**Council for Licensed Conveyancers**

**Application to the Legal Services Board**

**to issue an Exemption Direction**
**in relation to Compensation Fund contributions**
**for the period 2023-2024**

October 2023

**Background**

The CLC reviews its funding of the Compensation Fund annually. The Fund is funded through contributions by all regulated practices and is calculated as a percentage of the practice's turnover. The CLC is not proposing to make any changes to the Compensation Fund contribution arrangements last approved by the LSB in 2022. The next contribution period runs from 1 November 2023 to 31 October 2024.

The Council of the CLC has reviewed the position of the Fund and decided that it would not be appropriate to make changes to the existing funding arrangements as:

1. The Fund is sufficiently reserved in accordance with the reserving policy.
2. The Fund is currently generating a surplus.
3. Any reduction in the contribution rates or payment holiday this year would reduce the burden on practices but may result in additional cost in future years if reserve levels drop significantly in the short term.
4. Two large claims are nearing settlement and due to the uncertainty of the amount likely to be paid it is prudent to maintain additional reserves until they are finalized.
5. The CLC is aware of potentially significant investment property losses which may result in claims. Should these crystallise additional reserves may be required.
6. Leaving contribution rates unchanged this year reduces the risk of volatility in the fee rates in later years should large claims materialise.

As a condition of being issued with a Licence, all CLC Practices are required to contribute to the CLC's Compensation Fund in addition to paying the Practice Fee. The CLC sets the annual contributions at a level that is sufficient to fund the payment of grants and associated expenses of the Compensation

Fund. The CLC tracks expenditure against the budget throughout the year and at the half year point, forecasts expenditure for the remainder of the year and determines the funding requirement, and therefore the level of contributions required, for the following billing cycle which runs from 1 November.

**Overview of the Compensation Fund financial arrangements**

The Compensation Fund contributions levied on practices are calculated based on the practices' turnover and a sliding scale contribution rate as shown in Annex – A. The turnover bandings were updated in 2021 and were increased from 5 to 9 bands. This has created a better spread of practices and more effective tiering of contribution rates. This smooths the progression for practices as they move between bands on the basis of changing turnover.

The table below summarises the number of practices, fees collected and the percentage of total contribution by turnover band.

| Allocation of practice across turnover bands | Number of Practices | Fees per bandings | % of total contributions |
|---|---|---|---|
| £0 – £100,000 | 12 | 6,000 | 1% |
| £100,001 – £250,000 | 35 | 22,022 | 5% |
| £250,001 – £500,000 | 47 | 44,581 | 10% |
| £500,001 – £1,000,000 | 56 | 76,869 | 17% |
| £1,000,001 – £2,000,000 | 29 | 62,346 | 14% |
| £2,000,001 – £4,000,000 | 10 | 36,125 | 8% |
| £4,000,001 – £8,000,000 | 7 | 46,272 | 11% |
| £8,000,001 – £16,000,000 | 5 | 51,584 | 12% |
| £16,000,001 and over | 4 | 94,755 | 22% |
| | 205 | 440,553 | 100% |

The table below illustrates the contributions and percentage of turnover of the contribution for a range of practice turnovers. A minimum contribution has been set for practices with a turnover of £100k or less. This means that the smallest of practices pay more as a percentage of their turnover, however this rate drops significantly as a practice's turnover increases above £100k. The minimum rate was set to ensure that all practices make a meaningful contribution to the Fund, especially smaller practices which have historically resulted in additional cost or claims.

| **Illustration of Compensation Fund contribution payable** | | |
|---|---|---|
| **Practice Turnover** | **Compensation Fund Contribution** | **% of Practice Turnover** |
| £50,000 | 500 | 1.000% |
| £70,000 | 500 | 0.714% |
| £80,000 | 500 | 0.625% |
| £90,000 | 500 | 0.556% |

| Practice Turnover | Compensation Fund Contribution | % of Practice Turnover |
|---|---|---|
| £100,000 | 500 | 0.500% |
| £150,000 | 583 | 0.388% |
| £200,000 | 665 | 0.333% |
| £250,000 | 748 | 0.299% |
| £300,000 | 827 | 0.276% |
| £500,000 | 1,143 | 0.229% |
| £750,000 | 1,448 | 0.193% |
| £1,000,000 | 1,753 | 0.175% |
| £2,000,000 | 2,933 | 0.147% |
| £5,000,000 | 5,963 | 0.119% |
| £10,000,000 | 9,893 | 0.099% |
| £20,000,000 | 17,653 | 0.088% |

The CLC Compensation Fund contributions are ring fenced from CLC operations and they are used solely for the payment of costs relating to establishing, maintaining, administering, protecting and applying the Fund.

