Protecting the users of legal services: balancing cost and access to legal services

SRA consultation
March 2018

June 2018

Our questions in full

We are keen to hear your views on our changes to PII and the Compensation Fund.

An uninterrupted list of our questions is below.

Introduction

The Birmingham Law Society is the largest provincial local law society representing some 4,500 solicitors and is currently celebrating its bicentenary. This response has been prepared by the Society's consultation committee with input from the property committee. The consultation committee is a truly representative mix with a spread from a sole practitioner through to an international firm with multiple offices around the world and within the jurisdiction. The senior officers of the Society have read and approved the response which is the collective view of all those who have participated in the consultation.

To entitle this paper "Protecting the users of legal services" is disingenuous. None of the proposals in this paper increase or maintain protections for the users of legal services. The reverse is true – all of the proposals significantly reduce the protections available to clients and as a result damage the standing of the profession.

In relation to professional indemnity insurance, compulsory cover will be reduced for commercial clients from the current £2m (or £3m for incorporated practices) to nil. Compulsory cover for other clients will be reduced to £500,000 or £1m for conveyancing.

In relation to the Compensation Fund, clients will be excluded from making a claim on the Fund if their assets exceed £250,000 which could have perverse consequences. Also the maximum level of payments from the Fund would be reduced from £2m to £500,000.

The SRA consulted on a proposal to reduce compulsory cover to £500,000 in 2014 so this is a repeat of the same consultation. There has been no call from insurers or from the profession for any changes. Professional indemnity insurance has never been as cheap as it is now. To contend that premiums will be reduced as a result of the changes and that clients will benefit from costs savings is fanciful. The clamour for change is created unilaterally by the SRA in pursuit of its own agenda based upon internally generated ideas for the future structure of the profession.

Certainty and simplicity should be the key guiding principles here for the profession and for its clients. These proposals do nothing to enhance the reputation of the profession or protect its clients and should be abandoned as they were in 2014.

The Birmingham Law Society is vehemently opposed to the SRA's proposals and supports the representations made by the Law Society. The SRA is yet again seeking to sacrifice client protections upon its own altar of change.

Question 1: To what extent do you think the proposed changes to our PII requirements provide an appropriate minimum level of cover for a regulated law firm?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree - **strongly disagree**

Please explain your answer

The present arrangement means that clients are guaranteed a minimum level of cover (£2m or £3m) from the date that the retainer is entered into until completion of the work and from completion of the work until the date that a claim is made upon the insurance within the relevant limitation period.

If these changes are made it means that the firm could have adequate cover at the date of the retainer but by the time the claim is made it could have reduced its cover significantly meaning that the loss is uninsured. How can such a change be in the clients' best interests? Firms would have to pay for top-up cover for all existing clients for some years to come which would defeat the SRA's stated aim of saving money.

The SRA figures do not withstand close scrutiny. For example, the consultation paper states that 98% of claims would be covered by £500,000 cover. In fact, it is 98% of the premium that comes within £500,000 so only a minimum saving could be achieved.

Also, the figures that the SRA uses to support the case for change do not include figures from insurers that have already left the market because of expensive claims. The figures are therefore distorted in favour of the SRA's proposals.

As stated above, the minimum cover of £500,000 is too low for most firms so top-up cover will need to be purchased. Any saving may therefore be illusory. The firms most likely to need additional cover will be the firms that fail to purchase that cover.

A small firm is not necessarily well run and is not necessarily a good risk. Making a case for change based upon the cost to small firms is intellectually disappointing.

In addition, there are more general questions over the data that has been used. It was provided anonymously and voluntarily by the majority of insurers currently operating in the market. It accounts for 75% of insurance policies over a 10-year period beginning in 2004. It therefore does not include figures from 2014 to date and therefore excludes the changing market over the last four years.

Also, the SRA is intending to eliminate the differential level of cover for incorporated practices (£3m for limited companies at present). The SRA appears to have ignored the

principle of limited liability. In our view this is further evidence of yet another reduction in client protection.

