

EXPLANATORY MEMORANDUM TO

THE ACCESS TO JUSTICE (MEMBERSHIP ORGANISATION) REGULATIONS 2005

2005 No.2306

1. This explanatory memorandum has been prepared by the Department for Constitutional Affairs and is laid before Parliament by Command of Her Majesty.

This memorandum does not contain any information of special interest to the Joint Committee on Statutory Instruments

2. **Description**

2.1 These Regulations replace The Access to Justice (Membership Organisation) Regulations 2000 with effect from 1st November 2005, simplifying the prescribed client care and cost information requirements included in the existing secondary legislation.

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

3.1 None

4. **Legislative Background**

4.1 Section 30 of the Access to Justice Act 1999 applies where a body of a description to be specified in regulations undertakes (in accordance with arrangements satisfying conditions to be so specified) to meet liabilities which members of the body or other persons who are parties to proceedings may incur to pay the costs of other parties. Regulation 3 of the Access to Justice (Membership Organisation) Regulations 2000 sets out the existing requirements for arrangements to meet costs liabilities. Regulation 4 of the new Access to Justice (Membership Organisation) Regulations 2005 specifies the much simplified requirements that the arrangements must satisfy.

5. **Extent**

5.1 This instrument applies to England and Wales.

6. **European Convention on Human Rights**

No statement is required.

7. Policy background

7.1 The DCA conducted consultation exercises in 2003 and 2004 on the simplification of the secondary legislation governing the use of CFAs. The consultations also considered the secondary legislation concerning membership organisations. The final outcome of the consultation was published by DCA on 10 August 2005 – *New Regulations for Conditional Fee Agreements (CFAs) - A summary of responses to the consultation paper Making Simple CFAs a Reality, the DCA's conclusions and the new regulations.*

7.2 The Membership Organisation Regulations specify the way in which the Secretary of State prescribes the bodies which are entitled to recover a 'self insurance' premium. The regulations also set out the conditions which an arrangement must satisfy and the way in which the 'self insurance' premium is to be calculated. The regulations are permissive and place a minimal regulatory regime on membership organisations. In particular they require that the recoverable self-insurance element should not exceed the likely cost of an equivalent commercial premium. The consultations only sought comments on the contractual and other requirements set out in regulation 3.

7.3 The existing requirements are designed to ensure that the client is aware of the arrangements for payment of the solicitor's costs. However, given that the membership organisation will in nearly all circumstances be indemnifying the member for any costs liability, it has been concluded that the amount of detail required by the current regulation 3 was unnecessary and cumbersome and of no real value to the member. Therefore the requirements will be simplified in the new regulation 4 to the need for a written explanation (for those rare circumstances where an indemnity would not apply).

7.4 Although the substantive changes to the current regulations are focused on one regulation it was concluded that it would be clearer and simpler for those that have to work with these requirements to replace the existing regulations rather than issuing more complex amending regulations.

8. Impact

8.1 A Regulatory Impact Assessment is attached to this Memorandum.

9. Contact

Kevin Rousell at the DCA, tel: 0207 210 8712 or e-mail Kevin.Rousell@dca.gsi.gov.uk can answer any queries regarding the instrument.

Annex F: Final regulatory impact assessment

Simplifying CFAs - final regulatory impact assessment

Title of proposal

1. The Government's conclusion and proposals following a formal public consultation by the Department for Constitutional Affairs (DCA) on *Making Simple CFAs a Reality*.

Purpose and intended measure

Objective

2. The aim is to make CFAs simpler, clearer and more transparent both for the individuals using them and the solicitors advising individuals about their cases and whether to use CFAs.

Devolution

3. This change applies to England and Wales only.

Background

4. Conditional Fee Agreements (CFAs), Collective Conditional Fee Agreements (CCFAs) and the Membership Organisation Regulations 2000 made significant changes to the way in which personal injury cases are funded by introducing the concept of being able to recover success fees and after the event (ATE) insurance premiums from opponents.

