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(By post and email: consultation@sra.org.uk)

16 December 2014

Dear Sirs,

Response of the CLLS PRRC to the consultation on the SRA's regulation of consumer credit activities

The City of London Law Society ("**CLLS**") represents some 15,000 City lawyers though individual and corporate membership, including some of the worlds largest law firms. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

The CLLS responds to consultations on issues of importance to its members through its 19 specialist committees. This response has been prepared by the CLLS Professional Rules and Regulation Committee[1].

1. The Proposal

The SRA has proposed to withdraw from the Financial Conduct Authority's ("**FCA**") Designated Professional Body regime in respect of consumer credit activities. This regime currently

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[1] A list of the CLLS Professional Rules and Regulation Committee can be found at the end of this document.

enables SRA authorised firms to rely on the exemption in Part XX (the "**Part 20 Exemption**") of the Financial Services and Markets Act 2000 ("**FSMA**") from the need to become FCA-authorised in order to provide regulated financial services.

SRA authorised firms wishing to rely on the Part 20 Exemption must comply with the SRA Financial Services (Scope) Rules 2001 and SRA Financial Services (Conduct of Business) Rules 2001 (the "**SRA's Financial Services Rules**"). As an interim measure, following the transfer of consumer credit regulation from the Office of Fair Trading ("**OFT**") to the FCA on 1 April 2014, the FCA and SRA agreed that the SRA's Financial Services Rules should require SRA authorised firms relying on the Part 20 Exemption for consumer credit activities to comply with the provisions and guidance set out in Rule 1.3R of the transitional provisions in the FCA's Consumer Credit sourcebook ("**CONC**"). Having failed to reach agreement on appropriate amendments to the SRA Financial Services Rules to be applied when the interim measures end on 1 April 2015, the SRA is simply proposing to withdraw the Part 20 Exemption in respect of consumer credit activities from that date.

2. The SRA's Regulatory Obligations

A withdrawal of the Part 20 Exemption would lead to fundamental changes for those of our members who undertake consumer credit activities. We are therefore deeply concerned about the short time in which the SRA has chosen to consult on this issue and the inadequacy of the proposed transition period should it proceed.

The consultation was published on 13 October 2014, less than 6 months from the date on which the SRA proposes to withdraw the Part 20 Exemption. It is thought to take at least 6 months to become authorised by the FCA to conduct regulated consumer credit activities.

Unless a firm had already determined to make an application to become FCA authorised before this proposal was first announced, it is unlikely to be able to complete the process in time to continue to conduct these activities with effect from 1 April next year. Although the FCA will make a decision on complete applications within six months of receiving them, the decision to become dual regulated by the FCA and SRA is not a decision that can be taken lightly and the preparation for such an application will itself take time. If the SRA proceeds as suggested, it could force firms who currently rely on the Part 20 Exemption to cease consumer credit activities until such time as they can become dual regulated. Forcing an albeit temporary closure of a business area, and the subsequent dual regulation of firms that wish to continue with it, is clearly not going to be in the interests of those firms. It would also appear to:

- be detrimental to the interests of clients who currently receive consumer credit services from their SRA regulated legal providers; and
- discourage competition in the provision of professional services.

This would seem to be inconsistent with the SRA's regulatory objectives as set out in section 1 of the Legal Services Act 2007.

Should the SRA decide to withdraw the Part 20 Exemption in relation to consumer credit activities, it should only do so at a later date having agreed with the FCA a mechanism to enable

an orderly transition for those firms who wish to continue to assist their clients with this area of work.

3. Dual Regulation

As noted above, if the SRA proceeds with this proposal, firms that wish to continue to provide consumer credit related services in conjunction with their legal practice will have to become FCA-authorised. Since the FCA is not an approved regulator for the purposes of the Legal Services Act 2007, this will force those firms into dual regulation.

Dual regulation will impose additional costs on firms that are likely to need to be passed on to clients. Further, it will have administrative consequences for firms, including, by way of example, additional reporting obligations, and personal consequences for those partners who would have to become approved by the FCA.

We therefore wish to encourage the SRA to explore what the additional cost would be of establishing the necessary consumer credit expertise and capacity to continue to effectively regulate the legal profession when it undertakes consumer credit activities in a manner that would be acceptable to the FCA. The SRA should also explore the option of how to meet those costs either from the profession as a whole or from those who wish to rely on the Part 20 Exemption and compare this to the additional cost to those firms of FCA regulation. We believe that it would be far more cost effective for the SRA to continue to regulate consumer credit activities.

