set out a general requirement for the LSB to consult the profession, although it would have consult the Secretary of State for Constitutional Affairs, its Consumer Panel, the OFT and the Senior Judiciary when authorising/deauthorising approved regulators, bringing in unregulated activities under the LSB’s scope, regulating directly, reviewing targets/sanctions or altering the rules of an AR.	The Government intends to place a duty on the LSB to consider the representations of ARs or representative bodies before exercising its powers (e.g. the power to issue a direction). The LSB, once it is established, will have the flexibility to decide the most effective way to consult the profession in exercising its other statutory functions, including the option of setting up a professional panel.
<b>ABS - register for ABS firms</b>	The White Paper did not mention the maintenance of a register of ABS firms.	The Government considers that licensing authorities should be under a duty to maintain a publicly accessible register of their licensed ABS firms. The LSB will be required to make the rules governing the registers.
<b>ABS - removal of HOLP</b>	The White Paper proposed that ABS regulators would have to provide consent before an ABS	This requirement will not be set out in the legislation.

	firm could remove the HOLP.	
<b>Complaints - role of Ombudsmen</b>	The White Paper proposed that complaints about lawyers should be determined by arbiters.	The Government considers that complaints should be determined by ombudsmen rather than arbiters.
<b>Complaints - name of the new complaints handling body</b>	Sir David Clementi referred to the complaints body as the “Office for Legal Complaints”, and the Government adopted this term in public discussion – including in the White Paper.	Provision has been made in the legislation to allow the new complaints-handling body to determine its own trading name (so, as part of the Government’s preferred branding for Alternative Dispute Resolution schemes, the OLC could choose to operate under a title including the term Ombudsman).

### 3. Sectors and Groups Affected

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3.1. The Government has identified that the following sectors and groups will be affected by its proposals:

- consumers of any legal services;
  - members of the legal professions that provide reserved legal services (barristers, solicitors, legal executives, licensed conveyancers, notaries, patent agents, and trademark attorneys);
  - legal professional and/or regulatory bodies that regulate the provision of reserved legal services (Bar Council, Law Society, Institute for legal Executives, Council for Licensed Conveyancers, Court of Faculty, Chartered Institute of Patent Agents, and the Institute of Trade Mark Attorneys);
  - providers of unreserved legal services, including general legal advisors, will writers, employment advisors and claims managers;<sup>19</sup>
  - businesses and organisations that currently employ ‘in-house’ lawyers;
  - all NfP organisations that offer legal advice and purchase legal services;
  - Government and the Government Legal Service;
  - existing oversight regulators (e.g. the OFT);
  - potential investors/partners in ABS firms;
  - providers of immigration services and the Immigration Services Commissioner; and
- the Offices of the Legal Services Ombudsman and Legal Services Complaints Commissioner.

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<sup>19</sup> The Government has proposed to introduce a statutory framework for the regulation of claims management services. Measures to achieve this form part of the Compensation Act.



## 4. Reforming the Regulatory Framework for Legal Services

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### Options for reform of the regulatory framework

- 4.1. The following options for the reform of the regulatory framework for legal services have been considered:

#### **Option 1 – Do nothing**

- 4.2. The current regulatory arrangements for legal services would be retained. Under this option, the weaknesses of the current system of regulation for existing professional bodies that are over-complex and inconsistent would remain. Moreover, some existing professional bodies would retain their dual roles of representing and regulating their respective professions. There is a risk that regulations on conduct and business structures would continue to be set with insufficient regard to protecting and promoting consumer interests, and promoting competition.

#### **Option 2 – A new single regulatory authority**

- 4.3. Under this option a single regulatory authority, the **Legal Services Authority (LSA)**, would be created. It would be based largely on the Financial Services Authority (FSA) model, and would exercise full regulatory control over the provision of all legal services. The LSA's functions would be analogous to those of the FSA, including the setting and enforcement of the rules and codes governing service provision, giving guidance and advice on general policy, and exercising investigative, enforcement and disciplinary powers. Regulatory power would be taken away from existing self-regulating bodies and vested in the LSA, with the existing professional bodies relegated to a solely representative role.

#### **Option 3 – An oversight regulator**

- 4.4. Under this option, a new independent oversight body, the **Legal Services Board (LSB)** would be created. The LSB would assume the roles and responsibilities of the range of the existing oversight regulators, providing consistent and appropriate oversight of Approved Regulators (ARs). These would be existing (or new) professional or other bodies which could seek authorisation from the LSB to act as ARs for the provision of reserved legal services, to perform the day-to-day regulatory functions. In considering applications for authorisation, the LSB would want to ensure that ARs met its statutory requirements (e.g. in having appropriate governance arrangements that provide for a clear split in the exercise of their regulatory and representative functions).
- 4.5. In addition, if the LSB was satisfied that an authorised AR was not exercising its regulatory functions to a high standard, it would have the power to take action, including the right to de-authorise the failing AR. Where no appropriate AR exists, the LSB will have the power to regulate authorised persons directly. Where it is doing so, the LSB will have powers conferred on it to ensure that it can provide effective regulation. In addition, to provide additional consumer protection, the LSB could apply for designation as an enforcer under Part 8 of the Enterprise Act 2002. This would provide the LSB with the power to seek “stop now” orders. In effect this would mean that the LSB would be able to obtain a court order to require practices or individual practitioners to cease carrying out a specified activity immediately, where that activity breached certain legislation and harmed the collective interests of consumers. This can be used in rare cases of flagrant and particularly damaging abuse.

- 4.6. Additional legal service activities would be brought into, or taken out of, the scope of the LSB's regulatory reach by secondary legislation.
- 4.7. Where appropriate, there would be a statutory requirement for the LSB to consult the OFT, the Secretary of State, the higher judiciary and its Consumer Panel<sup>20</sup> about its regulatory decisions. The LSB would also be able to enter discussions regularly with other statutory regulators, such as the Financial Services Authority (FSA), on regulatory issues.
- 4.8. This is the option preferred by the Government on reforming the regulatory framework for legal services. Through retaining the day-to-day functions of the existing professional bodies, the proposed regulatory framework will be able to utilise the expertise of the legal professional bodies while providing an oversight body that has the powers to ensure that regulation is set according to consumers' interests. The LSB will be less bureaucratic while reducing the potential for additional regulatory burden on both professional bodies and firms, encouraging competition and innovation in the market, and possibly reducing the price of legal services while improving the quality of legal services. Most importantly, the LSB will have the power to ensure that the regulation of the profession is consistent with all the objectives of the Government's reform of the regulatory framework for legal services in England and Wales.

## **Benefits and costs of options of reforming the regulatory framework for legal services**

### **Option 1 – Do nothing**

#### *Benefits*

- 4.9. There would be no additional economic or social benefits arising from this option.

#### *Costs*

- 4.10. Through retaining the current regulatory arrangements for legal services, the weaknesses of the system, such as its over-complex and inconsistent arrangements, would remain. Consumers would continue to lack the necessary knowledge to make accurate assessments of the value for money of the services they have purchased and/or whether the legal advice and representation they received can solve their problems. In addition, there is a risk that regulations on conduct and business structures would continue to be set with insufficient regard to protecting and promoting consumer interests or promoting competition, innovation and diversity in the legal profession.
- 4.11. There would be no additional policy costs arising from this option. Using information provided by the legal professional bodies, PricewaterhouseCoopers (PwC), in their independent report on the regulatory reform of legal services,<sup>21</sup> estimate that the total

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<sup>20</sup> The Consumer Panel would advise the LSB on the need of consumers of legal services. The members of the Panel would be appointed on merit and would have experience of consumer affairs.

<sup>21</sup> PricewaterhouseCoopers prepared a report for the Department of Constitutional Affairs (DCA) in connection with the DCA's consideration of the financial assessment of the Legal Services Reform. The figures published/stated are exclusive of VAT and are dependent on the assumptions made by PwC and inevitably is subject to a number of uncertainties. PwC's independent report is published on DCA's website and can be found at: <http://www.dca.gov.uk/legalsys/lrreform.htm>

regulatory costs in 2005-06 were some £97.4 million. Of these costs some £64.9 million relate to regulatory functions, including disciplinary costs.<sup>22</sup> This estimate does not fully capture the opportunity cost of the time spent by high-level regulators (e.g. senior judicial and ministerial time) and therefore understates the total cost of regulation in this respect.

4.12. The Law Society's costs represent a substantial proportion of this total at approximately 71%.

## **Option 2 – A new single regulatory authority**

### ***Benefits***

#### Economic benefits

4.13. As all regulatory functions would be vested in and carried out by the LSA, whose objective would be to promote consumer interests, the emphasis on service-driven regulation should reduce the risks of regulations on entry to the professions and conduct and business structures being set more strictly than necessary. This in turn should help promote competition and innovation in the legal services market. Provided that the LSA was an effective organisation in ensuring that regulation was in the consumer interest rather than that of providers, prices for legal services could fall and the market expand, to the benefit of consumers.

4.14. The creation of a single and independent regulator that removed the self-regulatory elements within the regulatory framework and had significant non-legal/consumer influence should lead to greater accountability by reducing conflicts of interest between the regulatory and representative functions of the professional bodies. This would also improve the transparency of regulatory procedures and increase regulatory certainty. This in turn should increase consumer confidence in the professions, potentially leading to an increase in the demand for legal services.

4.15. A single regulator would be likely to lead to the harmonisation of regulation and the reduction of regulatory inconsistencies for the legal sector. The resulting reduction of regulatory burden stemming from the duplication of regulatory functions<sup>23</sup> and increased efficiencies could lower compliance costs for existing suppliers. This could encourage new entrants into the sector, increasing competition and innovation. The harmonisation of regulation should also prevent suppliers from taking advantage of the operation of different regulators covering the same services by choosing the one most convenient for them. This would reduce the risk of regulations being weakened and consumer protection endangered. As a result, the quality of legal services should improve, to the benefit of consumers.

4.16. The LSA's having the power to set and impose directly professional rules, standards of services and rules of conduct consistently across the legal professions, would mitigate the risk of regulatory capture<sup>24</sup>. This would ensure that decisions regarding regulatory issues were taken independently and would facilitate consumer input into the decision-making process, thus protecting consumer interests.

4.17. A single regulator should facilitate more consistency in training and entry standards, permitting common training between different legal service providers and making it easier to transfer between them. This should lower the barriers to entry to the legal services market for potential new entrants, and promote diversity and competition among providers.

4.18. A single regulator should provide a clear forum for dealing with any conflicts in the

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<sup>22</sup> This includes enforcement, rule making, monitoring, rule-making activities and setting entry standards, but excludes complaints handling and disciplinary costs.

<sup>23</sup> See Section 1, Rationale for Government Intervention to Reform the Regulatory Framework

<sup>24</sup> Regulatory capture occurs when regulators advocate the interests of the suppliers that they regulate rather than the consumer.

objectives within the regulatory regime. It is better that resolution of such conflict rests within one accountable body, rather than in separate bodies with different vested interests.

- 4.19. A single regulator should permit greater flexibility in the system. The emergence of new services that required regulation would not require the setting up of new bodies to regulate them in the future. This would reduce the emergence of regulatory anomalies and gaps. A single regulator would also make it easier to regulate Alternative Business Structures firms (ABS), through the simplification and concentration of regulatory powers in one body.