The table below summarises the forecast financial results and budget for the 2023 financial year. The budget does not include provisions for income and expenditure that by nature is difficult to determine the timing or value of. This includes aged balance receipts, Compensation Fund grants and new intervention costs. The CLC's approach is to run a budget that is sufficient to absorb the likely level of these costs and maintain reserves.

| 2023 Budget vs Forecast | 2023 Budget | 2023 Forecast | Var to Actual | % Var to Actual |
|---|---|---|---|---|
| Practice Contributions | 461,589 | 474,815 | 13,226 | 3% |
| Interest Received | 63,000 | 99,245 | 36,245 | 58% |
| Aged Balance Receipts | | 1,645,719 | 1,645,719 | - |
| **Income** | **524,589** | **2,219,779** | **1,695,190** | **323%** |
| **Expenses** | | | | |
| Intervention Support (3rd Party) | 4,000 | 31,397 | (27,397) | (87%) |
| Intervention Cost (Internal) | - | 8,525 | (8,525) | (100%) |
| Staff Cost Recharge | 132,459 | 132,459 | - | 0% |
| Legal Fees | 180,000 | 128,697 | 51,303 | 40% |
| Storage Costs | 57,600 | 59,097 | (1,497) | (3%) |
| File Request Costs | 5,960 | 5,004 | 956 | 19% |
| Compensation Grants | - | 3,139 | (3,139) | (100%) |
| Tax & Finance Charges | 11,981 | 16,872 | (4,891) | (29%) |
| **Total Expenses** | **392,000** | **385,189** | **6,811** | **2%** |
| **Net Surplus / (Deficit)** | **132,589** | **1,834,589** | **1,702,000** | **93%** |

The table below includes further information on the line items and budget variances for 2023.

| **Budget Line item** | **2023 budget vs forecast variance description** |
|---|---|
| Practice Contributions | Practice contributions are higher than budgeted due to recovery of arrears fees from a practice. |
| Interest Received | We received more interest than we budgeted for due to increasing interest rates. |
| Aged Balance Receipts | We do not budget for aged balance receipts due to the uncertainty in timing and amount of any aged balances that are received by the CLC. In the current year we have received a significant sum from a large practice and have forecast for a further receipt of £703k during Q4. |
| Intervention Support (3rd Party) | We only budget for intervention support when we have ongoing intervention work. We do not budget for possible future interventions as we cannot determine timing or cost thereof. We intervened into a practice in 2023 and these costs are included in the forecast for 2023. |
| Intervention Cost (Internal) | Direct intervention costs incurred by the CLC are included in this line, this can include post redirection, CMS subscriptions, travel and other incidentals incurred during and post intervention.<br><br>We did not budget for any cost as we had no ongoing interventions at the time the budget was set. The cost incurred in the forecast is a result of a new intervention during 2023. |
| Staff Cost Recharges | A portion of staff costs are allocated to the Fund based on the time being spent managing the Fund. The cost is based on the time spent by specific individuals that manage the operation of the Fund including claim management, updating rules and frameworks, making determinations, reporting and providing clients with files and wills. The charge is assessed regularly and is based on the level of activity. |
| Legal Fees | Legal costs are being incurred in relation to the administration of the Fund as well as on a project to update the Compensation Fund Operating framework rules and guidance. The costs incurred during the year have been lower than budgeted as some of the work has been done internally. Some claim related matters are moving slower than anticipated thereby reducing and delaying costs. |
| Storage Costs | Storage costs are the costs associated with the storage of closed practice paper files. The cost is lower than was budgeted due to the destruction of files during the year and lower than expected file request and courier charges (charged by the storage company). |

| | |
|---|---|
| File Request Costs | These are our costs to scan paper files and send them to clients. The cost is determined by the number of files requested by clients and postage/courier costs. |
| Compensation Grants | We do not budget for compensation grants due to the difficulty in determining the amount and timing of any claim. The variance is due to additional claims being provided for during the year. |
| Tax & Finance Charges | The CLC pays corporation tax on interest. The forecast charge has increased due to higher than budgeted interest receipts. |