New Regulation for Conditional Fee Agreements (CFAs)

5. The consultation paper issued in June 2003² examined the key issues and perceived problems concerning conditional fee agreements and the related regime, and sought views, comments and proposals on what, if anything, needed to be changed. Following consultation, the Government will revoke the existing CFA and CCFA regulations and focus client care and contractual responsibilities in the Law Society's practice rules and costs information code. The perceived problems were as follows:
 - . Existing CFA regulations are too complex and extensive.
 - . Existing regulations encourage technical challenges from the losing party.
 - . Existing CFA regulations are difficult for individuals to understand.
 - . Existing CFA regulations duplicated the requirements of the Law Society's Professional Conduct Rules.
6. The consultation paper *Making Simple CFAs a Reality* Issued in June 2004 provided a summary of responses to the consultation paper published in June 2003. It set out DCA's proposals to reform the secondary legislation governing the operation of CFAs and published a set of new draft regulations for consultation.

7. The paper also stated DCA's response and, where appropriate, proposed action on a number of other issues raised during the 2003 consultation period, including: the regulation of claimed management intermediaries; the indemnity principle; the impact of recoverability; and the potential for the use of CFAs in cases run on a pro bono basis. The paper also discussed the impact of CFAs and costs more generally in defamation cases and invited respondents to comment on the problems identified and on potential solutions.
 8. Respondents were also invited to comment on the partial regulatory impact assessment.
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2 Simplifying CFAs – The Conditional Fee Agreement regime including the Conditional Fee Agreements, Collective Conditional Fee Agreements and Membership Organisation Regulations – CP 09/03.

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9. The consultation was widely welcomed, and respondents included the legal professional bodies, trade unions, media groups, the judiciary, individual practitioners and the insurance industry. In addition, a round table event on issues raised by the consultation paper was held on 8 July 2004. This was hosted by the DCA Minister David Lammy, was attended by a range of key stakeholders, and provided a forum to discuss the implications of the consultation paper.
10. Respondents generally agreed with the proposal that the CFA regulations should be simplified and client care moved to the Law Society Professional Conduct Rules. Some suggested that it was essential that provision be made within the Professional Conduct Rules to describe the penalties for failure to comply with the rules.
11. The proposed changes are as follows:
 - To remove the client care and costs information requirements from the CFA regulations and to focus the client care and contractual responsibilities in the Law Society's Professional Conduct Rules and client care and costs information code.
 - To revoke the existing CFA and CCFA regulations for all new cases and to rely on the primary legislation (Access to Justice Act 1999) to provide the minimum government legislative framework for the use of the CFAs by the legal profession by Autumn 2005.
 - To work with the Law Society to make any necessary revisions to the Law Society costs information code and the development of a new model CFA for solicitors' use by Autumn 2005.
 - To simplify the Membership Organisation Regulations to the extent that primary legislation will allow.
 - To introduce consequential amendments to the Civil Procedure Rules in respect of changes to the regulations after the CFA legislation is amended.

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12. Retaining the existing CFA regulations with their complexities would minimise the use of CFAs and deny access to justice to people with genuine claims, and would hamper the development of CFAs as a preferred means of funding litigation.

13. The main risks identified are that the complexity of the current CFA requirements has made it more than necessarily difficult for solicitors to explain their application to their clients and has also made the process less transparent. All respondents agreed that the current CF A secondary legislation is unnecessarily complex and should be simplified, and that the regime should be made more transparent. They believed the very detailed nature of the requirements had led to enormous problems in the application of CFAs, which are virtually impossible to explain to clients.

14. There is duplication of regulation of solicitors in client care matters, which has caused some concerns among the professionals. This has made CFAs susceptible to technical challenges from third parties, has put unnecessary burdens on professionals and has caused wasted time and costs. Advice agencies have seen an increase in clients coming to them for advice on CFAs and their application. Revoking the current CFA regulations would reduce unnecessary regulations, improve the current legislation and achieve greater stability, simplicity, transparency and higher standards, which would help both the clients and the professional bodies. The majority of the respondents agreed that the proper place for regulating the behaviour of solicitors and for looking after the interests of consumers was in the Law Society's rules rather than in secondary legislation, which had instead become a target for payment avoidance tactics by losing defendants.

Scaling the Issues

15. There is a lack of data on the number of claims brought under a CFA. This information is not collected centrally. It has been suggested by the liability insurance industry and other major defendant organisations in personal injury cases that CF As have contributed to the general increase in legal costs. There is also the fear of CFAs being challenged. And this has led to more costs and undue strain on the viability of businesses. No data has been forthcoming from the respondents to the consultation.