#### Social benefits

- 4.20. A single regulator would be likely to lead to greater consistency, providing a single coherent system of authorisation, supervision and investigation, which would demonstrate transparency and accountability to the consumer. In addition, clearer lines of responsibility and greater accountability for the objectives of the regulatory system would lead to greater consumer confidence and awareness of consumer rights.
- 4.21. The shift away from a professionally-driven approach to one that was more service-driven might be accompanied by a more consumer-driven approach, one that emphasised the need to satisfy consumer interests rather than sustaining the standing of the professional provider. This should improve customer relations and society's perception of legal service providers.

#### *Costs*

##### Economic costs

- 4.22. There would be a substantial risk that, through increasing workload after its creation and with a lack of sound management, the LSA could become an overly bureaucratic and inefficient organisation, with consequent problems of cost and unwieldy procedures. In addition, it is possible that regulatory expertise would be lost during the transitional period, through the abolition of the professional bodies' regulatory powers. Moreover, with all regulatory functions being performed by the LSA, the potential for competition between the professional bodies in the provision of representative and regulatory services would be removed.
- 4.23. There is a risk that the creation of the LSA would produce additional regulatory burdens on the professions (compared to the other options), incurring significant additional compliance costs for existing and potential new suppliers. This might result in existing suppliers transferring the additional costs to consumers, leading to price increases without any corresponding increase in quality. Moreover, there is a risk that these costs would fall disproportionately on legal practitioners in rural areas and small practices, and potentially be passed onto their customers, as there would be fewer practitioners in these practices to shoulder the additional cost burdens. The additional costs might also result in a rise in entry costs sufficient to deter potential new entrants to the legal services market, stifling competition and reducing the incentives for existing suppliers to innovate.
- 4.24. Establishing an independent LSA with all regulatory powers vested in it would make it less likely that the expertise of the professional bodies for setting the levels of entry standards and training, formulating professional rules, monitoring compliance and enforcing the necessary codes of conduct would be utilised. It would be less likely that the professions would be willing to give up time freely to support the regulatory system; consequently, the cost of information for the formulation and interpretation of quality standards might rise.

- 4.25. Without the expertise of the professions, there would be a greater risk of the regulatory framework being set up inappropriately, to the detriment of consumers and the professions. Furthermore, the removal of regulatory functions from the professions might lessen the feeling of responsibility professionals have for the quality standards of their professions and would thus increase monitoring and enforcement costs.
- 4.26. Although the LSA would be independent from Government and fully funded by the professions, the fact that all regulatory powers would be vested in it might increase scepticism about the independence of the legal professions from outside influence. It has been argued that the resulting detrimental effect on confidence in the UK legal professions might deter foreign consumers of legal services from using the UK (and London in particular) as a centre for international and commercial litigation and arbitration. Figures show that up to 4,000 international disputes a year are dealt with in London, and more than 90% of disputes handled by international law firms in London involve at least one foreign party with the amounts in dispute totalling over US \$40 billion in 2002.<sup>25</sup>
- 4.27. Using the information provided by the professional bodies, the operating cost for the LSA, including disciplinary functions was estimated in PwC's Final Report<sup>26</sup> to be £66.4 million annually. This represents a total estimated net additional annual ongoing cost of £1.5 million greater than the current cost of separate legal regulation (i.e. the "Do Nothing" option).
- 4.28. Using broad assumptions, the PwC report estimates that the transition costs associated with the establishment of the LSA represent £55.3 million, spread over three years either side of the LSA inheriting its powers and duties.

<b>Option</b>	<b>Annual Running Costs</b>	<b>Transition Costs (two years before vesting)</b>	<b>Transition Costs (one year before vesting)</b>	<b>Transition costs (one year after vesting)</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Do nothing</b>	64,900	n/a	n/a	n/a
<b>With Legal Services Authority</b>	66,400	11,550	16,740	27,000

*Costs in 2005-06 prices.*

#### Social costs

- 4.29. Aside from the social costs referred to under the economic costs section there would be no additional social costs arising from this option.

### **Option 3 - An oversight regulator**

#### ***Benefits***

#### Economic benefits

- 4.30. By providing a single point of consistent oversight regulation, the establishment of the LSB

<sup>25</sup> International Financial Services London, (March 2005), *Legal Services: City Business Series*. *op. cit*

<sup>26</sup> PwC's independent report is published on DCA's website and can be found at: <http://www.dca.gov.uk/legalsys/lrreform.htm>

would lead to a reduction of inconsistencies in the current regulatory framework in the form of regulatory proliferation, confusion, fragmentation and anomalies for the legal sector. The process of altering professional rules as a response to changes in market condition would also be streamlined. This should result in a reduction in regulatory burden for existing suppliers and an increase in efficiency. Consequently, new entrants would be attracted to the legal services market, increasing competition and driving innovation within the sector.

- 4.31. The flexibility of the system would allow the LSB to authorise new and current ARs to regulate their members in the provision of a range of existing legal services and newly reserved areas of legal services, and would also help facilitate Alternative Business Structures (ABS) and consequently encourage competition and innovation in the market.
- 4.32. In addition, this flexibility should also increase competition for the regulation of the ABS firms, leading to efficiency drives among the ABS regulators and reducing regulatory burdens for ABS firms. Moreover, this flexibility should ensure that consumers were appropriately protected, especially with the legal services market developing rapidly and new forms of legal services emerging.
- 4.33. The LSB would have a statutory objective to protect and promote consumer interest, promote competition in the provision of legal services and encourage an independent, strong, diverse and effective legal profession. The objectives will ensure that regulation is applied in a manner that is ultimately beneficial to consumers.
- 4.34. A regulatory framework that gave responsibility for the regulatory functions to ARs with an LSB providing consistent oversight would mean that the expert knowledge of the legal professions in setting entry standards and training, formulating professional rules, monitoring compliance and enforcing the necessary codes of conduct would be retained. The risk of losing regulatory expertise during any transitional period should also be reduced. Leaving the day-to-day regulations as far as possible to the ARs would also be more likely to increase the commitment of suppliers to high standards, reducing the risk of rising monitoring and enforcement costs.
- 4.35. The duty of the LSB to consult with the Office of Fair Trading (OFT) when authorising new ARs, or adding to or removing from the list of reserved legal services, will ensure that competition issues are fully considered by the LSB and OFT. In addition, the LSB would be under a duty to respond to any competition issues that the OFT brought to its attention. This would reduce the risk of competition being stifled by anti-competitive practices, maintaining the benefits of innovation and diversity within the market.

#### Social benefits

- 4.36. If the oversight body was not created and the professional regulatory bodies were only required to separate their regulatory and representative functions, as the Law Society has suggested, there would still remain a number of deficiencies in the regulatory framework which these arrangements would not address. More specifically, the LSB would eliminate the inconsistencies in the existing regulatory framework and, by acting as an independent oversight regulator, would be able to identify best practices to meet the objectives of reforming the regulatory framework.
- 4.37. Through the creation of an oversight regulator, the regulatory framework would provide consumers with better protection. This is because an oversight body would monitor the legal services sector and ensure that regulatory gaps were identified and tackled before consumers were put at risk. The LSB would be responsible for authorising and regulating the ABS regulators who would license businesses to provide legal and non-legal services to consumers. We expect that ABS would encourage competition and innovation in the provision of legal services.

- 4.38. The separation of the regulatory and representative functions of the professional bodies would not on its own contribute to increasing consumer confidence. The LSB would be independent from the Government and the profession, and would therefore focus on promoting consumer interests and its statutory objectives. Such a system would help to increase consumer confidence in the system and improve the professional standing of providers.
- 4.39. Once the LSB has been established and its powers brought into effect, it will set out criteria which the ARs will need to meet when separating their regulatory and representative functions. If the ARs fail to meet these criteria then the LSB has the power of direction to intervene in order to correct failures.
- 4.40. The LSB would be a smaller, less bureaucratic and more efficient organisation than the LSA model. As such it would have a greater ability to adjust flexibly to future changes in the legal services market, and to make the appropriate regulatory response. This should aid future development in the market, in particular the possible expansion of the role of ABS firms in the provision of legal services. Further, this could also bring positive benefits in terms of increasing access to justice, especially to the most vulnerable sections of society, such as those consumers restricted in their geographical access to legal services and those with special needs. In addition, the LSB will be under a statutory duty to improve access to justice.
- 4.41. In accordance with the objectives of the new regulatory framework, the LSB will operate openly and transparently so that consumers could understand its decisions and hold it to account. The LSB would consult with consumers and would establish and maintain a Consumer Panel, further demonstrating its dedication to consumer interests. We expect that this feature of the LSB would instil greater confidence in consumers.
- 4.42. The clear separation of regulatory and representative functions, which the LSB would require ARs to have in place, in conjunction with an oversight regulator, would lead to greater accountability, transparency and regulatory certainty. Consumers can be assured that the people who are regulating and disciplining regulated persons are not the same people who represent the interests of the legal profession. The LSB's retention of the right to carry out regulatory functions directly, should an AR fail, would provide an incentive for ARs to regulate their professions with consideration for consumers' interests and consistent with the LSB's objectives.
- 4.43. Under the LSB option, the front-line regulatory powers would be exercised at AR level, subject to regulatory competencies and governance arrangements. The fact that day-to-day regulatory functions would be performed by ARs themselves would support the principle that the legal profession should be independent of Government, and would demonstrate it more clearly than the LSA model. This should mitigate any potential impact on UK legal services' international standing. In particular, this should reduce the risk of withdrawal of foreign purchasers and supplier of legal services from the UK legal services market, and the likelihood of English lawyers being prohibited from carrying out legal work within foreign jurisdictions post-reform, compared to the LSA option.

## *Costs*

### Economic costs

- 4.44. Under the LSB option, the legal professions would be subject to regulations set by the approved regulators. These regulations, and other regulatory arrangements, would require the approval of the LSB before coming into force. In addition, if, in the future, the LSB decided to widen the regulatory net to include previously unregulated professions, then regulatory costs associated with the new area would fall on practitioners in those professions. Although there is a risk that these costs could be passed onto consumers, this should be minimal, as increased competition among suppliers would provide an incentive for suppliers to identify cost-saving strategies to keep prices relatively low.

- 4.45. The LSB's ability to adapt to changes in the legal services market (including the possibility to widen its regulatory net) would not be without significant benefits. Oversight regulation conducted by the LSB would drive efficiency in the market while protecting consumer interests. The result of this would be a consistent level of high-quality provision across all professions within legal services.
- 4.46. ARs might use their knowledge of the current market conditions of the legal services' market to formulate regulations that put the interests of the professions above those of consumers. However, there would be safeguards to substantially reduce the incentives of bodies to set regulations in a way that harmed consumers. These would include the ability of the LSB to impose financial penalties on approved regulators. This should serve to deter ARs from acting in a manner contrary to the regulatory objectives of the LSB. In addition, the LSB also has the power to approve rules, to direct that rules be called in or amended, and to impose sanctions, with de-authorisation of the AR as a last resort.
- 4.47. In using these safeguards, the LSB would be required to act proportionately, exercising its powers consistently with the need to ensure effective regulation.
- 4.48. In their independent report on the costs of the Government's proposed arrangements,<sup>27</sup> PwC identified the ongoing annual running costs of the regulatory system (including disciplinary costs) under the LSB model to be around £67.3 million. The key driver for the difference in costs compared to the 'do nothing' option (which is estimated to cost £64.9 million) is the additional annual running costs of a Legal Services Board, estimated at £3.6 million (as per PwC's base-case scenario).
- 4.49. This represents a total estimated net additional annual cost of £2.4 million greater than the current costs of separate legal regulation (i.e. the "Do Nothing" option).
- 4.50. The cost of the LSB option would also be around £900,000 per year more than the LSA. Despite the much lower annual running costs of the LSB oversight regulator (£3.6 million as an 'oversight' regulator against £66.4 million for the LSA as 'sole' regulator), PwC estimated that under the LSB option, £63.6 million of the costs will remain with approved regulators. This is because the powers and duties of day-to-day regulation would be delegated down from the LSB and therefore the ARs will continue to incur costs (e.g. staff and accommodation costs) in largely the same way as they do under the current system.
- 4.51. The Government is content that the small increase in regulatory costs can be justified by the potential benefits accruing to consumers and the legal service sector as a whole from the introduction of an oversight regulator (as discussed above). This increase in regulatory costs should be seen in conjunction with the decrease in costs attributable to bodies involved in the regulatory framework from the creation of a single, independent complaints handling body (see 6.34 onwards).
- 4.52. PwC's base case cost was estimated on the assumption that the LSB would have a 39 core staff members, with a 9-member board and a 10-person Consumer Panel in an out-of-London location. The estimate assumed that the underlying nature of the regulatory activities, within the remit of the LSB's framework, would not be substantially different from those performed under the current regulatory framework.
- 4.53. The main driver for the LSB's estimated annual running cost of £3.6 million is direct staff costs of £1.9 million.
- 4.54. PwC estimated transitional costs of £2.3 million for the LSB, which would be spread over approximately three years either side of vesting powers in the new oversight regulator. The largest transition cost of £900,000 related to new premises costs (rent, rates and insurance).