The table below summarises the forecast figures for 2023 and the estimated figures for 2024.

| **2024 Estimate vs 2023 Forecast** | **2023 Forecast** | **2024 estimate** | **Var to Forecast** | **% Var to Budget** |
|---|---|---|---|---|
| Practice Contributions | 474,815 | 440,553 | (34,262) | (7%) |
| Interest Received | 99,245 | 108,696 | 9,451 | 10% |
| Aged Balance Receipts | 1,645,719 | - | (1,645,719) | - |
| **Income** | **2,219,779** | **549,249** | **(1,670,530)** | **(75%)** |
| | | | | |
| **Expenses** | | | | |
| Intervention Support (3rd Party) | 31,397 | 25,000 | 6,397 | 26% |
| Intervention Cost (Internal) | 8,525 | 10,950 | (2,425) | (22%) |
| Staff Cost Recharge | 132,459 | 151,187 | (18,728) | (12%) |
| Legal Fees | 128,697 | 180,000 | (51,303) | (29%) |
| Storage Costs | 59,097 | 55,200 | 3,897 | 7% |
| File Request Costs | 5,004 | 5,500 | (496) | (9%) |
| Compensation Grants | 3,139 | - | 3,139 | - |
| Tax & Finance Charges | 16,872 | 18,478 | (1,607) | (9%) |
| **Total Expenses** | **385,189** | **446,315** | **(61,126)** | **(14%)** |
| | | | | |
| **Net Surplus / (Deficit)** | **1,834,589** | **102,934** | **(1,731,656)** | **(1,682%)** |

The table below includes further information on the line items and variances.

| **Budget Line item** | **2023 forecast vs 2024 estimate variance description** |
|---|---|
| Practice Contributions | Practice contributions are expected to decrease in 2024 due to a reduction in practice turnovers. |
| Interest Received | We have based our estimate for 2024 on current interest receipts, any further rate increases will result in a positive variance in 2024. |
| Aged Balance Receipts | We have not included any aged balance receipts in the 2024 estimate as we have not been notified of any and we are not able to accurately predict the timing and amount of any payments made to the CLC. |
| Intervention Support (3rd Party) | We currently have one active intervention. We expect that the costs will continue into 2024 and have made provision for them. |
| Intervention Cost (Internal) | We currently have one active intervention and have estimated that we will need to continue the CMS subscription to support the practice closure for the duration of 2024. |
| Staff Cost Recharges | A portion of staff costs are allocated to the Fund based on the time being spent managing the Fund. The cost is based on the time spent |

| | |
|---|---|
| | by specific individuals that manage the operation of the Fund including claim management, updating rules and frameworks, making determinations, reporting and providing clients with files and wills. The charge is assessed regularly and is based on the level of activity.<br><br>The recharge for 2024 is expected to increase due to a planned cost of living adjustments to salaries. We have also included some additional cost allocations for staff who are involved in investigating and drafting compensation determinations. |
| Legal Fees | Negotiations for the settlement of two large claims are ongoing and we expect the work in relation to these claims to continue into 2024. We are also anticipating that we will need to do additional work on investment property claims during 2024. |
| Storage Costs | Storage costs are expected to decrease marginally due to the destruction of some files currently being held. |
| File Request Costs | File request costs are expected to increase during 2024 due to inflationary increases to postage and courier costs. |
| Compensation Grants | We do not budget for compensation grants due to the difficulty in determining the amount and timing of any claim. |
| Tax & Finance Charges | The CLC pays tax on interest. The estimated charge has increased due to higher interest receipts. |

The CLC reserving policy allows for various reserves to ensure that the Fund is sufficiently resourced to execute its mandate. The target reserve levels as at July 2022 are shown in the table below.

| **Compensation Fund Reserves** | **Reserve Totals** |
|---|---|
| Minimum reserve | 2,000,000 |
| Probable claim reserve | 2,385,716 |
| Insurance reserve | 2,000,000 |
| Contingency reserve | 651,817 |
| **Target reserve level** | **7,037,533** |

It is the CLC's policy to allow reserve levels to be up to £500,000 more than the target level before any action is taken to reduce reserve levels and/or the accumulation of additional reserves.

