

■ The role of the COLP

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How can the role of compliance officer for legal practice (COLP) be effectively carried out when outcomes-focused regulation (OFR) becomes a reality for law firms on 6 October this year?

COLP is defined in Chapter 14 of the new Code of Conduct as meaning 'the compliance officer for legal practice in accordance with rule 8.5 of the SRA Authorisation Rules' (which rules, like the Code of Conduct, are part of the SRA Handbook); and, in relation to an alternative business structure (ABS), COLP means 'a reference to its Head of Legal Practice within the meaning of the Legal Services Act 2007' (LSA).

The idea of having such a compliance officer originated in the LSA where it is provided in para. 11(2) of Sched. 11 to that Act that an ABS must at all times have an individual who is designated as head of legal practice (HoLP) and whose designation is approved by the licensing authority (which will be the Solicitors Regulation Authority (SRA)).

Section 91 of the LSA sets out the duties of the HoLP which include, inter alia, that the HoLP of an ABS must take all reasonable steps to ensure compliance with the terms of its licence and, as soon as reasonably practicable, report to the licensing authority any failure to comply with the terms of the licence, although not the terms of the licence under para. 20 of Sched. 11 (accounts) which are within the duties of the head of finance and administration (HoFA). Having a senior individual as a compliance officer to carry out this function is an understandable safeguard in relation to ABSs, where it is likely that large organisations will in future own law firms. In such cases the regulator will need to be able to look to an individual who values his or her reputation, career and pocket sufficiently to ensure compliance, and not just look to the owner organisation itself which may have deep pockets to pay any large penalties levied on it for compliance failures.

However, the role of the HoLP and the HoLP's duties in relation to ABSs have been extended by rule 8.5 of the Authorisation Rules to all types of law firms regulated by the SRA (and now renamed COLP). As a result, there is currently much discussion in law firms as to which individual in a firm is going to be the COLP and how the duties of the COLP can be effectively carried out.

Under rule 8.5 a law firm must at all times have an individual who is a manager or an employee, who is designated as its COLP, who is of sufficient seniority and in a position of sufficient responsibility to fulfil the role, and whose designation is approved by the SRA, if it is satisfied that the individual is a suitable person to carry out these duties. The COLP must be a lawyer of England and Wales (as that term is defined in Chapter 14 of the Code) or a registered European lawyer. As for the COLP's responsibilities, he or she must take all reasonable steps:

- to ensure compliance with the terms and conditions of the firm's authorisation except any obligations imposed under the SRA Accounts Rules (which fall within the scope of the responsibilities of the compliance officer for finance and administration (COFA));
- to ensure compliance with any statutory obligations of the firm, its managers, employees or interest holders in relation to the firm's carrying on of authorised activities; and
- to record any failure so to comply and make such records available to the SRA on request.

The COLP must also, as soon as reasonably practicable, report to the SRA any failure so to comply which is material either taken on its own or as part of a pattern of failures so to comply.

The guidance notes to rule 8.5 make it clear that the existence of the COLP in a firm and the requirements on the COLP to ensure that the firm, its managers and employees are complying with regulatory arrangements are not a substitute for the firm's and managers' responsibilities and their obligations under rule 8.1, which provides that a firm must have suitable arrangements in place to ensure that its managers and employees comply with the SRA's regulatory arrangements. This does somewhat beg the question as to why, if a firm and all its partners can in any event be called to account, it is necessary to put a specific responsibility on one individual?

The COLP must be of sufficient seniority and in a position of sufficient responsibility to fulfil the role

It is clear that the provisions of the Code and Authorisation Rules when they come into effect on 6 October this year will mean that the responsibilities of a COLP will in many law firms be onerous, if not unworkable, given existing 'cultures' within firms and the absence of any real notion of accountability on the part of partners. Accountability in this context means the willingness of partners to be managed and to put the interests of clients and the firm before any personal agendas. How often are managing partners still being told by other partners: 'You can't tell me what to do - I'm as much an owner of this firm as you are!'

Accordingly, and notwithstanding the provisions of rule 8.5 which state that a COLP must be of 'sufficient authority and in a position of sufficient responsibility to fulfil the role', how likely is it that COLPs will in many law firms really be able to effectively fulfil the role and not put themselves and their firms at risk of non-compliance?