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<sup>27</sup> PwC's independent report is published on DCA's website and can be found at: <http://www.dca.gov.uk/legalsys/lreform.htm>



The majority of transition costs (£1.6 million) would fall in the year before vesting powers in the LSB.

<b>Option</b>	<b>Annual Running Costs</b>	<b>Transition Costs (two years before vesting)</b>	<b>Transition Costs (one year before vesting)</b>	<b>Transition costs (one year after vesting)</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Do nothing</b>	64,900	n/a	n/a	n/a
<b>With a Legal Services Authority</b>	66,400	11,550	16,740	27,000
<b>With a Legal Services Board</b>	67,250	200	1,580	500

*Costs in 2005-06 prices.*

- 4.55. PwC's report also identified £1 million of additional "implementation costs" from setting up a task force for detailed organisation design for the LSB and an independent complaints handling body (i.e. the OLC). These costs were estimated to fall in the year before powers and duties would be vested in the new bodies.
- 4.56. PwC also costed alternative scenarios over and above their base case. This included costing for an incremental increase in the level of activity and locating the LSB in the North of England or London. A combination of these variables could result in the annual ongoing running costs of the LSB rising to £5.6 million (base-case plus incremental level of activity and located in London). Under this alternative scenario, transition costs could also rise by approximately £600,000.

#### Social costs

- 4.57. An over-arching regulatory body could dilute personal ethical responsibilities and regulatory accountability of individual solicitors. The removal of self-regulation could also de-moralise legal practitioners increasing the risk of lowering quality standards to the detriment of consumer interests. However, through the ARs retaining the responsibility for ethical and regulatory accountability, this should be prevented.

## 6. Reforming the Complaints Handling Arrangements in Legal Services

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- 6.1. The aim of this proposal is to simplify and improve the current arrangements in the way that consumer complaints are handled. The proposals should lead to a more accountable and transparent complaints handling system, and should improve consumer confidence in the complaints handling system.

- 6.2. The following options on reforming the complaints handling arrangements in legal services have been considered:

### **Option 1 – Do nothing**

- 6.3. The current structure to deal with complaints and disciplinary matters in the legal services market would be retained. This would mean leaving all consumer complaints with the professional bodies subject to differing levels of oversight and accountability by various bodies. Possible acts of misconduct would continue to be handled by the disciplinary procedures of the professional bodies. Tribunals that are independent of, but are funded by, the professional bodies would continue to hear cases of possible misconduct. This option would not attract any additional costs or create any additional burdens. However, there is a risk that the proliferation, fragmentation and overlap featured in the current complaints handling arrangements would remain. In addition, complaints handling by certain professional bodies would likely remain complicated and unsatisfactory, and the independence of the complaint system would continue to be questioned, undermining consumer confidence in the legal services market.

### **Option 2 – A single point of entry for all complaints against legal practitioners (the ‘post-box’ option)**

- 6.4. Under this option, a single point of entry for all consumer complaints would be established for complaints that remained unresolved at the ‘in-house’ level. Complaints would be sifted into different categories or type of complaints and would then be passed down to the ARs to deal with them. This point of entry would essentially be a ‘post-box’ for all complaints and the complaints handling system would remain in the control of the legal profession.

### **Option 3 – A new complaint handling body**

- 6.5. Under this option, the **Office for Legal Complaints (OLC)** would take over the role of the ARs in handling consumer complaints. The OLC would be a single body, completely independent from the ARs. The Office of the Legal Services Ombudsman and the Office of the Legal Services Complaints Commissioner would be abolished.
- 6.6. The OLC would form part of the new regulatory framework including the LSB and would be accountable to the LSB for its overall operation. This would ensure that the LSB had proper oversight of the entire regulated legal services sector. However, the LSB would have no authority to examine individual complaints.
- 6.7. Legal service providers would be required to maintain ‘in-house’ complaints handling procedures, which would have to satisfy any requirements set by the LSB, to deal with complaints made by consumers in the first instance. The OLC would handle all complaints made against the providers that could not be resolved at the local level. These complaints would be passed directly to the OLC. The OLC would refer potential issues of misconduct to ARs. It would be able to require an AR to inform it of the action the AR took on conduct matters.
- 6.8. In addition, the OLC would be empowered to provide redress to consumers where appropriate, up to a limit of £20,000. It could also refer complaints to other statutory regulators or their redress bodies. The existing disciplinary arrangements with regard to misconduct would be largely unchanged and would continue to be handled by the disciplinary procedures of the ARs, although there would be LSB oversight.
- 6.9. This is the Government’s preferred option on reforming the complaints handling arrangements in legal services. The OLC would be independent of the legal profession, which would help to improve consumer confidence in the legal services market, and should aid the regulatory framework in achieving its objectives. The OLC would provide a single

system with one point of entry for all consumer complaints, making the system simpler for consumers and helping to accommodate alternative business structures. In addition, the fact that the OLC would have powers to deal directly with complaints, as well as having the ability to provide redress of up to £20,000, would provide legal services providers with an incentive to act in an ethical and accountable manner to avoid complaints being lodged against them and also to provide consumers with adequate compensation, where necessary.

## **The Benefits and Costs of reforming the Complaints-handling arrangements for Legal Services**

### **Option 1 – Do nothing**

#### ***Benefits***

6.10. There would be no additional economic or social benefits arising from this option.

#### ***Costs***

6.11. There would be no additional economic or social costs arising from this option. However, there is a risk that the proliferation, fragmentation and overlap featured in the current complaints handling arrangements would remain. In addition, complaint handling by certain professional bodies might remain unsatisfactory, and the independence of the complaint system would continue to be questioned, undermining consumer confidence in the legal services market.

6.12. There would be no additional policy costs arising from this option. Using information provided by the legal professional bodies, PwC, in their independent report on the regulatory reform of legal services<sup>55</sup>, estimated that the total regulatory cost in 2005-06 was £97.4 million. Of this, £32.5 million related to complaints handling.

6.13. The Law Society's costs represent a substantial proportion of this total at approximately 88%.

### **Option 2 – A single point of entry for all complaints against legal practitioners (the 'post box' option)**

#### ***Benefits***

##### **Economic benefits**

6.14. This option would provide a single system with one point of entry for all consumer complaints, making the system simpler for consumers to use. This would also minimise the inefficiencies caused by consumer complaints being directed to the incorrect regulator.

##### **Social benefits**

6.15. The simplification of the complaints handling system would increase public understanding of the system and therefore encourage those consumers who had a valid reason to complain, to do so. This might help to restore some consumer confidence in the complaints handling system.

#### ***Costs***

##### **Economic costs**

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<sup>55</sup> PwC's independent report is published on DCA's website and can be found at: <http://www.dca.gov.uk/legalsys/lreform.htm>

6.16. A body with a ‘post-box’ role for consumer complaints would put an additional operational cost burden on suppliers, through the cost of creating and running the new body. This burden would probably be transferred to consumers, leading to higher prices. The fact that this body would have no power to deal with the substance of complaints would mean that the higher prices consumers would be paying would bring virtually no additional benefit to the complaints handling process.

Social costs

6.17. Under this ‘post-box’ complaints system, substantive complaints handling functions including adjudication would remain in the control of the legal profession, so there would continue to be some concerns over the system’s independence. This option might fail to improve consumer confidence in the legal services industry and would fail to aid the regulatory framework in meeting its objectives such as protecting and promoting consumers’ interests.

6.18. As the ‘post-box’ complaint office would be unable to award redress, there would be less incentive for suppliers to improve service quality. This complaint office will essentially act as a ‘complaints distribution centre’.

6.19. Using the information provided by the legal professional bodies, the operating cost for the ‘post-box’ option, were estimated in PwC’s final report to be £32.9 million annually.<sup>56</sup> This represents a total estimated net annual cost of £400,000 more than the current costs for complaints handling (i.e. the “Do Nothing” option).

6.20. Using broad assumptions, the PwC report estimated that the transition costs associated with the establishment of the ‘post-box’ option were £500,000, spread over one year.

6.21. The relatively small increase in costs under the ‘post-box’ option reflects the small change in the way complaints handling is arranged under this option.

<b>Option</b>	<b>Annual Running Costs</b>	<b>Transition Costs (two years before vesting)</b>	<b>Transition Costs (one year before vesting)</b>	<b>Transition costs (one year after vesting)</b>
	<b>£’000</b>	<b>£’000</b>	<b>£’000</b>	<b>£’000</b>
<b>Do nothing</b>	32,520	n/a	n/a	n/a
<b>Postbox</b>	32,920	-	-	500

*Costs in 2005-06 prices.*

**Option 3 – A new complaint handling body**

***Benefits***

Economic benefits

6.22. A single complaint body would bring greater consistency and clarity to the complaints handling process. With one point of entry for all consumer complaints, the system would be simpler and would also help to accommodate Alternative Business Structures (ABS) by

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<sup>56</sup> *ibid*

identifying the most efficient route for resolution when the complaint had not been successfully resolved via 'in-house' procedures. The clearer channels for complaints handling would lead to a more efficient and effective complaint mechanism. Coupled with potential scope for economies of scale, through the amalgamation of several systems into one, this should lead to time and overhead savings for ARs and suppliers of legal services.

- 6.23. The ability of the OLC to award redress of up to £20,000 in a manner that was fair and consistent to both consumers and providers should give consumers with valid reasons to complain an incentive to do so. Such a redress mechanism would have a further benefit to the profession to the extent that consumers would have more confidence in purchasing legal services. The ability of the OLC to award redress should also provide suppliers with an incentive to act in an ethical and accountable manner, and overall, improve the service quality of legal services.
- 6.24. The OLC would be funded in part by means of a general levy on all authorised bodies and in part through case fees (the 'polluter-pays' principle). The case fee would provide an incentive for providers to resolve complaints through in-house arrangements, to avoid the cost of the complaint reaching the OLC. However, it seems only fair that the OLC should have the ability to waive all or part of the case fee in circumstances where it considered that the legal service provider had made considerable efforts to resolve a complaint in house, and/or where it considers that a consumer had acted unreasonably. This would ensure that providers who took all reasonable steps to resolve complaints through their in-house systems would not be penalised unnecessarily.