The cash flow forecast based on the forecast and estimate outlined above result in the following estimated reserve levels for 2023.

| **Estimated Reserve Levels** | £ |
|---|---|
| **Cash reserves at 31 August 2023** | **7,747,586** |
| Net Cash receipts from operations | 735,714 |
| **Cash reserves at 31 December 2023** | **8,483,300** |
| Net Cash receipts from operations | 84,455 |
| **Cash reserves at 31 December 2024** | **8,567,755** |

Reserve levels at the end of 2024 will be approximately £1m higher than the reserving policy target (including the £500k buffer). A reduction in fee rates or payment holiday was considered to reduce the reserve balances during the next license year. It was however decided not to adjust fee rates this year as:

1) Two large claims are nearing settlement, there is some uncertainty as to the ultimate settlement cost which could be higher than has been forecast.
2) There is a possibility that Investments property claims will be made in 2024 which could require a significant provision.
3) Because of the uncertainty outlined above we do not want to reduce reserve levels in 2024 and then have to increase them the following year.

**Summary of consultations results**

The annual CLC Fee consultation was launched on 5 August and ran for 6 Weeks. The consultation was promoted in newsletters, the press and sent to key stakeholders. We also gave respondents the option to submit a quick response via an online survey rather than responding in full to the consultation document. The CLC reminded representative bodies about the consultation towards the time of its closure and received a response from one.

89% of the respondents (15 of 18 responses) agreed that the Compensation Fund contribution rates should remain unchanged. Four respondents provided comments. The key concerns raised were:

a) One respondent queried whether any Compensation for investment property claims would be paid by the regulated community, or if it would be paid by the firms involved.

*Should PI insurance not cover such claims, the claimant may make an application for a Compensation Fund grant which will be considered against the Funds rules.* The CLC's Compensation Fund Policy Statement on the CLC's website explains, at paragraph 13, *'The core purpose of the Fund is to answer to claims made by individuals or small businesses which arise from regulated conveyancing and probate transactions. The further a claim departs from this core purpose then the less likely the Fund will make a grant or that if it does, that the claim will be met in full. In particular the Fund is less likely to answer to claims involving speculative activities even though there may be a property or probate element.'*

b) Another respondent noted that any fee has an impact on the profitability of a firm.

This is undoubtedly true, however we are not proposing any increase in the Compensation Fund Contribution rates. Additionally, the contribution rates were cut by 60% in 2019.

We continue to monitor the financial needs of the Fund for the delivery of consumer redress within the terms of the scheme and will reduce contribution rates again should it be warranted.

The CLC considered the consultation responses and determined that there was no material objection by respondents to keep the fee rates unchanged for 2024.

**Significance, Impact and Risk Assessment**

To support our application for an exemption direction we have included the assessment of the significance, impact and risks of the proposed changes in the tables below.