Question 2: To what extent do you agree that our minimum PII requirements do not need to include cover for financial institutions and other large business clients?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree **– strongly disagree**

Please explain your answer

At present, commercial clients can instruct any law firm in England & Wales confident that each firm would have minimum cover of £2m (or £3m for limited companies). Many of these commercial clients are financial institutions who instruct small firms to undertake lender work on behalf of conveyancing clients. Introducing this ill-conceived proposal would remove the confidence to instruct small firms and may result in a reduction of small firms on lender panels.

If, as we anticipate, additional cover is required to cover such clients, it will increase cost for small firms and cancel the perceived overall saving of 5-10% upon which the SRA is basing this entire consultation. The purchase of top-up cover on an occasional or "as required" basis is the most expensive way of securing such cover. It will prove far better to buy £1m cover at annual renewal than to add top up cover for one additional client half way through the year. Dividing up the client base in this way increases costs both for law firms and for insurers. It adds a level of complexity and cost that is unnecessary. This proposal adds to the administrative and compliance burden for firms especially the smaller practices in checking the turnover of clients before deciding the level of cover on a case by case basis. As well as the additional cost of undertaking such work which will be passed down to the clients, there is scope for mistakes and for clients being under insured or uninsured.

We cannot see any advantage to clients or to firms in omitting financial institutions and other large business clients.

Please provide any additional comments on the alternative option that this could be at the election of the law firm

Question 3: Do you think our definition for excluding large financial institutions corporations and business client is appropriate?

Y/N **No**

We do not agree with the proposal for an exemption – see response to question 2 above.

In regard to the definition set out in the consultation, this is as follows:-

The exclusion is to be based upon the turnover (exceeds £2m) of the client in the financial year at the time the act giving rise to a claim occurred.

This definition is entirely impractical. It is ex post facto. A law firm needs to assess the turnover of the client before the retainer is entered into so it can decide whether or not it needs to purchase additional cover – not at some point which could be up to 15 years in the future when the law firm no longer exists and the commercial client makes a claim only to find it is not covered by insurance. Likewise the commercial client needs to know in advance that cover is in place when it enters into the retainer.

If no, please provide an alternative way of drafting the exclusion definition.

The only possible date for assessment of client turnover is the date of the retainer. It would be a term of the retainer that the law firm would provide professional indemnity insurance at the figure contained in the retainer.

Question 4: To what extent do you agree that we should introduce a separate component in our PII arrangements meaning only firms that need to have cover for conveyancing services are required to buy this cover?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree **– strongly disagree**

Please explain your answer

With the continuing increase in property prices, it would be unusual for a firm not to need higher cover than £1m thus negating the SRA's stated aim of reducing costs.

It also adds a level of uncertainty and complexity to the property market which in these days of money laundering and cyber-crime is not acceptable. More certainty, simplicity and trust are what is needed not less.

Question 5: Do you think our proposed definition of conveyancing services is appropriate?

Y/N **No**

We have no comment upon the definition per se. However, we disagree with the principle of separating conveyancing from the other legal services provided by firms. There is a risk that conveyancing within the scope of the definition could arise as part of other legal work. Most firms unless they were highly specialised would be better to obtain cover just in case one of its fee earners undertakes an element of conveyancing as part of other work which would be uninsured. There is a risk in separation which is not justified.

If no, please explain what you think should be an alternative definition.

Question 6: Do you think there are changes we should be making to our successor practice rules?

Y/N **No**

No separate comment – the Birmingham Law Society supports The Law Society response to this question.

If yes, please explain what these are and provide any evidence to support you view

Question 7: Do you agree with the approach we are taking to bring the MTCs and the PIA up to date?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree - **strongly disagree**

No separate comment – the Birmingham Law Society supports The Law Society response to this question.

Please explain your answer
Do you have any detailed comments on the changes we have made to the provisions in the MTCs?

Question 8: To what extent do you agree that the changes to our PII requirements provide law firms with more flexible options to potentially lower insurance costs?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree **– strongly disagree**

Please explain your answer

The insurance industry has described the idea that these reforms would lead to a reduction in premiums as “whimsical”. The Birmingham Law Society agrees with this assessment.