#### Social benefits

- 6.25. A complaint system that was independent of the legal profession will improve consumer confidence in the legal services industry. Consequently, consumers with valid reasons to complain should be more confident and inclined to do so, encouraging suppliers to improve the quality of their legal services and therefore reduce the number of complaints lodged against them.
- 6.26. The powers that the OLC would have to share information about complaints with consumers could empower consumers to make better-informed decisions about choosing their legal service provider thus improving consumer confidence in the legal services market. They would be confident that complaints would be dealt with transparently and independently. Such information would help consumers make better-informed decisions about purchasing legal services, helping to address the existing information asymmetries in the market and improve standards of quality and eventually, through increased competitiveness, reduce prices and improve access to justice.
- 6.27. Through establishing an independent and impartial complaint system, the OLC would provide a clear forum for dealing with complaints in a way that was consistent with the objectives of legal services reform. This would mainly involve protecting and promoting consumer interests; providing an incentive for individual practitioners to meet appropriate quality standards; and increasing public understanding of citizens' legal rights.
- 6.28. By leaving ARs with the power to discipline their own members, the reform of complaints handling arrangements would recognise that consumers are far more content with this aspect of their performance to date.

#### *Costs*

##### Economic costs

- 6.29. Increased consumer confidence in the complaint handling system, simplification of the complaint procedures, an increase in the redress amount and the greater transparency of the

disciplinary systems, could when taken together, lead to a rise in complaints, both genuine and spurious ones. The potential increase in complaint cases could increase the workload for suppliers of substandard legal services, as the OLC would now be more likely to follow-up a higher proportion of the complaints received. However, this cost has to be balanced by the fact that firms required by the OLC to compensate for poor service would have further incentives to improve the quality of their services, leading to fewer complaints being lodged against them. This would help reduce the likelihood of the cost involved in handling complaints being incurred in the first place.

- 6.30. Since the OLC should be more effective in handling complaints, there could be an increase in the numbers of legitimate complaints made, so it is more likely that suppliers who provide poor quality services would be complained against to the OLC. Consequently, the compliance costs for these suppliers would rise, for example in the form of paying financial redresses or extra investment in their 'in-house' complaints handling facilities. However, this risk should act as incentives for these suppliers to raise the quality of their services, or to improve their complaints handling facilities so that complaints can be satisfactorily resolved in-house, to the benefit of consumers.
- 6.31. It has been suggested that the introduction of the OLC might make legal professionals overly cautious, so that they might seek to avoid taking on more complex or 'difficult' cases, and could leave them more susceptible to complaints, thus incurring extra costs. This might lead to some suppliers withdrawing from some types of work, reducing competition, or worse still, abandoning them all together. As a result, consumers might be unable to find a supplier who was willing to provide them with the services they needed. However, this risk would be reduced by the proposal that the amount of redress the OLC can award would be limited to £20,000 and that it will have the power to waive fees for spurious complaints. Further, the risk of legal providers taking an overly cautious approach already exists under the current system and there is no empirical evidence that it has driven some lawyers to avoid these cases. The 'cab-rank' principle<sup>57</sup> also ensures that some lawyers are not allowed to select their clients by personal preference.
- 6.32. The cost of generating more complaints might not necessarily result in additional cost to particular sectors of the legal services market. In working out its funding mechanism, the OLC would consult with the profession to ensure that the costs of complaints handling were divided fairly. It would be open to the OLC, for example, to ensure that the cost per complaint was lower in areas where providers were inherently more likely to generate complaints. For example, criminal barristers generate high levels of complaints because their clients often view it as another quasi-appeal route; but these complaints are not especially likely to be upheld. The OLC would consult on its annual budget, and as it would be bound by the regulatory objectives, it would want to take steps to mitigate any risk that providers would shy away from particular areas of the law.
- 6.33. In their report on the costs of the Government's proposed arrangements, PwC identified the ongoing annual running cost of complaints handling system under the OLC option to be around £20.6 million.<sup>58</sup> This figure comprises £16.8 million for the OLC's running costs and approximately £3.8 million in unavoidable overhead costs currently allocated to regulators' complaints handling functions.
- 6.34. The key driver for the difference in cost compared to the 'do nothing' option (which costs £32.5 million) is the savings made against annual running costs from the rationalisation of the complaints handling system, which are estimated at £28.7 million, and the ongoing annual running costs of the new OLC, estimated at £16.8 million (for their base-case scenario).

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<sup>57</sup> The "cab rank" rule dictates that every member of the Bar is obliged, without fear or favour, to represent clients who offer themselves, regardless of how unpopular they may be in the community or elsewhere.

<sup>58</sup> PwC's independent report is published on DCA's website and can be found at: <http://www.dca.gov.uk/legalsys/lreform.htm>

- 6.35. This represents a total estimated net annual cost of £12 million less than the current costs of separate complaints handling (i.e. the “Do Nothing” option).
- 6.36. The OLC would also be around £12.3 million per year cheaper than the post-box option. This is because, under the ‘post-box’ option, complaints handling would continue to be done by the individual regulators, and thus would not benefit from the rationalisation of the current complaints handling framework.
- 6.37. This base case cost was estimated on the assumption that the OLC would have a core staff of 319 staff, with a 7-member board, based in the West Midlands. The estimate assumed that the underlying nature and volume of complaints under the new OLC would not be substantially different from those received under the current regulatory framework.
- 6.38. PwC estimated one-off transition costs of £23.6 million for the OLC, which would be spread over approximately two years either side of vesting powers and duties in the new single complaints body. The Government is satisfied that these costs would be justified by the benefits of a single, independent complaints-handling body as outlined above. Furthermore, these one-off transition costs should be seen in the context of the estimated £12 million annual decrease in operating costs under the OLC option.

<b>Option</b>	<b>Annual Running Costs</b>	<b>Transition Costs (two years before vesting)</b>	<b>Transition Costs (one year before vesting)</b>	<b>Transition costs (one year after vesting)</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Do nothing</b>	32,520	n/a	n/a	N/a
<b>Postbox</b>	32,920	-	-	500
<b>With an Office for Legal Complaints</b>	20,590	140	12,280	11,140

*Costs in 2005-06 prices.*

- 6.39. PwC's report also identified £1 million of additional "implementation costs" for setting up a task force for detailed organisation design for the OLC and an oversight regulator (i.e. the LSB). These costs were expected to fall in the year before powers and duties are vested in the new bodies.
- 6.40. PwC also estimated costs under alternative scenarios over their base case. This included costing for an incremental increase in resources required to accommodate an increase in the volume of complaints handled by the OLC. PwC considered an increase of 25%. Under PwC's analysis the annual ongoing running costs of the OLC operating at this incremental level of activity could rise by approximately £4.2 million to £21.0 million (base-case plus incremental level of activity, for a single-site option located in the West Midlands).
- 6.41. Under this alternative scenario, transition costs could also rise by approximately between £3.5 million and £6.6 million (dependent on the nature of the increase in complaints) to between £27.1 million and £30.1 million.
- 6.42. PwC considered the prospect of an increase in the level of complaints handling post-establishment of the OLC. By way of example they identified a number of possible scenarios. It is difficult to predict the potential increase in complaints, although one figure of 25%, which PwC identified, appears from our own review to be broadly in the range experienced in some other sectors.<sup>59</sup> However, the circumstances in those sectors are very different to those in the legal sector and the Government considers it difficult to make any meaningful assessment about any potential increase in complaints handling as a result of the establishment of the OLC on the basis of data currently available.
- 6.43. One important factor, which is not evident in the majority of comparative bodies, is the potential for the OLC to levy a case handling fee in respect of any complaint it receives. We consider this should act as a strong incentive to reduce the prospect of considerably higher levels of complaints being made to the OLC. Further, approved regulators will be charged by the LSB with ensuring the persons they regulate have appropriate and effective in-house complaints handling arrangements in place and the LSB will take regulatory action against them should this not be the case.

<sup>59</sup> Other sectors reviewed include: finance, energy, postal services and the communications industries; their regulatory bodies are Financial Ombudsman Service (FOS), Energywatch, Postwatch and Ofcom, respectively.



- 6.44. Any increase in other sectors have generally occurred some two to three years after establishment of the new complaints handling bodies, and if this did prove to be the case in terms of legal services complaints such a delay would enable the OLC take a flexible approach to the structuring of its organisation and processes in order to absorb any such impact. Data from other complaints handling bodies consistently show decreasing unit costs with increasing complaint volumes possibly due to a combination of parallel reforms regarding processes, organisational design and operational structures. It is also possible that any increases in complaints handling could either be absorbed within the efficiencies which PwC consider the new arrangements will provide, or by fine tuning the fees that may be levied by the OLC under the "polluter pays" regime.
- 6.45. The Government commissioned PwC to provide independent financial analysis to support the draft Legal Services Bill. In order to do this PwC needed to make a number of assumptions on the potential structure and operational capacity of the new bodies. PwC consulted with approved regulators, officials at the DCA and other interested parties, but it is important to emphasise that the assumptions made in their final report are those of PwC and not the Government.<sup>60</sup>
- 6.46. One aspect of PwC's report that has attracted a number of concerns relates to the potential for efficiency savings resulting from the establishment of the OLC when compared to the cost of operating the existing array of individual schemes. In this context, the Joint Committee on the Draft Legal Services Bill commented that:

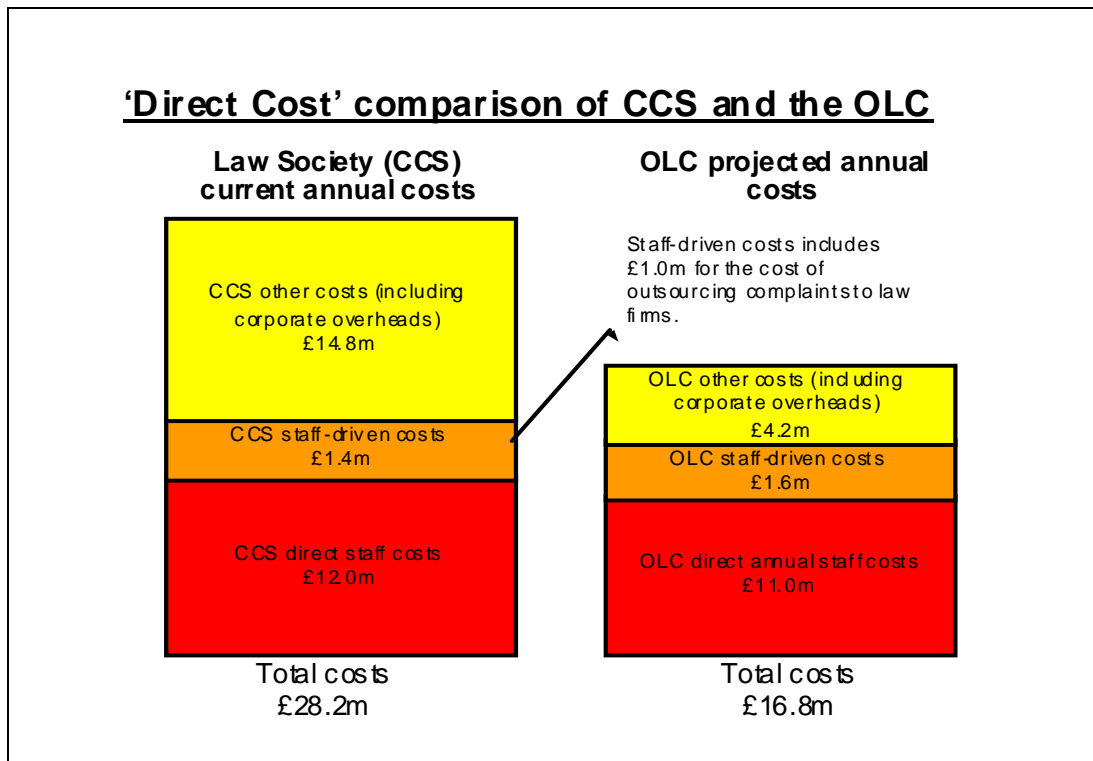
*It is unclear to us how PwC move from the assumption of 15% efficiency savings, to estimating a running cost of almost 40% lower than current costs ...*<sup>61</sup>

The key issue here is that the 15% efficiency savings that PwC estimated were only one of a number of assumptions that contributed to the overall cost reduction of 40% in moving from the existing complaints handling service operated by the Law Society to that operated by the OLC.