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16. CFAs are at risk of legal challenge. Defendant solicitors have brought legal challenges on the grounds that the CFA the claimant solicitors had entered into with their clients was materially breached. Different legal challenges may well focus on different aspects of the CF As, causing a rise in the number of cases being brought to court. Courts may also experience a rise in the number of claims on costs issues. No respondents commented or provided any data or further information on this subject.

17. Most respondents believed that consumers should have access to justice and that legal costs involved in bringing an action should be reasonable. Liability insurers are frequently paying out on legal costs and the success fee of a CFA. This has the knock-on effect of making insurance more expensive for everyone, which is particularly unfair on the vast majority of consumers who do not make a claim.

Options

18. The main options are:

Option 1 - Do nothing: make no changes to the CFA regulations

This option would retain the existing CFA regulations with their complexities, minimising the use of CFAs, denying access to justice to people with genuine claims, and hampering the development of CFAs as a preferred means of funding litigation.

Option 2 - Simplify the CFA regime

This option would replace the existing complex CF A and CCF A regulations with a simpler set of requirements contained in one set of regulations that would form the minimum statutory framework. Simplifying the CFA regime would also focus client care and contractual responsibilities in the Law Society's practice rules and costs information code.

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Option 3 - Revoke the existing CFA regulations

The consultation process has helped make it clear that simplification can be taken further than originally proposed by revoking the existing CFA regulations for all new cases and relying on primary legislation to provide the government legislative framework. Client care would be more appropriately and effectively covered in the law Society's Professional Conduct Rules. Regulations duplicating the requirements of the Law Society's Professional Conduct Rules would cease.

Benefits

19. Option 1 - Do nothing: There would be no clear benefits. The objective of making CFAs simpler, clearer and more transparent both for individuals and the solicitors would not be achieved.
20. Option 2 - Adopt the proposed changes to simplify the CFA regime: This option would remove the detailed client care and costs information requirements from the current CFA regulations. It would revoke the CFA regulations introduced in 2000 and replace them with one set of regulations for both CFAs and CCFAs. Lawyers and clients using CFAs in bringing claims should find the process easier and more straightforward.
21. Option 3 - Adopt the proposed changes to revoke the CFA regime: This option should make the process simpler for both lawyers and clients who wish to bring a claim. The proposed changes should also remove the lack of clarity and transparency from the CFA regime, build trust and confidence among the lawyers and small businesses using CFAs, maintain stability of CFAs and reduce legal challenges in the courts on CFAs and their application.
22. The bodies we consulted did not provide any quantification of the possible benefits the proposals would achieve. However, all welcomed the proposals to replace the existing CF A regulations with a simpler set of requirements making the regime more transparent. Overall there may be some marginal reduction in costs for small businesses because revoking the CFA regulations would remove a complex regime with its lack of clarity and transparency. The Small Business Service did not provide any information on the savings small businesses might experience.

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23. Many stakeholders from the legal profession have commented that generally simplifying the CFA regime would mean less expense and time for solicitors explaining the CFA - an average saving of one hour per case and, in terms of monetary value, approximately £150.00. The changes should also improve access to justice for claimants and defendants, as the regime should be less complicated.
24. The value of the benefit is difficult to quantify. Although information was invited from consultees as to the probable level of savings, none was received. We believe the removal of the regulations for new cases should enhance the benefits identified and be a major step towards better regulation. The removal of the regulations would also be consistent with the Better Regulation Task Force's current report *Regulations - Less is More. Reducing Burdens, Improving Outcomes* aimed at considering how Government can take deregulation much more seriously and boost the process of removing unnecessary and outmoded regulations.
25. Those benefiting from the proposals are as follows:

Main beneficiaries

- consumers
- the legal profession (solicitors and other legal providers)

Other beneficiaries

- advice agencies (in general)
- trade unions

26. For the consumers the proposed reforms would have the following benefits:

- Consumers would be able to receive clearer, more transparent, simpler and more accurate information from their solicitors and advisers about agreement on CFAs. This would help them make an informed decision about their claim.
- Consumers who are well informed are better able to make decisions based on the best option according to their circumstances and case. This is likely to reduce the number of consumers entering into agreements that they do not fully understand.

