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9th June 2015

Dear Sirs

Response of the CLLS Professional Rules and Regulation Committee to the SRA's consultation "SRA Regulatory Reform Programme" (the "Consultation")

The City of London Law Society ("CLLS") represents approximately 17,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. 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 a variety of consultations on issues of importance to its members through its specialist committees. This response to the Consultation has been prepared by the CLLS Professional Rules and Regulation Committee (see list of members attached).

Foreword on the SRA's use of guidance

On a general note, we are concerned that two of the Consultation questions (13 and 16) propose the addition of new guidance to the Code of Conduct. In our view, Outcomes Focussed Regulation and the recently stated aims of the SRA about its approach to proportionate regulation should result in a tendency towards no guidance rather than more.

Both the process for producing guidance and its status are opaque. In our view, there have been instances of guidance being issued in the past that is incorrect or could cause confusion, with no evidence of consultation with the profession prior to its release. At least one of the issues addressed in this Consultation may be attributed, in whole or in part, to inconsistent SRA guidance. Further, the SRA publishes guidance in a variety of formats and locations which makes it difficult for the profession to maintain appropriate awareness.

In addition, the status of such guidance, in relation to Outcomes, indicative behaviours, other guidance and enforcement decisions, is often unclear. Part of the purpose of Outcomes

Focussed Regulation was to give authorised bodies a wide berth of flexibility in determining the means by which regulatory outcomes are to be achieved. Outcomes or other rules should be capable of being understood on their face. If an Outcome is unclear, we consider that the most appropriate course of action is to address it directly by amending the drafting of that Outcome.

We believe that the SRA shares this view and it is our hope that this will be reflected in future iterations of the Handbook.

Finally, it is worth noting that those providing (non-reserved) legal advisory services in the unregulated sector do so free of any Outcomes, Indicative Behaviours or guidance which also suggests that be less rather than more SRA guidance should be a (level playing field) goal.

The Consultation Questions

In respect of some of the Consultation questions, we do not consider that the issues in question are especially relevant to CLLS members. Accordingly, this response is limited to Consultation questions 4, 5, 9-11, and 13-18.

4. **CQ4: Do you have any views on the SRA's proposal to simplify candidate declaration and notification processes?**

4.1 We agree with the SRA's proposal to simplify candidate declaration and notification processes.

5. **CQ5: Do you agree with our proposal to simplify authorisation by removing the requirement for firms to carry out reserved legal services?**

5.1 Yes. We also agree with the SRA's proposed changes to rules 4.2, 4.3 and 22.1. This arises in one particular situation for international firms when opening a new office outside England and Wales, where for technical reasons this needs to be a separate entity and not a branch of the main SRA authorised LLP, so a new entity (perhaps another LLP) is chosen, but it is a requirement, or at least highly desirable from the point of view of registration with the local bar, that the entity itself already be SRA authorised. The firm would be seeking SRA authorisation for an entity that may not, in fact, practice in or from England and Wales. The proposed rule change would be helpful in this regard.

9. **CQ9: Do you agree with our proposal to adjust the regulations to cover the event of partnerships entering administration?**

9.1 Yes.

10. **CQ10: Should the SRA approve third party managed accounts?**

10.1 While we have no objection in principle to the use of third party accounts as an alternative to client accounts, our members are firmly in favour of client accounts as the primary means of managing client monies. We acknowledge the SRA's view in paragraph 41 of the Consultation with regard to the cost of regulation associated with client accounts, although we note that no evidence is offered to support the suggestion that third party managed account may offer a lower cost alternative. In any event, we consider that the SRA must recognise that client accounts provide significant benefits to firms and clients. Those benefits include:

(a) *Security and clarity for both clients and firms.* The accounts that can be used as client accounts are strictly defined and are held in secure institutions. Clients are familiar with these institutions and understand that their funds are held securely under strict requirements prescribed in the SRA Accounts Rules.

(b) *Flexibility to place funds to meet clients' needs*. Although the institutions where client accounts can be held are strictly defined, there is flexibility to take account of a particular bank or building society that a client may prefer and the interest rates available.

(c) *Speed of access to funds to enable immediate completion of a client's' transactions*. Whether the sum held is a few thousand pounds or hundreds of millions of pounds, the same processes apply to the transfer of funds which can be effected extremely quickly, whilst remaining within the recognised secure banking system. Speed of access and transfer is an important part of our service.