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<sup>60</sup> To view the PwC Report see - [http://www.dca.gov.uk/legalsys/pwc\\_finanalysis\\_060524.pdf](http://www.dca.gov.uk/legalsys/pwc_finanalysis_060524.pdf)

<sup>61</sup> Joint Committee on the Draft legal Services Bill, Session 2005-06, Volume 1 Report, HC 1154-1, HL Paper 232-I



*\*Note - the OLC will not have to bear overheads of some £3.8million currently applied to the CCS. Approved regulators will either continue to bear these costs or seek to reorganise their operations to reduce these costs.*

- 6.47. It is clear from the above table that the estimated 40% savings were made up of a number of individual elements. In respect of the efficiency savings in particular, PwC took the view that it was reasonable for a new organisation with a clear consumer focus for the delivery of quick and fair redress, and with modern operating systems and processes, to be able to realise a 15% efficiency gain over the Law Society's current case-handling arrangements. As well as this 15% efficiency gain, PwC also assumed that there would be a reduction in the overhead costs which are currently levied on the CCS by the Law Society, costs towards the OLSCC and general administrative costs borne by the CCS. In reaching their assumption, PwC were further influenced by research conducted by Experian in January 2004 for the Lyons Review into the effect that public sector relocation can have on embracing different working methods and technologies.<sup>62</sup>
- 6.48. A complaint that involved legal and non-legal professions in the ABS firm could lead to confusion among ARs, the OLC and the regulatory bodies of the non-legal professions as to how it should be handled. Any lack of consistency among legal and non-legal handling bodies could lead to increases in the operational and compliance costs of ABS firms. However, licensing authorities would be required to have suitable and transparent arrangements with non-legal regulators in place before being authorised to allow license ABS firms.
- 6.49. Confusion could also arise for consumers if their complaints were passed from the OLC to a non-legal complaints handling body. However, this confusion would be mitigated by ABS firms making it clear at the outset that different regulators have regard to different services provided by the firm. By having the authority to enter into discussions with other statutory regulators, the LSB would have the opportunity to

<sup>62</sup> For more information see: <http://www.hm-treasury.gov.uk/media/98E/EB/ExperianResearch.pdf#search=%22Experian%3A%20%E2%80%98The%20Impact%20of%20Relocation%E2%80%99%20January%202004%22>

ensure that the handling of the complaint would be consistent across the professions involved.

## 9. Diversity Impact Assessment

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- 9.13. Under the Government's preferred option, the LSB will act as an oversight regulator, delegating day-to-day functions to ARs. The LSB will be under a duty to act in a manner consistent with the regulatory objectives, including 'encouraging a strong, effective and diverse legal profession'. A similar duty will also apply to ARs. This will include a duty to publish policy statements on how the statutory objectives are being achieved, on which the LSB will be able to issue guidance if necessary.
- 9.14. If ARs were found to be acting inconsistently with the regulatory objectives, the LSB will also have effective enforcement powers and will be able to set sanctions, for instance the power to direct the failing AR. This system will ensure that ARs will be free to use their expertise to fulfil the objectives in the most efficient way, but also enables the LSB to intervene when the interests of consumers and disadvantaged groups are compromised.<sup>86</sup>

## 12. Implementation, Delivery Plan and Post-Implementation Review

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- 12.1. Implementation of the proposals in the Legal Services Bill will be managed by the Department for Constitutional Affairs (DCA) working in consultation with stakeholders. The DCA considers the input of stakeholders to be key to the successful delivery of the reforms and is committed to a consultative approach to working throughout the implementation process.
- 12.2. To ensure that implementation is taken forward in a structured manner, which enables progress to be carefully monitored, programme management will be used in line with principles of best practice. This will provide for continual assurance of the implementation and planning process including benefits realisation, management of risk and stakeholder engagement.
- 12.3. Consultation with other Government departments and organisations with experience in managing comparable or similar implementation programmes will be factored into the delivery plan as will benchmarking exercises to identify best practice in regulation and complaints handling.

### **Implementation period**

- 12.4. Engagement with stakeholders is already ongoing. This will continue throughout the passage of the Bill and beyond.
- 12.5. Planning for implementation and preliminary work is in hand. Full-scale implementation will begin once the Bill has received Royal Assent, in line with Government Accounting rules. After further work to refine implementation plans, our expectation is that, following Royal

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<sup>86</sup> Department for Constitutional Affairs – Nov 2005, "Increasing Diversity in the Legal Profession: A report on Government proposals", [http://www.dca.gov.uk/legalsys/diversity\\_in\\_legal\\_2col.pdf](http://www.dca.gov.uk/legalsys/diversity_in_legal_2col.pdf) reported that there were a number of factors preventing women and ethnic minority groups from succeeding in legal careers. The Panel recommended that the LSB should be properly resourced to conduct or commission its own research into issues such as racial equality and diversity, and in addition to be able to facilitate future monitoring or diversity within the professions

Assent, implementation will take a minimum of two years. This timetable incorporates implementation of supporting secondary legislation.

***Funding of transition costs and effect on the profession***

- 12.6. The Government's position is that the reforms it is introducing are needed to correct failures in the existing system, particularly in terms of more effective and independent complaints handling arrangements and greater competition. These changes are essential to ensure that the market for legal services operates more effectively and in the consumer interest. The changes will of course mean there will be additional costs in establishing the new machinery. There have been calls from many for the Government to make a contribution to these costs. While this could be achieved through an increase in general taxation, the Government considers the more appropriate arrangement would be for those being regulated to bear these costs. The Legal Services Bill therefore includes provision for the Legal Services Board to make a levy on the profession to fund the cost of establishing and running the new arrangements.
- 12.7. In their report of May 2006, PwC estimated the total transition costs (for LSB and OLC) to be some £26.8 million.<sup>92</sup> It has been argued that it is unreasonable to expect the professions to bear the full cost of these transitional arrangements. However, it is important to set these into the context of the overall value of the legal sector. For example, in 2003 the sector achieved an annual turnover of some £19 billion. In their associated report of June 2006 on compensation fund arrangements, PwC identified that some 144,000 members were subject to regulation by the seven bodies that are identified in the Legal Services Bill as approved regulators<sup>93</sup>, so at the most basic level, we could conclude that each regulated person is responsible for generating a turnover of around £132,000 year.
- 12.8. It will be for the LSB to apportion costs on a fair and proportionate basis between approved regulators. And in turn it will be for approved regulators to pass on these costs, again on a fair and proportionate basis, to those they regulate. As per the PwC report, total transition costs are £26.8 million. Of this, £11.0 million will fall directly on the Law Society, £8.0 million of which represent costs currently incurred by the Law Society (parallel running of CCS at Holborn and avoidable overheads). At the most basic level, and assuming that every member regulated by the Law Society were to make the same contribution, with approximately 101,000 members, the additional one-off costs of approximately £3 million equates to a one-off cost of £28.56 per member for one year.
- 12.9. The LSB, in consultation with the Approved Regulators, will also agree how best to apportion the remaining £15.8m of transition costs on a fair and proportionate basis between the Approved Regulators. Again at the most basic level, these transition costs, which PwC identified as directly associated with the establishment of the LSB and OLC, would represent a contribution of some £44 per person, per year, for two-and-a-half years for each member of a currently approved regulator (including members of the Law Society). This assumes that implementation takes place in accordance with year PwC's base-case scenarios and implementation timetable.

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<sup>92</sup> PwC's independent report is published on DCA's website and can be found at: <http://www.dca.gov.uk/legalsys/lreform.htm>

<sup>93</sup> The seven approved regulators are The Law Society, Bar Council, CLC, ILEX, CIPA, ITMA and CoF. 'Financial Analysis on Compensation Fund Options for the Legal Services Sector', PwC (June 2006). Available at: <http://www.dca.gov.uk/legalsys/lreform.htm>

## **Key milestones**

### Royal Assent

12.10. Subject to receiving Royal Assent, expenditure on implementation can begin in line with Government Accounting rules. The first task will be the appointment of the LSB and the OLC and their Chief Executives and senior managers. Our intention is to begin the recruitment process immediately following Royal Assent. Six to nine months is usually considered to be the lead-in time required to make an upper-tier appointment.

### Staff appointments

12.11. With the exception of the appointment of an interim Chief Executive of the OLC by the Secretary of State, staff appointments to both organisations will be made by the LSB and the OLC. We expect that staff appointments will take upwards of 4 months.

### Building acquisition and/or fit out

12.12. The expectation is that building acquisition and/ or fit out will begin in tandem, or shortly before, the staff appointments process and will also take between 6 to 12 months.

### Post-Implementation Review

12.13. At the point of Programme closure a review will be carried out to assess and evaluate the performance of the programme and its management processes to identify lessons that may help other programmes. The closure process will also be used to identify whether a further review, after closure of the programme, might be required to provide a complete assessment of the overall benefits realisation process.

12.14. This RIA will provide the baseline against which any post-implementation review will be measured.

12.15. The DCA will also seek to review the effectiveness of the reforms on a continual basis in its capacity as sponsoring department. The DCA will continue to work with stakeholders as part of this process.

12.16. Additionally, the proposed reforms have levels of accountability built in to ensure compliance with the legislation.

12.17. The **Legal Services Board** will be accountable to Parliament through the Secretary of State for Constitutional Affairs as sponsoring Minister. It will be required to present an annual report to the Secretary of State, who will lay it before Parliament and make it available publicly. The annual report will include the LSB's assessment of:

- the discharge of its functions,
- how it has met the regulatory objectives,
- its performance against standards of service delivery, and
- its statement of accounts.

12.18. The LSB will also have a duty to report to the Secretary of State at his request on any matter concerning the discharge of its duties.

12.19. Additionally, the Government expects that the Constitutional Affairs Select Committee will want to scrutinise the LSB's work by calling the Chair or other members to give evidence

under existing select committee powers.

- 12.20. The Chief Executive of the LSB will act as the accounting officer for the LSB. This will include responsibility for the propriety and regularity of finances, for keeping proper records, and for safeguarding assets. As accounting officer, the Chief Executive will be responsible to the Permanent Head of the Department for Constitutional Affairs as accounting officer of the sponsoring Department.
- 12.21. Although the OLC will be wholly independent in its handling of complaints, the OLC will remain accountable to the LSB in respect of its targets and funding. The LSB will be able to remove the chair of its board or board members in cases of poor performance or conduct, or of bringing the OLC into disrepute.