The notion of accountability is still not universally accepted in many firms. However, it is central to a COLP being able to fulfil the role satisfactorily. Compare that with large corporate organisations (the type which are likely to establish ABSs) where clear lines of reporting and responsibility will already exist and where the need for such a compliance officer is likely to be readily understood, accepted and implemented.

From speaking recently to managing partners of a number of law firms (managing partners are arguably the right people to carry out the COLP role), it is clear that there is some reluctance on their part to become the COLP. Some are, however, turning this to their advantage and using the introduction of COLPs as a means to deal with the lack of accountability on the part of partners. As one experienced managing partner said to me recently: 'I have told my partners that if I have to do the job, then we are first going to have a very serious debate within the partnership as to how this firm will be managed in the future!'

Ensuring compliance with the 10 principles and 87 outcomes in the Handbook will be a full-time role

Others I have spoken to are intending to have agreements in place between themselves, as COLPs, and their firms and their partners to contractually require that the firm and each of the partners will do everything required to enable the COLP to effectively carry out the role. Some are also seeking indemnities against potential liabilities on COLPs in the event that a firm and its partners breach their obligations under such agreements.

However reluctant or otherwise some managing partners and others may be to take on the COLP role, how will they be able to make it easier for themselves and their firms not only to be compliant, but also to be able to demonstrate to the SRA that the mandatory outcomes required by the Code are actually being achieved?

Given that the role of the COLP will be to take all reasonable steps to ensure full regulatory compliance, the role will not be something to be done in odd moments between doing client work. Ensuring compliance with the 10 principles, the 87 outcomes and all the other rules and provisions in the SRA Handbook will arguably be a full-time role. Large firms will already have full-time risk and compliance officers who themselves are likely to have teams reporting to them. At the other end of the spectrum, how can small and medium-size firms with only limited resources realistically deal with the COLP role in a satisfactory and compliant manner?

The scale of the task facing the individual becomes clear when we look at examples of some of the widely drafted mandatory outcomes which illustrate the mountain COLPs will have to climb:

'You have effective systems and controls in place to achieve and comply with all the Principles, rules and outcomes and other requirements of the Handbook, where applicable' (outcome 7.2 of the SRA Code of Conduct 2011).

'You identify, monitor and manage risks to the achievement of all outcomes, rules, Principles and other requirements in the Handbook if applicable to you and take steps to address issues identified' (outcome 7.3 of the SRA Code).

How many law firms can say that they would currently achieve and be able to demonstrate achievement of these mandatory outcomes?

The COLP will be under an obligation to report to the SRA as soon as reasonably practicable any material failure to achieve such outcomes and the guidance notes to the Authorisation Rules make it clear that it is not sufficient just to put right a failure – there is still an obligation to report that failure. Of concern to many, if there is a failure to report, are the likely personal consequences (including financial penalties) for the individual. Access by the COLP to detailed knowledge of what is happening in every nook and cranny of a firm will be required if the role is to be performed effectively and with personal safety. How will COLPs be able to decide or to take a view on what is or is not a material failure to comply? In particular, will COLPs have to check (with hindsight) every known failure to comply in order to establish whether there has been a pattern of failures, none of which if taken on its own is material, but taken together would be material and require reporting?

One of the most difficult issues is whether a COLP will be able and prepared to take a view on a failure to comply, in the face of opposition to reporting by fellow partners, and risk disciplinary action? Serious conflicts and stresses and strains are likely to arise in partnerships in such circumstances. Set out below are some thoughts on how firms (and COLPs in particular) might approach OFR.

First, the guidance notes to rule 8 of the Authorisation Rules make mention of a 'compliance plan' and at the outset a firm and its COLP should, given the limited resources available to many firms, consider carrying out a cost-benefit analysis to establish the most resource-effective method of constructing a compliance plan. For example, should compliance management be resourced:

- by partners on a part-time basis, which is unlikely to make for good compliance or financial sense, or by bringing in a full-time professional to assist the COLP as part of a compliance team?
- using an existing practice management system or by buying in bespoke or off-the-peg IT software, as a tool to use to systemise compliance management procedures?

Second, COLPs will need, in particular, to manage their firm's knowledge if they are effectively to get to grips with compliance management. Unless COLPs have full knowledge and understanding of the risks arising from non-compliance then it will not be possible adequately to manage those risks and compliance obligations. Failure to manage knowledge is itself a major risk to law firms.