4. Acceptable new Rules for those relying on the Part 20 Exemption

The SRA has expressed a concern that incorporating CONC, or a substantial part of it, into the SRA Financial Services Rules, could result in rules that are not proportionate and which unnecessarily duplicate existing SRA requirements and are not consistent with the SRA's general approach to regulation. Forcing SRA regulated firms to become dual regulated by the FCA instead, with the result that they will have to comply with CONC in full, does not address this concern. Not only will those firms still be faced with rules that may not be proportionate and which duplicate requirements, they will also potentially have to comply with two sets of rules in relation to the same service.

The Institute of Chartered Accountants in England and Wales ("**ICAEW**"), the Institute of Chartered Accounts in Scotland and Institute of Chartered Accountants in Ireland (operating as Chartered Accountants Ireland), each of which is a Designated Professional Body for the purposes of the Part 20 Exemption, have also been discussing with the FCA new rules that they will need to adopt to enable their members to continue to rely on the Part 20 Exemption in relation to consumer credit activities from 1 April 2015. We understand that these three Institutes and the FCA are working closely together to reach an agreement that will enable their members to conduct consumer credit activities as an incidental service subject to compliance with a condensed version of CONC. The aim being to ensure that firms are not deterred from providing consumer credit services while still extending appropriate protection to consumers.

Perhaps the SRA could engage again with the ICAEW and other Designated Professional Bodies who are seeking to adopt a version of CONC that would be appropriate to their members

and proportionate to the risks posed by the ancillary consumer credit activities their members undertake and explore whether this is a model that could also work for the SRA.

5. Matters the SRA should be raising with the FCA and HM Treasury

Although a number of the points below arise primarily as a result of the withdrawal of the group licence previously granted to The Law Society of England and Wales, rather than the SRA's proposed withdrawal of the Part 20 Exemption, we firmly believe the SRA should be making representations to the FCA and HM Treasury to:

5.1 Clarify, and provide guidance on, the activities carried on by solicitors that are within regulated consumer credit activities

It is generally easy to spot if someone is conducting consumer credit activities by way of business, but the breadth of these activities means that activities that might otherwise be considered a necessary part of the provision of legal advice, and so not obviously within the scope of the specified activities, may be caught.

For example, it is clear that it is possible to provide legal advice to lenders under regulated credit and hire purchase agreements concerning their regulatory obligations, policies and procedures without requiring regulatory authorisation. It equally seems apparent that more specific legal advice can be given on a lender's position under a specific credit or hire purchase agreement provided the firm does not cross the line and stray into a regulated consumer credit activity, but is it always clear where that line should be drawn?

To provide a further illustration, firms handling personal injury claims will often act for clients who are vulnerable and who are debtors under a number of regulated credit or hire purchase agreements. When these clients receive compensation in respect of their claims, they will often seek initial advice about what they can do with the compensation from the law firm they have come to trust. If these firms are not FCA regulated or within the Part 20 Exemption, to what extent can they assist their client?

5.2 Extend the contentious business exclusions

Articles 36F, 39K and 89C (Activities carried on by members of the legal profession etc) exclude from the consumer credit activities specified in chapters 6A (Credit broking), 7B (Activities in relation to debt) and Part 3A (Specified activities in relation to information) of the FSMA (Regulated Activities) Order 2001 ("**RAO**"), activities carried on by SRA authorised firms acting in the course of contentious business.

Contentious business is defined as business that takes place once proceedings have been commenced before a court or arbitrator. These exclusions cannot, therefore, be relied upon in respect of pre-action work where proceedings have not yet been commenced or may not be commenced because the matter settles. If these exclusions could be extended to make it clear that preparatory or pre-action work which might become contentious was also excluded (whether or not the matter does in fact become contentious), a significant number of firms that currently seek to rely on the Part 20 Exemption would not need to do so and would not be forced, unnecessarily, into dual regulation.

This would also be in the interests of consumers who require services which may become contentious. If the Part 20 Exemption is withdrawn, these consumers will otherwise need to use an FCA-authorised firm for pre-action work and to then switch to a person who is authorised under the Legal Services Act 2007 for the contentious aspects. This is unlikely to be cost effective or efficient. Alternatively, the consumer will be limited to using firms who are dual regulated which is likely to significantly limit the consumer's choice.