## 13. Summary and Conclusion

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### **Options preferred by the Government**

- 13.1. As a result of the cost-benefit analysis that the Government has carried out on the three options for reforming the regulatory framework for legal services, the Government has concluded that in order to simplify the current regulatory framework for legal services, the creation of an independent Legal Services Board (LSB) is the Government's preferred option.
- 13.2. The creation of the LSB will provide an independent, single point of oversight regulation to the legal service profession with effective powers to ensure that the day-to-day regulatory functions of the Approved Regulators (ARs) are in accordance with the overall objectives of the LSB, including improving access to justice, protecting and promoting consumers' interests, and encouraging a strong, effective and diverse legal profession.
- 13.3. The effective powers granted to the LSB will ensure that consumers' interests are put at the forefront of legal service provision, and transparency and accountability are achieved in the legal services market. The LSB will be responsible for authorising the ARs to conduct the day-to-day regulatory functions if it were satisfied with their competence and governance arrangements, and also that the ARs have demonstrated that they have satisfactorily separated their regulatory and representative functions.
- 13.4. The LSB will also have statutory powers to intervene if ARs are judged to be failing in their duties, which ensures that the incompetence of an AR will not persist to the detriment of consumers. In further demonstrating its commitment to protecting and promoting consumers' interests, the LSB will set up and maintain a Consumer Panel to ensure that it is in touch with the views and demands of different consumers.
- 13.5. The LSB will also be able to propose to the Secretary of State that additional legal service activities will be brought into, or taken out of, the scope of the LSB's regulatory reach by secondary legislation. This mechanism will ensure that the powers and functions of the LSB have the flexibility to adapt to potential future changes in the regulatory requirements of the legal services market.
- 13.6. As per the analysis conducted using PwC's independent report, the Government is confident that the slight increase in ongoing running costs (£2.4 million), and the one-off transition costs (£2.3 million) associated with the LSB option, are justified by the benefits accruing to consumers and the legal service sector as a whole, from the introduction of an oversight regulator. This increase in regulatory costs under the LSB option should be seen in conjunction with the decrease in annual running costs attributable to bodies involved in the regulatory framework from the creation of a single, independent complaints handling body

(£12 million).

- 13.7. As a result of the cost-benefit analysis that the Government has conducted on the three options proposed for facilitating alternative business structures, we have concluded that the option for facilitating full Alternative Business Structures (ABS) via a licensing regime is best suited to meeting the objectives of the reform for legal services.
- 13.8. The proposal will enable lawyers and providers of non-legal services to work together, with external financing, to provide services under a licensing regime. This will be subject to the approval of a licensing authority that has obtained an authorisation from the LSB to regulate that form of ABS. By permitting this form of business structure in the legal services profession, ABS will encourage competition, innovation and efficiency in service delivery while simultaneously improving the quality of legal services for consumers.
- 13.9. In order to assess the suitability of a prospective ABS firm, the licensing authority must be satisfied that the prospective ABS has attained the set standards. In particular, a prospective ABS firm will be required to satisfy the LSB's compensation fund and indemnity insurance requirements and to nominate a Head of Legal Practice (HOLP) and a Head of Finance and Administration (HOFA) to ensure that the conduct of legal business and practice management is in accordance with the regulatory rules.
- 13.10. External investors of the ABS firm will also have to pass a robust 'fitness to own' test set by the licensing authority before being permitted to invest in the firm.
- 13.11. The ABS option is much less restrictive than the LDP option we also considered, allowing firms to offer both legal and associated non-legal services. ABS firms that contain a mixture of lawyers and non-lawyers could lead to the sharing of good management practice, technological innovation and efficiencies across the market, enhancing competition among firms and potentially reducing the price of legal services. In addition, access to external finance will enable firms to spread start-up risks, access equity to possibly expand their business, diversify and improve the efficiency of their service provision to the benefit of consumers.
- 13.12. The Diversity Impact Assessment (including the Racial Equality Impact Assessment) revealed that the ABS proposals have the potential to have a positive effect on the BME consumers and solicitors through the expected reduction in prices and the changes in business structures. The Diversity Impact Assessment also indicated that female legal practitioners could also benefit from the increased opportunities that the ABS proposals could promote.
- 13.13. The Government expects the ABS proposals to have a positive effect on legal aid suppliers. The Legal Aid Impact Test has identified a number of areas where benefits will accrue to the legal aid consumer through an increase in the level of legal aid service provision and facilitation of complementary services provided through the integration of mixed service providers. In addition, through the potential reduction in prices, there could be an improvement in access to justice through affordability for the middle bracket of consumers.
- 13.14. The Government has carried out a Small Firms Impact Test and is satisfied that the proposed options will provide greater opportunities for small firms to access equity, diversify, expand and effectively compete in the market for legal services.
- 13.15. As a result of the cost benefit analysis that the Government has conducted on the three options proposed for reforming the complaints handling arrangements in legal services, we propose the establishment of a new Office for Legal Complaints (OLC) to take over the role of the professional bodies in handling consumer complaints. The OLC will provide an independent complaint handling system with effective powers to deal with complaints made against providers that cannot be resolved at the local level.

- 13.16. The OLC will also be empowered to provide redress to consumers, set standards for complaints handling and identify best practice.
- 13.17. Through the independence of the OLC, we envisage that consumer confidence in the complaints handling system will increase, which will encourage consumers to file legitimate complaints against inefficient providers.
- 13.18. The OLC will be accountable to the LSB for its overall operation, to ensure that the LSB has proper oversight of the entire regulated legal service sector and that the OLC is operating in accordance with the LSB's objectives for the regulation of legal services.
- 13.19. As per the analysis conducted using PwC's independent report, the Government is confident that the transition costs associated with the OLC option (£23.6m), are justified by the benefits accruing to consumers and the legal service sector as a whole from the introduction of a single, independent complaints handling body. These one-off costs should be seen in the context of the estimated £12m decrease in annual running costs of the complaints handling system.

### Summary of expected benefits and costs

13.20. The table below summarises the expected benefits and costs of the Government's preferred options for the reform of legal services:

	<b>Benefits</b>	<b>Costs</b>
<b>An oversight regulator (LSB)</b>	<p><u>Economic</u></p> <ul style="list-style-type: none"> <li>i. Consolidation of regulatory roles and responsibilities of the multiple oversight regulators to a single point of consistent regulatory oversight.</li> <li>ii. As a relatively small oversight regulator, LSB will be less bureaucratic and more efficient.</li> <li>iii. Simplified regulatory framework that reduces regulatory proliferation, fragmentation and inconsistencies. May lead to lower compliance costs for suppliers.</li> <li>iv. Risk of additional regulatory burdens reduced.</li> <li>v. Reduced likelihood of regulatory anomalies and gaps, offering greater protection to consumers.</li> </ul>	<p><u>Economic</u></p> <ul style="list-style-type: none"> <li>i. Risk of adding regulatory burdens on those suppliers of currently unregulated legal services, if these services are brought into the LSB's regulatory net.</li> <li>ii. Additional regulatory costs may be passed on to the consumer through higher prices. However, anticipated that additional regulatory burdens on professions will be minimal.</li> <li>iii. Risk of the professions formulating regulations that put the professions' interests above those of consumers. Risk minimised by LSB's ability to call in rules and to impose sanctions to ensure that regulations will not be set in such a way that would harm consumers.</li> </ul>



		<p><u>Social</u></p> <p>i. <i>Removal of self-regulation could dilute ethical responsibilities and regulatory accountability of individual practitioners increasing the risk of lowering standards to the consumers' detriment. This risk should be minimised through ARs' responsibility for ethical and regulatory accountability.</i></p>
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	<p>vi. <i>No self-regulatory element within the framework, ensuring that regulatory decisions are made in consumers' interest.</i></p> <p>vii. <i>Reduced risk of regulations being set to the detriment of competition and innovation.</i></p> <p>viii. <i>Less likely to lose regulatory expertise during transitional period.</i></p> <p>ix. <i>Retention of day-to-day regulation in hands of professional bodies should increase quality standards reducing risk of rising monitoring and enforcement costs.</i></p> <p>x. <i>Increased independence of regulatory decisions.</i></p> <p>xi. <i>Increased consumer confidence via greater accountability, transparency and regulatory certainty.</i></p> <p>xii. <i>Greater flexibility in the regulatory system, especially with regard to regulation of ABS firms.</i></p> <p>xiii. <i>Duty to consult with OFT when authorising new ARs and observing market behaviour will</i></p>	
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	<p><i>reduce anti-competitive practices.</i></p> <p><i>xiv. Independence of oversight regulator will ensure that foreign consumers are not deterred from using the UK for international and commercial litigation and arbitration.</i></p>	
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	<p><u>Social</u></p> <ul style="list-style-type: none"> <li>i. Principle of the legal profession being independent of Government will be demonstrated more clearly than if the regulatory role were removed from the professional bodies entirely.</li> <li>ii. Greater ability to adjust to future changes in the legal services market and to make the appropriate regulatory response. This will aid the future development in the market, bringing positive benefits in terms of increasing access to justice and diversity within the legal professions.</li> <li>iii. Introducing the LSB will eliminate the inconsistencies in the existing framework and identify best practice to achieve the objectives of reforming the regulatory framework.</li> <li>iv. Oversight regulator will ensure that regulatory gaps are anticipated and tackled before consumers are put at risk.</li> <li>v. Increased consumer confidence and improvement in professional standing of legal service providers.</li> </ul>	
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	<ul style="list-style-type: none"> <li>vi. Promotion of consumer interests and achievement of regulatory objectives.</li> <li>vii. Consumer input in LSB, through Consumer Panel, will ensure that decisions are made in the interests of the consumers.</li> <li>viii. Consumers will be better enabled to understand the system and feel empowered to make well-informed choices about purchasing legal services.</li> <li>ix. Compulsory separation of regulatory and representative functions of ARs will lead to accountability, transparency and an increase in regulatory certainty.</li> </ul>	
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	<u>Benefits</u>	<u>Costs</u>
<b>A new complaints handling body, the Office for Legal Complaints (OLC)</b>	<p><u>Economic</u></p> <ul style="list-style-type: none"> <li>i. <i>Independence for the complaints handling system, thus increasing consumer confidence in the legal services industry.</i></li> <li>ii. <i>Single point of entry for all service complaints simplifies complaint-handling arrangements for consumers and eliminates duplication of roles across profession leading to time and overhead savings for ARs and suppliers</i></li> <li>iii. <i>Greater consistency and clarity in the complaints handling process, leading to a more efficient and effective complaint mechanism, thus inducing savings for ARs and suppliers.</i></li> <li>iv. <i>Reduced inefficiency in complaints handling system by ensuring complaints are directed to the correct AR.</i></li> <li>v. <i>Redress award of up to £20,000 will provide an incentive for suppliers to improve quality of services to protect reputations of suppliers, thus reduce the likelihood of complaints lodged against them, potentially reducing administrative burdens.</i></li> <li>vi. <i>Possibility of redress will also encourage legitimate complaints from consumers who have received a poor service, increasing their confidence when purchasing legal services.</i></li> <li>vii. <i>Because the OLC will be an independent body with effective powers the legal professionals will have an incentive to adhere to the code of practice and disciplinary procedures as outlined by the ARs and OLC.</i></li> </ul>	<p><u>Economic</u></p> <ul style="list-style-type: none"> <li>i. <i>Increased rise in complaints will lead to an increased workload to handle complaints for sub-standard suppliers, though this may act as an incentive for them to improve standards of services.</i></li> <li>ii. <i>Legal professionals may become overly risk-averse and avoid taking more complex and difficult legal cases, reducing access to justice. But this risk already exists under the current system and there is no evidence to suggest that lawyers have been driven to avoid these types of cases.</i></li> <li>iii. <i>Confusion among ARs, the OLC and other statutory regulators as to how complaints should be handled. The LSB's duty to liaise with other statutory regulators will ensure the handling of complaints will be consistent across the professions involved.</i></li> </ul>
	<p><u>Social</u></p> <ul style="list-style-type: none"> <li>i. <i>Independence of the OLC will improve consumer confidence in the complaints system and aid the</i></li> </ul>	<ul style="list-style-type: none"> <li>iv. <i>Due to more effective complaints body, compliance costs for firms will rise in order to meet the standards set for 'in-</i></li> </ul>