| Significance Assessment | | |
|---|---|---|
| | **Criteria** | **CLC assessment** |
| 1 | Would the change require approval under the previous Ministry of Justice /<br>Legal Service Consultative Panel system? | No changes to the regulatory arrangements are being proposed. |
| 2 | Is there a direct impact on or synergy with the Regulatory Objectives as detailed in Part 1 of the Act? | A review of impact and synergy with the regulatory objectives is included below:<br>**RO1 Protecting and promoting the public interest** – Promoted, the Fund may provide a means for enabling recovery when others are not available.<br>**RO2 Supporting the constitutional principles of the rule of law** – neutral, although the Fund may provide a means for enabling recovery when others are not available.<br>**RO3 Improving access to justice** - neutral, although the Fund may provide a means for enabling recovery when others are not available.<br>**RO4 Protecting and promoting the interest of consumers** – promoted, the Fund may provide a means for enabling recovery when others are not available.<br>**RO5 Promoting competition in the provision of services** –<br>i. the Fund enhances the reputation of the profession - it may provide a means for enabling recovery when other means are not available.<br>ii. contributions are maintained at the minimum level required so that the costs of regulation are as low as is reasonably required for the purpose for which the Fund is maintained.<br>**RO6 Encouraging an independent, strong, diverse and effective legal profession** –<br>i. the Fund enhances the reputation of the profession - it may provide a means for enabling recovery when other means are not available.<br>ii. contributions are maintained at the minimum level required so that the costs of regulation are as low as is reasonably required for the purpose for which the Fund is maintained so that costs are not a barrier to entry thereby enhancing diversity of the profession. |

| | | |
|---|---|---|
| | | **RO7 Increasing public understanding of the citizen's legal rights and duties** – neutral.<br>**RO8 Promoting and maintaining adherence (by authorised persons) to the professional principles** – promoted, not increasing the Compensation Fund contribution amounts to a reduction in real terms and is less burdensome to CLC regulated practices. |
| 3 | Is the change consistent with the Better Regulation Principles? | The CLC believes that it has fulfilled the better regulation principles as set out at s.28 Legal Services Act 2007.<br><br>a. It is transparent in that it has consulted on the proposed changes and an explanation about the contributions CLC practices will each be required to make to the Compensation Fund will be sent to each practice.<br>b. It is accountable in that its Annual Financial Statements include a report on the Compensation Fund income and expenditure.<br>c. It is consistent in that contributions to the Compensation Fund are determined by a contribution method that has not changed in 10 years (levied as a percentage of turnover)<br>d. It is targeted in that the Compensation Fund contributions are determined by reference to the turnover of CLC practices. However, the minimum contribution to the Compensation Fund of £500 continues on the basis that as a class small practices give rise to a disproportionate level of grants after they have closed when compared with the contributions they have made whilst licensed by the CLC. |
| 4 | Will the change require a statutory instrument and / or parliamentary time in<br>order to be completed? | The proposal does not require a Statutory Instrument or Parliamentary time in order to be completed. |
| 5 | Has there been activity in relation to changing the regulatory arrangement in<br>the past two years for example an application made under the previous system, change considered by internal Board, consultation with regulated<br>community or others? | The Council has considered the demands on the Fund, reserving levels and burden on the regulated community.<br><br>The proposal not to amend the regulatory arrangements and specifically the contribution rates has been consulted on. |
| 6 | How much interest in the alteration is there within the Justice system and therefore how much is the confidence of those with an interest in the Justice system likely to be impacted by the alteration? | The requirement is for the CLC to set the contributions at the appropriate level. In the CLC's view the proposal will not impact on the Justice system and there will be no interest in any changes. |

| Impact Assessment | | |
|---|---|---|
| | **Criteria** | **CLC assessment** |
| 7 | The number and proportion of people (consumers, procurers, regulated community) that will be affected by the alteration? | CLC practices will be impacted directly in that the costs of regulation will be unchanged. |
| 8 | Is there an anticipated impact on the ability of members to practise, operate effectively, make a profit, and earn a livelihood? | There will be no impact as the contribution is variable, based on levels of turnover. The contribution as a percentage of turnover is at most 1%. |
| 9 | Will the change affect the ability of or requirements for prospective members to enter and/or operate effectively within the regulated community? | The proposed amendments will have no impact on prospective members wanting to become CLC regulated as there will be no changes to the method of determination or quantum of the collection. |
| 10 | Is there any crossover and / or conflict with other bodies regulating the same area or person? Are there differences in standards (standards must be comparable not necessarily the same)? | The CLC's Fund is parallel to those managed by other regulators which have Compensation Fund arrangements in place, though no specific conflict as the various funds cover only those practices within each regulator's ambit. The CLC's Compensation Fund arrangements derive from s.21 Administration of Justice Act 1985. In the CLC's view, the proposal to maintain contribution rates to the CLC's Compensation Fund at their current level is not an issue likely to give rise to regulatory conflict. There appears no reasonable prospect in the short terms to further harmonise compensation fund arrangements with other Approved Regulators. |
| 11 | The number of alterations included within the application. | There are no proposed amendments in this application. |
| 12 | What are the integrated consumer protection and competition impacts? Will the proposed alteration result in the addition of regulation or the removal of regulation (as opposed to a neutral amendment to existing regulation)? | Whilst the Fund itself promotes the consumer interest by providing an extra level of possible recompense, this particular proposal is neutral to consumer protection and competition impacts as it proposes maintaining the status quo. |