The increased administration and compliance burden required to implement these changes will far outweigh any savings that the SRA imagines will be present. Coupled to that would be the purchase of more costly top-up cover. Those costs will fall fairly and securely upon the smaller firms which are the very firms that the SRA is hoping to assist. “Flexibility” in this context will result in increased cost for firms, reduced consumer protection and uncertainty for all concerned.

Question 9: Do you agree the proposed level for the cap on cover in run-off provides adequate protection for the users of legal services whilst balancing the need for premiums to be more affordable?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree – **strongly disagree**

Please explain your answer and what evidence you have to support your view, or if you have a view on an alternative level for the cap.

The current arrangement is based upon turnover in the final three years before closure of a firm. This is an arbitrary arrangement but is a reasonable guide to the amount of activity in the firm and therefore the risk. A cap bears no relation to the level of activity or risk within a firm pre closure. It reduces the protection available to the

clients. Cost is likely to be the most significant factor upon closure of a firm. A sole practitioner closing his or her firm will take out the cheapest possible cover without paying any heed to the risks to clients. The retiree will want to be out of the firm. The retiree will have no practising certificate and will be off the Roll of Solicitors so no sanction by the SRA could bite. The retiree could be abroad. Again, the SRA proposals result in reduced protection for clients and for what purpose?

Question 10: To what extent do you agree that the changes to our PII requirements could encourage new firms to enter the legal services market increasing choice for users of legal services?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree **– strongly disagree**

The SRA argument is a non sequitur. An entrant to the market has many different costs and expenses in addition to PI insurance. For example, the payments to the SRA for annual practising certificate fees and firm registration fees are often higher than the amounts paid for PI insurance.

We have not seen any evidence to support the SRA's claim that these changes will encourage new firms to enter the legal services market. The Law Society reports in its response to this question that an insurance broker has assisted with 60 new start-ups at an average premium of £3000 under the existing system. Such a figure seems entirely reasonable and again does not support a change to the present arrangements.

Also new entrants to the profession of the type envisaged by the SRA are in the market to make money not to act as a charitable supplier of legal services. It is naïve to think that savings will be passed down to the hapless clients.

We respectfully remind the SRA of the response that the Birmingham Law Society submitted in the 2014 consultation as set out below.

It is the Society's view that although some or, indeed, all the proposals might, as the paper points out, result in some practitioners seeing a saving in the level of premium whilst others might experience an increase, what the paper ignores is that the insurers collectively know what to expect by way of premium income (both under the compulsory cover and top-up provided) and what they are likely to have to pay out. The effect of competition, which already exists and the possibility of new entrants into the field of PII cover, is wholly speculative and capable of being exaggerated. PII is a very specialist area of insurance. If changes are effected it is more than likely that it will be more of a case (please forgive the analogy) of "rearranging the deckchairs on the Titanic". It is also questionable whether the practices who

gain by a reduction in premium are the ones most frequently used by consumers i.e. those intended to be the main beneficiaries. High Street practices who deal with the whole gamut of property transactions, wills and estates and litigation remain amongst the most vulnerable to claims which is reflected in their premiums. If there are to be any 'winners' out of this, it is likely to be small niche practices who restrict themselves to specialist areas of law not especially vulnerable to claims.

Please explain your answer

Question 11: Are there any positive or negative EDI impacts from the proposed changes to our PII requirements that you think we have not identified?

Y/N **Yes**

No separate comment – the Birmingham Law Society refers to The Law Society response to this question.

If Yes, please explain what you think these impacts are

Question 12: Are there any options for changes to our PII requirements that we are not proposing or have not identified that we should consider further? Please explain why and provide any evidence that supports your view

No separate comment – the Birmingham Law Society refers to The Law Society response to this question.

Question 13: To what extent do you agree that the proposed changes to the Compensation Fund would clarify its purpose as a targeted hardship fund protecting the vulnerable that need and deserve it those in most?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree **– strongly disagree**

Please explain your answer

The Compensation Fund was set up to compensate all clients of law firms without fear or favour. It has always been a selling point for our profession that everyone is compensated if they suffer loss as a result of a problem. Tampering with it will reduce the security available to clients and damage the reputation of the profession.