	<p><i>LSB in achieving its objectives through focusing on consumer interests.</i></p> <p>ii. <i>The power that the OLC will have to share information about complaints will empower consumers to make better decisions when choosing their legal services provider and provides an incentive for providers to improve the quality of their services.</i></p>	<p><i>house' procedures. However, this may act as an incentive for providers to improve standards to reduce likelihood of complaints being lodged against them.</i></p> <p><u>Social</u></p> <p>i. Confusion may arise for the consumers when using ABS firms, as to how the complaints concerning cross-service practitioners should be handled. However, licensing authorities will have to have suitable and transparent arrangements with non-legal regulators in place before being authorised to allow firms to provide non-legal services. Firms will also have to make it clear to consumers at the outset how different regulators regulated different services in them.</p>
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13.21. The tables overleaf summarise the operating and transitional costs of the options proposed by the Government on reforming the regulatory framework and complaints handling arrangements for legal services:

### Reforming the regulatory framework:

<b>Option</b>	<b>Annual Running Costs</b>	<b>Transition Costs (two years before vesting)</b>	<b>Transition Costs (one year before vesting)</b>	<b>Transition costs (one year <u>after</u> vesting)</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Do nothing</b>	64,900	n/a	n/a	n/a
<b>With a Legal Services Authority</b>	66,400	11,550	16,740	27,000
<b>With a Legal Services Board</b>	67,250	200	1,580	500

### Reforming complaints handling arrangements:

<b>Option</b>	<b>Annual Running Costs</b>	<b>Transition Costs (two years before vesting)</b>	<b>Transition Costs (one year before vesting)</b>	<b>Transition costs (one year <u>after</u> vesting)</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Do nothing</b>	32,520	n/a	n/a	n/a
<b>With a Postbox</b>	32,920	-	-	500
<b>With an Office for Legal Complaints</b>	20,590	140	12,280	11,140

*All Costs in 2005-06 prices*

13.22. PwC's report also identified £1 million of additional "implementation costs" from setting up a task force for detailed organisation design for the LSB and the OLC. These costs were estimated to fall in the year before powers and duties are vested in the new bodies.

13.23. PwC have also costed alternative scenarios over and above their base cases outlined above.

13.24. For the LSB, this included costing for an incremental increase in the level of activity and locating the LSB in the North of England or London. A combination of these variables could result in the annual ongoing running costs of the LSB could rising to £5.6 million. The LSB costs would therefore rise to £69.0 million. Under this alternative scenario, transition costs could also be expected to rise by approximately £600,000.

13.25. For the OLC, this included costing an incremental level of resource for higher volume of complaints, at 25% and locating the OLC in the West Midlands. A combination of these variables could result in the annual ongoing running costs of the OLC rising to £21.0 million (base-case plus incremental volume of complaints, with a single-site location in the West Midlands). Under this alternative scenario, transition costs could also be expected to rise by approximately between £3.5 million and £6.6 million (dependent on the nature of the increase in complaints).

## **Legal Services Bill**

### **Supplement to Regulatory Impact Assessment**

#### **Introduction**

1. The Regulatory Impact Assessment (RIA), which was published with the Legal Services Bill in November 2006, set out the rationale for the reform of regulation of legal services. In March 2006, the Department for Constitutional Affairs (DCA) engaged PricewaterhouseCoopers (PwC) to prepare an independent report in connection with the DCA's consideration of the financial assessment of legal services reform. This report was published in May 2006. PwC's report, using broad assumptions, provided estimates for implementation and running costs of the options considered for regulatory reform, as well as reform of the complaints handling system. These estimates were used in the RIA to inform the Government's evaluation of the different policy options for reform.
2. Things have moved on considerably since PwC produced their report. Our implementation plans have been refined and amendments have been made to the Bill.
3. During the Lords debate on the Legal Services Bill at Report stage, on 8th May 2007 peers were supplied with revised headline figures for the costs associated with legal services reform. This supplement to the RIA, which was published with the Legal Services Bill in November 2006, seeks to provide further information on the costs stated during the debate.
4. PricewaterhouseCooper's (PwC) original forecast (in 2005 prices) for implementation costs was £26.8 million, of which £13.6 million would be recovered through the levy, £10.9 million would fall directly on the Law Society and £2.3 million would fall on the DCA now



Ministry of Justice (MoJ). Following further analysis by officials, the forecast for implementation costs now stands at **£32.1 million** (in 2007-08 current prices) of which £19.9 million would be recovered through the levy, £9.8 million would fall directly on the Law Society and £2.4 million would fall to the MoJ.

5. Running costs have also been reviewed and at 2007-08 current prices they now stand at £4.0 million for the Legal Services Board (LSB) and £19.9 million for the Office of Legal Complaints (OLC). PwC established running costs (in 2005 prices) stood at £3.6 million for the Board and £16.8 million for the OLC.
6. The tables in Annex A which provide a more detailed breakdown of figures for the revised implementation and running costs also show PwC figures at 2007-08 prices for comparison purposes.

### **Scope**

7. As stated in the full RIA published with the Legal Services Bill, its purpose was to set out the rationale for the reform of the regulation of legal services and analyse the likely effect on a range of key stakeholders of the options considered for implementing these reforms. It is not the intention of this supplement to revisit this work but only to provide a cost update based on the most current information available, with regard to the implementation of the preferred options identified in the RIA.
8. The preferred option for reforming the regulatory framework for legal services was to create a new independent oversight regulator, the Legal Services Board (LSB). In relation to reforming the complaints handling arrangements in legal services the preferred option was a new single complaint handling body, the Office for Legal Complaints (OLC), which would be independent from Approved Regulators.

### **Reforming the Regulatory Framework for Legal Services**

9. As detailed in part 4 of the RIA 'Reforming the Regulatory Framework for Legal Services' the preferred option was the establishment of a Legal Services Board, as an oversight regulator.
10. PwC's original forecast for implementation costs for the establishment of the LSB was £2.3 million (in 2005 prices). Following further analysis by officials, the forecast for implementation costs now stands at £4.2 million. The ongoing running costs as established by PwC were £3.6 million (in 2005 prices) of which £1.9 million were direct staff costs. The revised running costs of the LSB are now £4.0 million of which £2.0 million are direct staff costs.
11. These calculations are still based on the base case assumptions as established by PwC of 39 core staff members, with a 9-member board, a 10-person Consumer Panel in an out-of-London location and the assumption that the underlying nature of the regulatory activities, within the remit of the LSB's framework, would not be substantially different from those performed under the current regulatory framework.

12. Main adjustments to the implementation and running costs of the LSB include:

- All costs now stated at 2007-08 current prices
- VAT has been included in implementation costs
- Provision for staff training prior to go-live of the LSB
- Provision for a rules formation team, which will be responsible for developing different rules and policy statements for the Board.
- Provision for a project team to support the Board once they assume responsibility for managing the implementation process

### **Reforming the Complaint Handling Arrangements in Legal Services**

13. As detailed in part 6 of the RIA 'Reforming the Complaint Handling Arrangements in Legal Services' the preferred option was the establishment of a single complaints handling bodies for the entire profession, that is the Office for Legal Complaints.

14. PwC's original forecast for implementation costs for the establishment of the OLC was £23.6 million (in 2005 prices). Following further analysis by officials, the forecast for implementation costs now stands at £26.7 million in 2007-08 prices. The ongoing running costs as established by PwC were £16.8 million (in 2005 prices) using their base case scenario. The revised running costs of the OLC are now £19.9 million in 2007-08 prices.

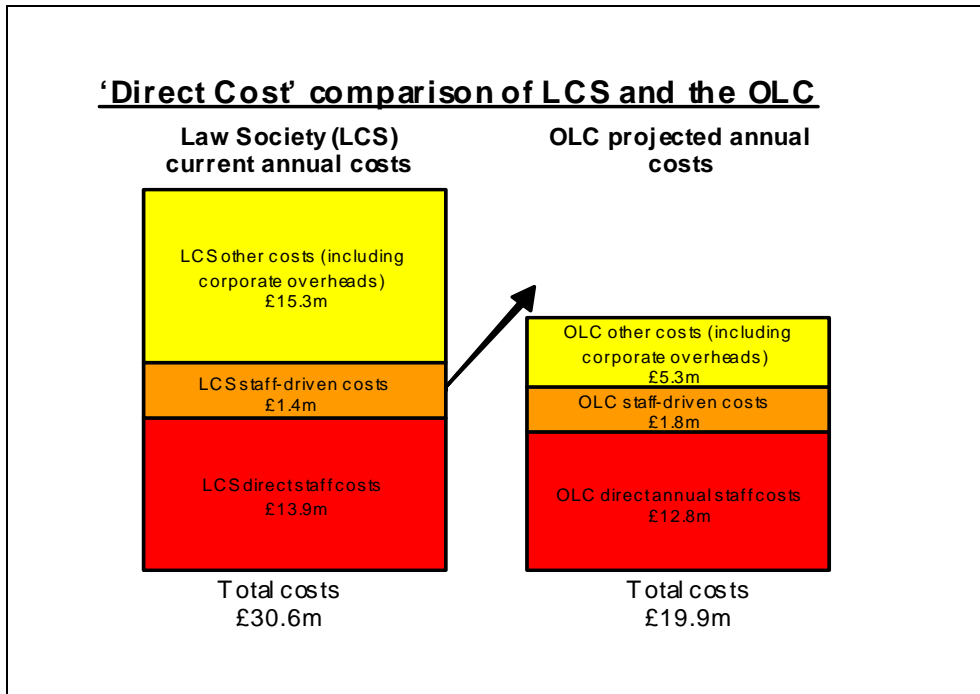
15. These calculations are still based on the detailed work that PwC did in relation to organisational design and the assumptions of a 7-member board and offices based in the West Midlands. However the staff profile has been adjusted to reflect an assumed year-on-year 5% increase in case receipts between now and go-live of the OLC. This has lead to an increase in staff from the 319 as estimated by PwC to 355 (excluding the board).

16. The same adjustments as listed above at point 12 in relation to adjustments made to LSB costs were also applied to the OLC.

#### Efficiencies based on cost revision

17. The RIA in section 6 discusses the issue of efficiency gains made by the OLC over the current complaint handling system. With the annual running cost of the OLC now estimated at £19.9 million (at 2007-08 current prices), there is now an estimated efficiency saving of 35% between the costs of the LCS and OLC, rather than the original PwC estimate of 40%. However, the OLC costs are now based on additional work undertaken to profile case receipts and therefore it is estimated that the OLC will be dealing with a higher volume of cases than originally estimated, with a year-on-year increase of 5%.

18. The figure below, which was contained in the original RIA (p.48), has been updated and now compares the cost breakdown of the revised estimate against the annual outturn figures provided by the LCS for the period ending December 2006.