How many law firms sufficiently understand the nature and extent of the risks they are running from non-compliance to enable them adequately to manage those risks? COLPs should ask themselves questions such as:

- Where in our firm does knowledge of our compliance risk areas reside?
- Can we access that knowledge?
- Do we have systems to maintain and upgrade our knowledge?

Next, one of the main questions for a COLP in relation to managing compliance under OFR, given the wide scope of the mandatory outcomes is: where to start?

I would suggest that a systematic approach is needed which incorporates, for example, some of the following:

- it should be management driven from the top so that managing compliance risk has (and is seen to have) management buy-in and is adhered to by everyone throughout the firm;
- 'zero tolerance' is required – there can be no exceptions;
- managing compliance risk should be seen as 'everyone's job';
- a 'no guilt' culture throughout the firm should be developed to encourage disclosure where there are failures to comply;
- investment is made in training and education programmes to build awareness and to change mindsets throughout a firm;
- a continuous process of challenging the effectiveness of current levels of compliance procedures is implemented.

Above all, this systematic approach will enable the firm and the COLP:

- to put in place a formal compliance management process to identify and manage every area of compliance and risk; and
- to establish a comprehensive database covering all areas of compliance risk.

The advantages of a formal compliance risk management process are that it will:

- provide a structured approach to prioritise effectively and focus on the most appropriate compliance risk areas;
- demonstrate the effectiveness of a firm's compliance risk procedures in relation to achieving preset outcomes;
- ensure continuous monitoring which should mean that the management of compliance is 'lived' on a day-to-day basis; and
- provide comfort to professional indemnity insurers in relation to how effectively a firm manages its compliance and other risks.

At the outset, if adopting this approach, compliance risk issues will need to be identified by the COLP. This process will need to be management driven and is likely to involve 'top down/bottom up' brainstorming sessions to identify and assess compliance risks by asking:

- Are we compliant in every area?
- How will we achieve all the mandatory outcomes required by the Code and appropriate to the firm?
- Do we have gaps in the achievement of outcomes?
- What will we need to do to fully comply?
- To what standards should we comply?
- How can we monitor on a regular basis whether and the extent to which we are achieving outcomes?
- How should we prioritise our efforts?

Finally, how can using an IT system assist a COLP in this process? IT is not a panacea for all the ills of managing compliance risk: it is merely a tool. IT can, however, be a very powerful tool which, with careful planning and by integration with a firm's compliance procedures, help to:

- create and maintain a central and up-to-date compliance risk database providing access to all who need it in relation to exposure to risk;

- embed compliance risk management procedures and controls into the way the firm is operated (an example of this is where IT is already widely used to manage and control compliance with client inception procedures); and
- streamline identification, assessment, monitoring and reporting in relation to compliance risk management.

Some of the mandatory outcomes in the new Code would appear to break new ground compared with what has hitherto been regarded by lawyers as 'professional regulation'. As a consequence, many law firms will now need urgently to reappraise how they should be managed if the COLP is to carry out his or her duties in a satisfactory manner.

Some of the mandatory outcomes appear to break new ground

In this regard, one issue of concern is whether, given the nature of the responsibilities which will be imposed on the COLP, there will be people willing in the future to take on senior management roles in law firms? The unintended consequence of the COLP role, far from improving the management of law firms, may be that it is going to be even more difficult to find good quality managers to run law firms in the future.

Some law firms, even currently, find it difficult to identify good managers capable of successfully building strong businesses to meet the challenges ahead. Even where there are partners in a firm who have the potential to be good managers, they may well have second thoughts about accepting, at age 40 or 45, a management role for a limited period of say three or five years which requires them to give up a secure client practice. Now, in addition, there is the COLP role, which is likely to present a new hurdle to even more good quality, potential managers who may well be deterred by the prospect of not being able to get their partners to accept that sensible compliance will be good for a firm and, in the process, also expose themselves to potential regulatory liability.

Individuals are only likely to be able to carry out the COLP role satisfactorily and compliantly if the principle of accountability on the part of partners is universally accepted in law firms. However, issues such as accountability of partners and their unwillingness to be managed are usually cultural in nature and not necessarily capable of being dealt with solely by regulation. In a law firm, it is generally the position, as many managing partners will tell you, that 'you have to take your partners with you'.

How workable the role of the COLP will in practice be, as the SRA seeks to use COLPs to 'police' law firms, remains to be seen.

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