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27. The following benefits to the legal profession from the proposed reforms were identified:

- The current CFA requirements have led to some problems in their application and are difficult for solicitors to explain to clients. The legal profession believed that simplifying the current CFA regulations would reduce these problems and help to save time and expense - an average of one hour per case or approximately £150.00 per case. The proposed changes may lead to fewer cases being taken to courts on costs issues. We have consulted the departmental economists who carried out a forecasting of claims. They concluded that the number of cases going to courts had declined considerably since 2004 due to the effects of new costs rules relating to CFAs. Revoking the CFA regulations may further enhance the downward trend.

- Regulations governing the behaviour of solicitors and client care are duplicated in the Law Society's practice rules and costs information code. Removing the client care protection from the secondary legislation in favour of the Law Society's rules should make CFAs less susceptible to technical challenges from third parties.

28. For the advice agencies the proposed reforms would have the following benefits:

- The advice agencies have experienced a large number of cases where people with genuine claims have had difficulty in understanding the risks and liabilities they are exposing themselves to, as CFAs have not been clearly explained to them at the outset. The agencies also expressed their concerns about the ways in which claims intermediaries have exploited the CFA regime and pressured consumers through high-pressure sales tactics into agreements that they do not understand. The advice agencies believed that simplifying the CFA regime would reduce the number of customers entering into agreements which they do not understand and which may not necessarily be the best option for them. They also believed that simplifying the CFA regime would provide access to effective redress.

29. Trade unions would benefit from the proposal to remove the detailed client care and costs information required from the current CFA. Trade unions believed that the current CFA secondary legislation was unnecessarily complex and should be simplified.

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Costs

Business sectors affected

30. The legal profession (small and large firms), advice agencies in general, individuals and DCA are likely to be affected by the proposed changes wherever civil litigation involves the use of CFAs and CCFAs. If the proposal to revoke the regulations is adopted then the burden on these groups should be reduced. DCA will have to revoke the regulations to reflect the changes, and the costs will be marginal. Fewer cases will go to court on costs issues. DCA believe that the downward trend in the number of cases going to court will be accelerated if the CFA regulations are revoked. The Law Society will need to revise its Professional Rules to include the client care component.

31. Changes to policy wordings and the model conditional fee agreement may be needed.

Costs for a typical business

32. The changes should impose no new requirements or costs on legal practitioners. Respondents did not provide information about any new costs they thought might arise from the changes.

Equity and fairness

33. Option 1 - Do nothing: Duplication of regulating solicitors and client care will continue. Those solicitors wishing to use CFAs would still be required to adhere to both the CFA regulations and the Law Society's Rules. The existing CFA regime is complex. The difficulty solicitors have in explaining to clients the CFA regime would result in clients being less likely to fully understand the process and being misled. This imbalance between the legal profession and client would continue.

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34. Option 2 - Simplifying the CFA regime would mean solicitors would not have to spend as much time explaining the CFA to clients because it would be much simpler. Focusing client care and contractual responsibilities in the Law Society's Professional Conduct Rules and client care and costs information code would remove duplication and potential unfairness whereby the solicitor has to follow both the regulations and the Law Society's Rules.
35. Option 3 - Revoking the existing CFA regulations and minimising the statutory framework would result in parties concerned being better informed and clearer about the CFA process. This will create a level playing field between claimant and defendant lawyers as well as removing the unfairness to consumers who make poorly informed decisions. Revoking the regulations entirely would take this simplification to its ultimate conclusion and would be a major step in removing unnecessary legislation.
36. The proposals to revoke the CFA regulations will not affect any racial group unfavourably.

Compliance

37. It is believed that any compliance costs would be marginal. The legal profession currently complies with the existing CFA regulations and the Law Society's costs and information code. No figures or comments were received from the exercise, although further information on costing was sought as part of the consultation process.

Sensitivity analysis

38. The proposals are deregulatory and it is not anticipated that they will increase costs for businesses. Information to further improve assessment of the costs of the proposals was not forthcoming from respondents.

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Consultation with the Small Business Service

39. We have consulted with the Small Business Service (SBS) who agreed that reforms to the existing CFA regulations should favour small businesses. The SBS commented that clients (businesses, claimant and individual) would receive adequate legal information on claims before agreeing to sign any document. The SBS also commented that all legal advisers would be required to focus on client care and contractual responsibilities in the Law Society's practice rules and costs information code.