19. Factors identified by PwC which contributed to the estimated saving, and which are still relevant in relation to the revised costs, included:

- A “bottom-up” approach to the calculation, based on a completely new cost model
- Reduction in the overhead costs for the OLC as compared to those levied on the LCS by the Law Society under current arrangements
- No contribution required to the cost of the Office of the Legal Services Ombudsman
- Implementation of modern systems and processes
- 15% efficiency gain in relation to case-handling

In reaching their assumption, PwC were further influenced by research conducted by Experian in January 2004 for the Lyons Review into the effect that public sector relocation can have on embracing different working methods and technologies.<sup>4</sup>

### **Funding of Implementation Costs and the Effect on Professions**

20. As stated in the RIA the Legal Services Bill includes provision for the LSB to make a levy on the profession to fund the cost of establishing and running the new arrangements. In part 12 of the RIA ‘Implementation, Delivery Plan and Post-Implementation’ paragraphs 12.6 to 12.9, information was supplied in relation to the affordability of this to the professions, which has been updated below.

<sup>4</sup> For more information see: <http://www.hm-treasury.gov.uk/media/98E/EB/ExperianResearch.pdf#search=%22Experian%3A%20%2E%80%98The%20Impact%20of%20Relocation%E2%80%99%20January%202004%22>

21. The legal services industry was estimated by the Office of National Statistics<sup>5</sup> to have a provisional turnover of £22 billion in 2005. Figures for members subject to regulation by the eight front line regulators identified by the bill in May 2005 stands at some 148,000. So at the most basic level, we could conclude that each regulated person is now responsible for generating a turnover of around £132,000 a year.
22. It would be for the LSB to apportion costs on a fair and proportionate basis between approved regulators. And in turn it would be for approved regulators to pass on these costs, again on a fair and proportionate basis, to those they regulate.
23. Although the basis for apportionment is yet to be agreed, at the most basic level the £19.9 million estimated as recoverable through the levy for implementation costs would represent a contribution of some £45 per member of an approved regulator. This is based on the 2007 membership figures supplied by regulators and assumed that the LSB will seek to recover the costs over a three year period in order to reduce any possible impact.
24. The implementation costs of £9.8 million which would fall directly to the Law Society are made up of two components. £6.2 million relates to the one-off costs of closing down the Legal Complaints Service (LCS) and any period of parallel running which may be required during handover. This equates to approximately £59 per member, based on a membership of approximately 104,500 in May 2007. The remaining £3.6 million which was identified by PwC relates to overhead charges levied by the Law Society onto the LCS, which the Law Society will be unable to avoid at the time the new complaints service goes live. This would constitute an additional one-off charge to Law Society members of £34 per person.

### **Methodology & Assumptions**

25. The work undertaken by PwC to produce the 'Financial Analysis to support the draft Legal Services Bill' published in May 2006 has provided the basis for the further work undertaken by the MoJ to update the costs based on current information and policy developments.
26. The key areas which were addressed during the review and produced outcomes which varied from PwC's were as follows.

#### Costs in current 2007/08 prices

27. In updating PwC's financial analysis all costs have been stated in current 2007/08 prices. This applies to both the costs identified by PwC and any additional items that have been identified such as the need for staff training (as detailed below).

#### VAT

28. VAT has been included in implementation costs as well as running costs. VAT in relation to implementation costs accounts for £3.3million. This figure has been calculated on the basis of

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<sup>5</sup> Office of National Statistics, Annual Business Inquiry – <http://www.statistics.gov.uk/abi>

advice from Her Majesty's Revenue and Customs (HMRC) that it is prudent to assume all non-staff costs will attract VAT of 17.5%.

### Staff training

29. Ensuring staff are adequately trained before the Board and the OLC assume their responsibilities will be crucial to ensuring both organisations are properly equipped from the outset and in a position to get off to the best possible start. Consequently, provision for staff training has been built into the implementation costs and accounts for £1.1million.
30. Identifying the costs associated with training, however, is obviously dependent on a number of factors including the skills and experience of existing staff, training lead in times and the resource needs of the legacy organisations and the new organisations in the lead up to, and following, vesting day.

### Caseload Profiling (to inform implementation process and staffing)

31. As a starting point a case work model was built, which profiles the case receipts and closures, and resulting work in progress of the Law Society, and once established the OLC, over the next seven years. The model assumes a year-on-year increase of 5% in case receipts, which is based on the Compound Annual Growth Rate (CAGR) of the Law Society's case receipts for 1977-2006. (The model has been built using Law Society case receipts because they account for 96%<sup>6</sup> of the total annual volume of cases. Additional flexibility has been built into the model, however, to take account of complaints about other legal service providers.)
32. This model was then flexed to reflect a revised profile on the basis that a proportion of the Law Society's work in progress will transfer to the OLC following vesting day. This revised profile has in turn been used to inform the number of staff that the OLC will need to have in post and trained by vesting day and its resource requirements over the months that follow. It has also been used to inform the number of staff that the Law Society will need to clear the cases that will not transfer to the OLC and consequently the period of parallel running that will be necessary. The assumptions that have been made in relation to staff training take into account whether staff will be transferring from the legacy entities or whether they will be new recruits. Advice from HR experts and specialists involved in managing training programmes for staff performing comparable functions in other organisations have also been used to inform the staff intake and training schedule and the resulting costs profile.
33. There are obviously a number of different ways in which the implementation from the Law Society and the other professional bodies to the OLC could be managed, and the approach, which has been costed only represents one option. The incoming OLC and its senior management team will undoubtedly have views on the way in which the process should be

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<sup>6</sup> This figure is taken from the Legal Service Ombudsman's annual report for 2005/06.

managed and it will also be critically important for the professional and consumer bodies to be involved in planning for this, and other aspects of, the implementation process.

#### Other adjustments

34. In addition to restating costs at current 2007/08 prices, VAT and staff training a number of other adjustments have also been made, which have involved both increases and decreases. The key increases include:

- provision for a rules formation team, which will be responsible for developing the different rules and policy statements that the Board and the OLC will need to be in place prior to vesting day; and
- provision for two project teams to support the Board and the OLC once they assume responsibility for managing the implementation process.

#### Contingency

35. The revised figures are based on a robust analysis and consequently the implementation costs will form the basis of the implementation budget for the Board and the OLC. However, it is obviously prudent at this early stage in the implementation process and given the scale of the reform programme, to build in a margin for unforeseen costs. The margin, which has been built in, is 15%, which is approximately £5million.

#### Assumptions

36. All costs have been calculated with regard to various underlying assumptions as detailed below:

- There are no significant changes to the Bill in relation to the activities of the LSB and OLC.
- The Cabinet Office will classify the bodies as NDPBs
- That all expenditure will be incurred by the LSB and OLC (excluding the recruitment costs for the Chair and Board for both organisations and any costs directly incurred by the Law Society or MoJ)
- Pay and benefits will be modelled on MoJ and LCS as appropriate

37. Assumptions which relate directly to the LSB are:

- 38 staff including CEO (excluding Board and Chair)
- The office will be in an out-of-London location
- That the LSB will utilise central services supplied and supported by MoJ

38. Assumptions which relate directly to the OLC are:

- 354 staff including both the CEO and Chief Ombudsman (excluding Chair and Board)

- A 5% increase in complaints year-on-year until go-live of the OLC
- The office will be in a West Midlands location
- 80% of staff will transfer from LCS

### **Summary and Conclusion**

39. Based on PwC's original estimate of the financial impact of the changes to the entire industry, the revised costs would still see a net decrease in overall cost to the legal services sector of £3 million. However, the increase in estimated running costs of the LSB and OLC may also be matched by an increase in the net regulatory cost of the industry since PwC's figures were produced in 2005 prices.

ANNEX A

**Legal Services Reform Programme - Implementation Cost**

	<b>MoJ</b>	<b>Law Society</b>	<b>LSB/OLC Levy</b>	<b>Total</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b><u>Implementation Cost for LSB</u></b>				
Salary Costs	2		1,588	1,588
Project Management	3		749	749
Recruitment Costs			500	500
Staff Driven	4		109	109
Accommodation	5		620	620
Business and IT Development	6		115	115
Other Costs	7 75		195	270
<b>Total Cost for LSB Implementation</b>	<b>75</b>	<b>0</b>	<b>3,876</b>	<b>3,951</b>
<b><u>Implementation Cost for OLC</u></b>				
Salary	2	1,785	2,033	3,818
Project Management	3		1,169	1,169
Recruitment Costs			568	568
Staff Driven	4		716	716
Accommodation	5		4,880	4,880
Business and IT Development (inc 6 Data Migration)	6		3,000	3,000
Other Costs	7 1,116	6,832	1,583	9,531
<b>Total Cost for OLC Implementation</b>	<b>1,116</b>	<b>8,617</b>	<b>13,949</b>	<b>23,682</b>
MoJ Programme Management Costs	1,161			1,161
<b>Total Implementation Costs (Exc. VAT)</b>	<b>2,352</b>	<b>8,617</b>	<b>17,825</b>	<b>28,794</b>
VAT @ 17.5% (non-staff)	8	1,196	2,070	3,266
<b>Total Implementation Costs (Inc. VAT)</b>	<b>2,352</b>	<b>9,813</b>	<b>19,895</b>	<b>32,060</b>
<b>PwC Implementation Costs (at 2007-08 Prices)</b>	<b>9</b>			<b>28,198</b>

Notes



- 1 All costs are stated at current 2007-08 prices
- 2 Salary costs relate to senior management in place during implementation (e.g. Chair, Board, Chief Exec.)  
Also includes staff for rules formation and staff training and restructuring costs for the LCS
- 3 Staff which will support each Board during implementation and associated accommodation costs
- 4 Costs which directly relate to staff e.g. Travel and Subsistence and Pension set up.
- 5 Includes all costs associated with finding accommodation and the fit out
- 6 Includes Business Analysis, Organisational/Process Design, Development of IT, specialist IT Project Management
- 7 Includes Communications, premises exit cost for existing organisations, running costs of LSB and OLC prior to go-live due to staff training, and any parallel running costs associated with the OLSO and LCS Holborn site following go-live of the OLC.
- 8 A 17.5% VAT provision on all non-staff costs per HMRC guidance, excluding early recruitment costs incurred by MoJ
- 9 PwC figures have been inflated using the CPI to provide comparative figures.

**Legal Services Reform Programme - Base Case Running Costs**  
**2007-08 Prices**

		<b>Total £'000</b>
<b><u>Running Costs for LSB</u></b>		
Direct Staff Costs	<i>1</i>	1,983
Staff Driven	<i>2</i>	112
Accommodation	<i>3</i>	467
Other Costs	<i>4</i>	1,100
Irrecoverable VAT	<i>5</i>	294
<b>Total Reviewed Cost for LSB Running Costs</b>		<b>3,956</b>
<b>PwC Established Running Cost (at 2007-08 Prices)</b>		<b>3,736</b>

**Running Costs for OLC**

Direct Staff Costs	<i>1</i>	12,754
Staff Driven	<i>2</i>	1,755
Accommodation	<i>3</i>	2,885
Other Fees	<i>4</i>	1,424
Irrecoverable VAT	<i>5</i>	1,044
<b>Total Cost for OLC Running Costs</b>		<b>19,862</b>
<b>PwC Established Running Cost (2007-08 Prices)</b>	<i>7</i>	<b>17,621</b>

Notes

1. This includes salaries, pensions and national insurance for all staff and board members.
2. These are costs relating directly to staff e.g. training and travel and subsistence.
3. All costs relating to the accommodation of staff including rent, rates and utilities.
4. Includes all other running costs e.g. Communications, provision of central functions such as HR and finance, pensions administration.
5. A 17.5% VAT provision on all non-staff costs per HMRC guidance.
6. All costs are stated in current 2007-08 prices.
7. Revised running costs are based on updated assumptions on case profiles and related staff changes and therefore are not directly relational to the original PwC work.