10.2 For the above reasons, we would not wish any rule change intended to expressly approve the use of third party managed accounts to become a precursor to restrictions on firms managing their own client accounts. No changes should be made to the use of client accounts without full consultation with the profession as part of a wider principles-based review of the SRA Accounts Rules.

11. **CQ11: If so,**

- **should these be assessed and considered by the SRA on a case by case basis, or**
- **Should the SRA identify a minimum set of safeguards that should apply to all third party managed accounts?**

11.1 If the SRA were to implement rules expressly enabling the use of third party accounts, we consider that case-by-case approval would be disproportionate, particularly where the purpose of the rules is to reduce the costs of regulation associated with client accounts.

11.2 If the SRA were to identify a minimum set of safeguards, such as those in Annex A, that should apply to all third party managed accounts, we consider that those safeguards should, at a minimum, be commensurate with the safeguards applicable to client accounts. Furthermore, any such safeguards should be made express in the Accounts Rules as opposed to guidance documents or other ancillary publications.

13. **CQ13: Does the SRA's additional guidance on recording of non-material breaches provide further clarity on this requirement?**

13.1 We consider that rule 8.5(c)(1)(C) is clear and unambiguous in its current form and leaves significant discretion to COLPs and COFAs with regard to the means of compliance. Accordingly, we do not consider that introducing further guidance is necessary, particularly where extensive guidance relative to Rule 8 already exists and in light of our earlier stated views on guidance generally.

13.2 Should the SRA takes the view that guidance is necessary, we would suggest simply stating: "*The obligations to record non-material breaches under Rule 8.5(c)(i)(C) and Rule 8.5(e)(i)(B) do not require a record to be kept in any particular form*".

14. **CQ14: Should the SRA also give consideration to removing the requirement for firms to record such breaches at all? If so, why?**

14.1 There is a variety of views on this subject. Arguably, all that is necessary is for firms to follow their obligations to monitor compliance and manage risks as set out (for example) in Outcomes 7.3 and 7.4. The majority of our members, however, take the view that a specific obligation to record non-material breaches assists those within a firm who are responsible for managing compliance to ensure matters are reported to them from the front line in a consistent and timely way and thus allows them to monitor

for patterns of breaches as well as take steps to fulfil their reporting obligations in terms of material breaches.

14.2 That said, we would question whether it is proportionate for the SRA to continue to require non-material breaches to be recorded at all (by law firms which are not ABS) – particularly as the result of the SRA's separate business rule consultation could well be that traditional law firms will be able to invest in unregulated businesses providing legal advice which will have no breach recording/reporting requirements.

15. **CQ15: Does the current rule in relation to outsourcing present unforeseen difficulties to firms wishing to take advantage of cloud computing options?**

15.1 We do not consider that the current rule in relation to outsourcing presents such difficulties to firms. We do, however, consider that existing SRA guidance may have generated confusion with regard to the application of Outcome 7.10(b) to cloud computing.

15.2 In paragraph 54 of the Consultation, the SRA states in relation to Outcome 7.10(b) that: "*it is important to note that (as the connecting word is '**or**' enter the premises, and not '**and**'), provided that a firm has an agreement to obtain or inspect the information, there would be no specific requirement to be able to enter any relevant premises*". We agree with this interpretation, which is consistent with the natural language of Outcome 7.10(b).

15.3 The SRA has, however, issued previous guidance which conflicts with its statement in paragraph 54. For example, at page 13 of the SRA's guidance document 'Silver Linings: cloud computing, law firms and risk' (November 2013), the SRA states: "*Firms dealing with cloud providers must be able to meet the requirements of Outcome 7.10 of the SRA Code of Conduct, which requires contractual terms authorising the SRA to access data **and** visit provider premises*" [1] (emphasis added).

15.4 This 2013 guidance may be the source of uncertainty among firms concerning the application of Outcome 7.10(b) to cloud computing. Such inconsistency highlights the risks to firms of regulatory guidance which is not of the appropriate quality and which fetters firms' discretion in determining how they achieve regulatory outcomes.