5.3 Extend the exemption for activities carried on in the course of a profession or non-investment business

Article 67 RAO excludes many activities that would otherwise fall within the regulatory remit of the FCA, such as insurance mediation and investment activities, from the general prohibition where they: (i) are carried on in the course of carrying on any profession or business which does not otherwise consist of the carrying on of other regulated activities; and (ii) may reasonably be regarded as a necessary part of other services provided in the course of that profession or business.

Extending this exclusion to cover consumer credit activities would ensure that firms providing these activities as a necessary and inseparable part of the provision of legal services, for which they are not separately remunerated, will not inadvertently be caught by the need to become FCA-authorised. Any firm that is providing consumer credit services as an additional business area, which could be separated from their legal advice, would not fall within this exemption and so would still need to fall within the Part 20 Exemption or be FCA regulated. Extending this exemption would provide a significant amount of certainty for a number of firms that do not conduct these types of activities as a business area but may, occasionally, touch on consumer credit related activities in the course of providing legal advice. We urge the SRA to seek to have this exemption extended to consumer credit activities as a matter of priority.

5.4 Allow firms regulated by the FCA for consumer credit activities to continue to rely on the Part 20 Exemption and Article 67 RAO exclusion for other financial services

If the SRA is going to withdraw the Part 20 Exemption for consumer credit activities, it should push for a redrafting of both the Part 20 Exemption and Article 67 RAO exemption, so that firms that become FCA-authorised for the purposes of consumer credit activities can continue to rely on this exemption or exclusion in respect of other financial services. If this does not happen, the level of unnecessary dual regulation that these firms will face could be very significant indeed.

Some firms that currently rely on the Part 20 exemption for consumer credit activities also rely on it in respect of other financial service activities, such as insurance mediation. If the SRA withdraws the Part 20 Exemption as proposed, these firms will need to make separate applications to become fully FCA regulated for each of the other financial services they provide as an incidental part of their legal services. This is because the Part 20 Exemption and Article 67 exclusion can only be relied upon if the firm does not carry on any other FCA regulated activities. The additional cost and administrative burden for these firms will not be limited to that of becoming dual regulated in respect of consumer credit. Again these costs will need to be passed on to clients or those firms will need to cease those activities. Neither of these options would be desirable for clients who currently receive these services from SRA regulated firms.

5.5 Exempt extended payment terms offered to clients

Where a law firm makes an arrangement with a client who is an individual and who might otherwise be unable to pay its fees, allowing the client to pay his/her fees over an extended period, this should not by itself mean that the firm is conducting consumer credit activities that require it to be regulated by the FCA or to fall within the Part 20 Exemption (if it is retained).

Law firms can avoid any such arrangement being a regulated consumer credit agreement by relying on the exemption in Article 60F RAO if they agree: (i) not to charge interest; (ii) that the amount must be paid in full within twelve months; and (iii) that the amount must be paid in four or fewer instalments, but this may not be possible for the client to comply with. Law firms who wish to come to a different arrangement with their client about how to meet their fees are not extending loans or credit to their clients by way of business, but merely trying to ensure that their fees will be paid. Although law firms are not in a unique position in this regard, there are a couple of reasons why an exemption of this type would be reasonable:

- the fee mechanisms law firms can agree with clients, especially as regards contentious business, are already subject to significant legal and regulatory restrictions; and

- removing the ability of firms to reach fee agreements with individual clients that do not meet the conditions set out in Article 60F RAO, may limit a client's access to legal advice and justice.

If the exemptions and exclusions discussed above cannot be extended, it will be easy for firms, especially smaller firms that may not have centralised risk management departments, to provide consumer credit activities in connection with their legal services without realising that they are doing so. Thus potentially and unnecessarily becoming exposed to criminal liability and the risk that they might bring the profession into disrepute.

We urge the SRA to reconsider its proposals and we would be pleased to support any lobbying efforts the SRA may be willing to make vis-à-vis the FCA and HM Treasury on the points raised in this letter.

Yours faithfully

P.P. G Thorne

Sarah de Gay
Chairman, CLLS Professional Rules & Regulation Committee

THE CITY OF LONDON LAW SOCIETY

Professional Rules & Regulation Committee

Individuals and firms represented on this Committee are as follows:

Sarah de Gay (Slaughter and May) (Chairman)

Tracey Butcher (Mayer Brown International LLP)

Roger Butterworth (Bird & Bird LLP)

Raymond Cohen (Linklaters LLP)

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Jonathan Kembery (Freshfields Bruckhaus Deringer LLP)

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