40. It is unlikely that small businesses would be affected by any increase in costs. We do not believe that revoking the existing CFA regulations would have any financial implication for small businesses. The SBS did not provide any information on costs to small businesses. Respondents did not provide any information about any cost implications associated with the proposed changes.

Competition assessment

41. It is not anticipated that Option 3 would have any impact on competition. The competition filter was completed and indicated no impact on competition.

Enforcement and sanctions

42. The Law Society regulates solicitors through the professional practice rules and costs information code and would therefore oversee conduct and compliance. Failure to comply with the rules may result in solicitors being subject to disciplinary action. If a CFA is not materially compliant with the Law Society's rules and model agreements the courts may find that a CFA is unenforceable and solicitors will lose their costs.

Monitoring and review

43. The Law Society would monitor the operation of the new set of rules. The operation of the proposal to revoke the CFA regulations would be reviewed three years after implementation.

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Consultation

44. The consultation paper was published on 29 June 2004 and closed on 29 September 2004. Forty responses were received. They included responses from the legal professions, the judiciary, Insurance industry, media organisations, trade unions and individual practitioners. In addition a round table event hosted by the DCA Minister was held on 8 July 2004. The event, attended by a range of key stakeholders, provided a forum to discuss the implications of the consultation paper.
45. We also consulted with other government departments and agencies including Cabinet Office, Department of Trade and Industry, Department for Work and Pensions. HM Treasury and Office of Fair Trading. HM Treasury responded favourably.
46. The consultation was also published on the DCA website at: www.dca.gov.uk
47. All but one of the forty respondents favoured the proposal to simplify CFA regulation and to move client care to the Law Society Professional Conduct Rules. One respondent felt that on balance it would be better to keep the existing regime.

Summary

48. The consultation paper *Making CFAs a Reality* (code CP 22/04) published on 29 June 2004 set out the Department for Constitutional Affairs' (DCA) proposals to reform the secondary legislation governing the operation of Conditional Fee Agreements (CFAs) and published a set of new draft regulations for consultation.
49. The changes would be achieved by a number of secondary legislation reforms within the existing primary legislative framework, which do not create or require any new primary legislation. These include removing the detailed client care and costs information requirements from the current CFA regulations, revoking the CFA regulations introduced in 2000 and replacing them with one set of regulations for both CFAs and CCFAs. We are working with the Law Society to ensure that appropriate revisions to the Law Society's practice rules and costs information code are made. The Law Society is also working on producing a new model CFA for solicitors' use. The new regime will come into force in November 2005.

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50. Legal representatives and clients using CFAs to bring claims should find the process easier and more straightforward. Advice agencies may experience a reduced number of customers approaching them for advice or help on bringing a claim under a CFA. Those who responded to the partial regulatory impact assessment commented that simplifying the CFA regime would mean solicitors would not have to spend as much time explaining the CFA to clients because it would be a much simpler document. The decision to revoke the regulations entirely will take this simplification to its ultimate conclusion and will be a major step in removing unnecessary secondary legislation.

Recommendation

51. We recommend Option 3 - the proposal to revoke the CFA regulations. This should make the process simpler for all parties concerned, remove lack of clarity and transparency from the CFA regime, and reduce legal challenges in the courts on CFAs and their application. Overall, the benefits of the proposal outweigh any costs and relieve all parties of the burden of the current regime's complexity.

Option	Costs to DCA	Total benefit per annum
1. Do nothing	A rise in the number of cases being brought to courts	Nil
2. Simplify the CFA regime	We will have to amend the CFA regulations to reflect the changes	and time for solicitors explaining the CFA Duplication removed
3. Revoke the CFA regime	Negligible - We will have to amend the CFA regulations to reflect the changes	and time for solicitors explaining the CFA removed Better informed customers going to courts Improved access to justice

Option 3 is recommended as this delivers the full set of proposals.

New Regulation for Conditional Fee Agreements (CFAs)

Declaration

I have read the regulatory impact assessment and I am satisfied that the benefits justify the costs.

Signed

Baroness Ashton of Upholland

Date 10 August 2005