| Risk Assessment | | |
|---|---|---|
| | **Criteria** | **CLC assessment** |
| 13 | Previous track record of the AR in competently making changes that have been fully consulted on and the impacts fully assessed. | The CLC keeps the Compensation Fund under review throughout the year. The CLC has consulted on the proposal and assessed the impact of the proposal.<br>Previous changes to the contribution arrangements have not resulted in any unintended consequences or volatility. |
| 14 | How transparent and robust are the internal processes that the AR will follow in making changes? | The processes used to determine the contribution rates are established and have not been amended in recent years.<br>The process and impacts are outlined in full in our application. |
| 15 | Is there a high level of good quality data and evidence to support / justify the making the change? | The CLC has comprehensive financial and claim information in relation to the Fund. This data is used to determine the contributions required, reserving levels and expected expenditure. We are comfortable that this data is sufficient to make an informed judgement in relation to required contribution levels, reserves and expected expenditure levels. |
| 16 | How many would be impacted how quickly (immediacy of impact)? | There will be no impact on any identifiable group as the contributions rates and turnover banding remains unchanged. |
| 17 | If the change did not go ahead, what would the impact be? | No changes are being proposed. |
| 18 | How and when does the AR plan to assess the impact of the change following its introduction? What action would be taken if the benefits were not realised?<br>Has consideration been given to whether there is need to include a defined sunset clause? | The changes are expected to be neutral and we do not expect any financial or administrative changes. We monitor performance against plans and budgets closely and any variance is assessed against the achievement of these plans and budgets.<br>The contribution rates are assessed annually, and if necessary amended based on claim levels, reserving and planned and past expenditure.<br>A sunset clause is not relevant to this application. |
| 19 | Has there been activity in relation to changing the regulatory arrangement in the past two years (see paragraph 5)? | The Compensation Fund contribution rates have only changed once since 2011, with contribution rates being reduced by 60% in 2019. The Council approved this reduction to reduce the financial burden on practices and to reduce the accumulation of reserves.<br><br>The turnover banding was amended in 2021, this resulted in an adjustment to the Fee rate to keep contributions in line with contributions before the change. |
| 20 | If the change introduces regulation, does the AR have the capability of identifying breaches and providing / ensuring appropriate remedy and / or enforcement (see paragraph 12)? | This proposal introduces no new regulation. |

# ANNEX – A

## Compensation Fund contribution rates

| COMPENSATION FUND (2023-24) | | | | |
|---|---|---|---|---|
| **Turnover Banding** | **Compensation Contribution payable** | | | |
| £0 – £100,000 | £500 | | | |
| £100,001 – £250,000 | £500 | plus | 0.165% | of turnover in excess of £100,000 |
| £250,001 – £500,000 | £748 | plus | 0.158% | of turnover in excess of £250,000 |
| £500,001 – £1,000,000 | £1,143 | plus | 0.122% | of turnover in excess of £500,000 |
| £1,000,001 – £2,000,000 | £1,753 | plus | 0.118% | of turnover in excess of £1,000,000 |
| £2,000,001 – £4,000,000 | £2,933 | plus | 0.112% | of turnover in excess of £2,000,000 |
| £4,000,001 – £8,000,000 | £5,173 | plus | 0.079% | of turnover in excess of £4,000,000 |
| £8,000,001 – £16,000,000 | £8,333 | plus | 0.078% | of turnover in excess of £8,000,000 |
| £16,000,001 and over | £14,573 | plus | 0.077% | of turnover in excess of £16,000,000 |