Question 14: Are there any options for changes to how we manage the Compensation Fund that we have not identified that we should consider further?

Please explain why and provide any evidence that supports your view

No separate comment – the Birmingham Law Society refers to The Law Society response to this question.

Question 15: To what extent do you agree that we should exclude applications from people living in wealthy households?

Strongly agree

Somewhat agree

Neither disagree or agree

Somewhat disagree

Strongly disagree **– strongly disagree**

The proposed imposition of a bar to individuals from households with assets over £250,000 is likely to lead to irrational decisions as the Compensation Fund is intended to be a fund of last resort. It could also lead to unfairness. The Law Society has provided a number of examples in its response to this question.

Also of relevance is the increased administration cost to the SRA of determining eligibility based upon this financial criteria.

Please explain your answer

Question 16: Do you think our proposed measure of wealth and threshold for excluding these application is appropriate?

Y/N **No**

We do not agree with the proposed change for the reasons referred to above.

If no, do you have any suggestions for an alternative measure of wealth and or at what level the threshold should be set?

Question 17: Do you think we should be making any other changes to eligibility and/or the circumstances where we would make a payment?

Y/N **No**

If yes, please set out your suggestions and reasons for the change

Question 18: Do you think we have set out the right approach for assessing when a maximum payment has been reached?

Y/N **No**

If no, please explain why.

For the reasons set out by The Law Society in its response to this question i.e. lack of historical data the Birmingham Law Society is unable to comment further.

Question 19: Do you think the current formula remains a fair way to apportion the costs of maintaining the Compensation Fund?

Y/N **No**

Because of the forthcoming changes to the Accounts Rules e.g. third party managed accounts fewer firms will hold client accounts and therefore fewer firms will make an annual contribution to the Compensation Fund.

If the changes to professional indemnity insurance contained in this consultation paper are implemented we forecast that there will be more claims on the Compensation Fund caused by under insurance or lack of insurance.

The clients of all firms could potentially make claims upon the Compensation Fund whether the firms hold a client account or not.

There is therefore a simple yet powerful argument that all firms should pay into the Compensation Fund on an annual basis whether or not they retain a client account. We would support such a change.

If no, please explain you answer and any suggestions you have for alternative approaches

Question 20: What steps do you think might be reasonable for someone to take to investigate a scheme/transaction before committing money to it and that it is genuine?

We cannot understand why this question has been included within a consultation concerned with professional indemnity insurance and the Compensation Fund. This is a question for the government with its Money Advice Service and for the Financial Conduct Authority not the SRA and the profession.

Question 21: Do you think setting out clear Guiding Principles in the rules or as guidance could make the purpose and scope of the Fund and how we make decisions clearer to users of legal services and their advisors?

Y/N **Yes**

Transparency in relation to decision making is always welcome. The SRA website should be updated in this regard.

However, the SRA should not mislead either itself or anyone else if it believes that a user of legal services i.e. a client or law firms will read and appreciate these Guiding Principles before they enter into a retainer. These Guiding Principles will only be considered at the point when a claim on the Compensation Fund is needed for a very unfortunate client. The client will assume from the outset of the retainer that because of the trusted reputation of the profession that he will be covered in the event that his solicitor is dishonest or he suffers hardship and a claim needs to be made on the Compensation Fund. The Compensation Fund is an integral part of the reputation of the profession. The client will not expect his rights to be curtailed in the way proposed by the SRA in this paper.

Please explain your answer

Question 22: Are there any positive or negative EDI impacts from the proposed changes to the Compensation Fund that you do not think we have identified?

Y/N

No separate comment – the Birmingham Law Society refers to The Law Society response to this question.

If Yes, please explain what you think these impacts are

Question 23: Can you suggest any other approaches or strategies that the SRA might adopt to prevent firms being victims of cybercrime attacks?

No separate comment – the Birmingham Law Society refers to The Law Society response to this question.

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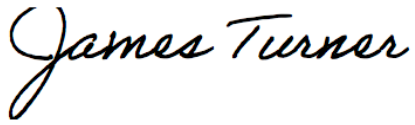

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