16. **CQ16: Does the addition of the proposed guidance note on Outcome 7.10 provide sufficient clarity, or should the SRA make changes to this Outcome to provide further guidance to firms?**

16.1 It is our view that neither the guidance on interpreting Outcome 7.10(b) (Option 1) nor the amendments specified in Annex C (Option 2) are necessary. We suggest that the best way to resolve confusion concerning Outcome 7.10 and achieve the SRA's regulatory intent is to delete the existing guidance concerning cloud computing and simplify Outcome 7.10 by deleting Outcomes 7.10(b), (c) and (d). The resulting outcome would state: "*subject to Outcome 7.9, where you outsource legal activities or any operational functions that are critical to the delivery of any legal activities, you ensure such outsourcing does not adversely affect your ability to comply with, or the SRA's ability to monitor your compliance with, your obligations in the Handbook*". In addition to resolving existing confusion, the above would avoid unnecessary guidance and eliminate outcomes which merely exemplify others.

16.2 Notwithstanding the above, we strongly favour option 1 (new guidance) over option 2 (Outcome changes specified in Annex C). The drafting of option 2 has the potential to create further confusion as it removes the term '**or**' such that items (i), (ii) and (iii) are required in the conjunction. With regard to item (ii), we would interpret this as a requirement to *always* include a contractual term in outsourcing contracts enabling the SRA or the firm to "*enter such premises as may be appropriate*". This goes beyond

[1] www.sra.org.uk/documents/.../cloud-computing-law-firms-risk.pdf

what is necessary and we do not believe it is what the SRA intends. If, notwithstanding our view in paragraph 16.1, the SRA chooses Option 1, we consider that the draft guidance in Annex C should be further clarified. Specifically, sentence three of the draft guidance states: "*It will not be necessary for all such arrangements to include a right to enter the third party's premises depending on the nature of the activities or operations outsourced and the arrangements in place for carrying these out*". Some firms may interpret this as implying that most arrangements will require a right of access. We do not believe that is the intention. We consider that the following alternative would provide greater clarity: "*A right to enter third party premises is unlikely to be necessary in many outsourcing arrangements where there is otherwise a right to inspect or obtain such information as might be required to enable the SRA to exercise its powers in respect of you. You should have regard to the nature of the activities or operations outsourced".*

16.3 We do not therefore think either option is appropriate but, for the sake of clarity, have added our comments on both.

17. **CQ17: Do you have any comments on the SRA's proposal to clarify the current requirements for the recording and reporting of diversity data?**

17.1 To the extent that this proposal merely formalises existing obligations on firms to monitor and report workforce diversity data, we have no objection to the proposal. It is our belief, however, that the proposed new Outcome 2.6 goes beyond current requirements in relation to publication.

17.2 Current guidance states: "*it is **only a summary of the data that needs to be published** and firms can present the data in a variety of ways*"[2] (emphasis added). The proposed new Outcome 2.6 states: "*you have appropriate arrangements in place for … publishing workforce data*". So as to reflect current requirements and avoid any ambiguity as to what data must be published, we suggest that the SRA amends the proposed new Outcome 2.6 to state: "*you have appropriate arrangements in place for monitoring and reporting workforce diversity data, and for publishing a summary of that data.*"

18. **CQ18: Do you agree with our proposal to enable qualification as a solicitor through an apprenticeship route?**

18.1 The CLLS Training Committee is submitting a separate response to this question.

Yours faithfully

THE CITY OF LONDON LAW SOCIETY

Professional Rules and Regulation Committee

[22] http://www.sra.org.uk/diversitydata/#Collection_5

Individuals and firms represented on this Committee are as follows:

Sarah de Gay (Slaughter and May, Chair)

Roger Butterworth (Bird & Bird LLP)

Jonathan Kembery (Freshfields Bruckhaus Deringer LLP)

Clare Wilson (Herbert Smith LLP)

Chris Vigrass (Ashurst LLP)

Antoinette Jucker (Pinsent Masons LLP)

Mike Pretty (DLA Piper UK LLP)

Jo Riddick (Macfarlanes LLP)

Raymond Cohen (Linklaters LLP)

Annette Fritze-Shanks (Allen & Overy)

Heather McCallum (De Vere Group)

Douglas Nordlinger (Skadden)

Tracey Butcher (Mayer Brown)