**Proposed Draft Guidance on D5 (As revised)**

**General Comments**

The legislative and regulatory framework in Scotland currently only permits corporate bodies to do legal work reserved to solicitors where the body is an ‘incorporated practice’ recognised as such by the Society.

Rule D5 sets out how to apply for recognition – and the requirements which must be met to obtain and retain recognition.

*Management and Ownership and Control Restrictions*

The 1980 Act (section 34(1A)) imposes restrictions on who may manage, control (and be a member of) an incorporated practice. There are also Society practice rules (e.g. those at Rule D2) which restrict those who may be managers in any practice unit (as those terms are used in the practice rules – i.e. sole practitioners; partners in a traditional partnership which is a firm of solicitors; members of a limited liability partnership which is an incorporated practice; directors and shareholders of a company which is an incorporated practice).

The combination of those legislative and regulatory requirements means that all of those who are managers of an incorporated practice must be either:

* Solicitors holding valid unrestricted practising certificates issued by the Society (and who meet any other requirements which apply to them under the rules at D2, e.g. the experience requirements at D2.1.3, if applicable);
* Registered foreign lawyers (RFLs) registered with the Society (if there are RFLs amongst the managers the incorporated practice will also have to comply with the legislative and regulatory requirements on multi-national practices – see Rules D7, D8 and related material. Note, in particular, that there must, at all times, be at least one manager with a valid unrestricted practising certificate issued by the Society as above);
* Registered European lawyers (RELs) registered with the Society – see Rule D6 and related material. The inclusion of an REL manager does not trigger the requirements re multi-national practices but there will still need to be at least one Society PC holder, as above;
* Another incorporated practice recognised by the Society[[1]](#footnote-1).

No other categories of person or entity can hold any ownership or control interest in, or manage, a body recognised as an incorporated practice.

The purpose of many of the rules at D5 is to ensure that only those within the permitted categories seek to own, control or manage an incorporated practice – and that there is always at least one person within those categories available to manage the business.

*Permissible Structures*

An incorporated practice can be a company or a limited liability partnership. The Society acknowledges that the relevant legislation permits the formation of a company which has only one natural person as sole director and sole shareholder – and permits the formation of a limited liability partnership where the minimum 2 members are one natural person and a company, even if that same natural person is the sole director and sole shareholder of the company. However, the Society stresses that there are risks associated with adopting such a structure which require careful consideration and management.

*Risk Management*

The Society will seek evidence that anyone seeking to set up an incorporated practice which is reliant on one individual for its ability to practice in accordance with legislative and regulatory requirements has taken appropriate measures to manage and mitigate the associated risks. Those risks may include the individual ceasing to be able to practise, either as a result of ill-health or due to suspension, withdrawal or restriction of the individual’s practising certificate – which can be triggered by a variety of circumstances related to health, financial position, conviction for certain offences, failure to comply with accounts rules or disciplinary action, for example.

Where there is no individual permitted to manage and control an incorporated practice actually exercising that management and control the Society may have no option but to revoke the recognition of the incorporated practice which has very serious consequences for the business, its owners and its employees and, most importantly, can have a significant adverse impact on its clients. If the practice has a client account, the ability to operate that account can cease immediately on the occurrence of the event which triggered the cessation of the relevant individual’s ability to practise, leaving clients unable to access funds. The Society does not have an automatic, effective and reliable right to intervene to resolve such issues. It may be possible for the Society to seek the appointment of a judicial factor – but the availability of that remedy depends on the circumstances. Pursuing this remedy can involve the Society (and hence the profession) in considerable expense which may be disproportionate to the sums at issue – but cannot be avoided if clients’ interests cannot otherwise be protected.

The practice rules require all solicitors to act in the best interests of their clients, not permit their own personal interests to influence advice to, or actings on behalf of, clients and to deal with the Society in an open, timely and co-operative manner, so as to enable the Council to properly exercise and fulfil its regulatory functions. The Accounts Rules obviously impose a number of specific obligations which are of relevance, including the requirement to ensure that all client money held in a client account is available when required by the client or for the client’s purpose.

Breaches of such rules can have serious disciplinary consequences and solicitors are expected to take appropriate and effective measures to prevent breach and protect clients’ interests. This includes taking all possible steps to ensure that clients’ interests will be protected in the event of a manager of the incorporated practice losing the ability to manage and control the practice.

Appropriate measures to mitigate risks and protect clients may obviously vary depending on the circumstances. The risk of there being no available individual able and permitted to manage and control an incorporated practice may obviously diminish where the incorporated practice has a number of managers in place – but the risks may not disappear altogether. All the managers of an incorporated practice may share personal responsibility for certain liabilities of the business by way of personal guarantees, for example, and hence they could all face the risk of personal sequestration in the event of financial difficulties originating with the business. The Society therefore needs to see evidence of an appreciation of risks and the adoption of appropriate mitigation measures from all those who seek to operate as incorporated practices, but understands that what measures are appropriate will vary with the circumstances.

1. The rules make certain provision for executors of deceased solicitors etc but an executor cannot exercise voting rights [↑](#footnote-ref-1)