

**Application made by the Solicitors Regulation Authority  
Board to the Legal Services Board under Part 3 of  
Schedule 4 to the Legal Services Act for the approval of  
changes to regulatory arrangements relating to  
Compensation Fund contributions  
19 July 2018**

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**Application made by the Solicitors Regulation Authority Board to the Legal Services Board under Part 3 of Schedule 4 to the Legal Services Act for the approval of changes to regulatory arrangements relating to Compensation Fund contributions.**

**A. Proposed alterations**

**Compensation Fund Contributions**

1. The SRA needs to set the Compensation Fund contributions for the practising year 2018/19. The methodology used to allocate the cost of the fund throughout the regulated community remains the same as last year. Regulated individuals will contribute 50% of the funding requirement and regulated firms holding client money will contribute 50%.
2. A contribution level of £25.6m (2017: £11.1m) would result in an individual contribution of £90 (2017: £40) and a firm contribution of £1,680 (2017: £778). This is a significant increase year on year but, based on the best information available, is necessary, to properly manage the fund on a sound financial basis.
3. The proposed level of contribution has been calculated in line with the established methodology, which involves assessing expected pay outs and levels of claims by looking at historic trends in relation to claim numbers, amounts and timings and refined to take account of relevant more specific information where available.
4. This year, we have also had to make a further increase to the fund's appropriate reserve, to take account of a number of high-value exceptional cases. Primarily, these arise from solicitor involvement in investment schemes where individual clients have potentially suffered significant losses.
5. The calculation also uses the best view of predicted numbers and costs of interventions for 2018/19 onwards, continuing trends for business as usual, the impact of the closure of the Assigned Risks Pool (ARP) and claims in relation to uninsured firms with consideration also being given to any high-risk potential liabilities where known.
6. The forecast sum for grants during 2018/19 is £14.7m, plus a provision of £10m for claims arising from the small number (but high total value) of investment scheme cases. The latter is our best assessment of payments that may be made on these cases in 2018/19.
7. The contributions are not practising fees under the Legal Services Act 2007 (LSA), and so approval is needed under part 3 of schedule 4 rather than under section 51 of the LSA.

**B. Details of the relevant regulatory arrangements**

**Nature and effect of the existing position**

8. Under statute, we must maintain a Compensation Fund to compensate consumers who lose money due to the dishonesty or failure to account of solicitors (including RELs and RFLs) or firms. The Compensation Fund applies to all firms we authorise and regulate.

9. The statutory powers permit the SRA to require the regulated community to contribute to the Compensation Fund. The Compensation Fund Rules require both regulated individuals and regulated firms to make an annual contribution, collected mainly during the annual renewal/data collection exercise. Payment is required by 31 October for the following practising year.
10. We propose keeping the same arrangement for collecting the Compensation Fund contributions as we have done in previous years (i.e. collecting 50% from solicitors and 50% from firms). We have made this decision based on the fact that we are consulting on arrangements for the fund, and it is therefore not an appropriate time to make changes.
11. Each year, our Board reviews and sets how much individual solicitors and firms should contribute towards maintaining the fund. The contributions must fund the cost of claims, reserves and the cost of handling the claims. Our Finance and Audit committee reviews the nature of claims and any trends, level of reserves and budget for staff to handle the claims before making a recommendation to the Board. The Board then makes a recommendation to the Law Society Council which must, under the Law Society's General Regulations, approve the overall funding requirement. The Board then makes the final decision on how the total funding requirement should be divided between individuals and firms and sets out the contribution by resolution (the Compensation Fund determination).

### **C. Nature and effect of the proposed change**

12. The Finance and Audit committee, having gone through a detailed review, recommended that the funding requirement for 2018/19 should be £25.6m. The basis of this recommendation is included at annex A, which sets out the relevant financial analysis to support the need for £25.6m. Our Board considered and approved this on 30 May 2018. It was then approved by the Law Society Council on 4 July 2018. We now seek approval of the following determinations from the LSB:

#### **Annex B: Draft determination of Compensation Fund contributions 2018**

- This details how much individual and firms must contribute to the Compensation Fund.

#### **Annex C: Draft determination of Compensation Fund contributions for licensed bodies 2018**

- This details the contributions licensed bodies must contribute towards the Compensation Fund.

### **D. Rationale for level of contribution**

13. The funding requirement for the fund will vary year on year, depending on the nature of claims and any trends. The proposed level of contribution has been calculated in line with the established methodology and refined to take account of relevant, more specific information where available, with consideration being given to additional high-risk potential liabilities.
14. Over the years, the level of contribution has varied, with sometimes significant increases, for example, during property recessions. The reserving policy referred to in annex A and forecasting seeks, as much as possible, to avoid large swings and

has been refined to take account of relevant, more specific information where available, with consideration given to additional high-risk potential liabilities. Our Finance and Audit committee has debated the additional reserve in detail.

15. The table below shows the expected cash inflows and outflows to the fund, illustrating that a contribution of £25.6m is needed to maintain an appropriate reserve.

	<b>2017–18</b>	<b>2018–19</b>
<b>Income</b>		
Compensation Fund contributions	3,200*	25,640
Subrogated claims	9,557	9,575
Compensation Fund recoveries	1,615	1,700
Residual balances from statutory trust accounts (STAs)	1,061	760
Bank and investment income	177	176
<b>Total income</b>	<b>15,610</b>	<b>37,852</b>
<b>Expenditure</b>		
Compensation Fund grants	19,889	14,658
Fees, tax and other costs	51	60
SRA support costs recharged	11,917	10,994
<b>Total expenditure</b>	<b>31,857</b>	<b>25,712</b>
<b>Surplus/(deficit)</b>	<b>(16,247)</b>	<b>12,140</b>
<b>Opening balance</b>	<b>41,302</b>	<b>25,055</b>
<b>Closing balance</b>	<b>25,055</b>	<b>37,195</b>

\*As the majority of contributions are paid in advance of the practising year, the contributions collected in the 2017/18 practising year was in excess of £11m. The majority of that amount was collected in the 2016/17 year. Although the £25.6m collection for 2018/19 is shown in that year, some cash will be collected during October 2018 and the actual year-end balance will be higher as a result.

16. The appropriate reserve level (closing balance before exceptional cases) is established through an agreed formula:

(1.5 x weighted average grants in previous 7 years) + (3 months' costs) and an additional amount to take account of high value exceptional cases.

(1.5 x £16.3m) + (£2.7m)	£27.2m
Plus potential grants on exceptional cases	£10.0m
<b>Total appropriate reserve</b>	<b>£37.2m</b>

## **E. Statement in respect of the Regulatory Objectives**

17. The existence and effective operation of the Compensation Fund primarily protects and promotes the interests of consumers. It makes sure consumers receive compensation if their money is lost or not accounted for while in the hands of a

regulated individual or entity. However, it also promotes the public interest and improves access to justice, as it gives the public the confidence to entrust funds to and therefore use solicitors' and firms' legal services. It is also in consumers' interests to make sure the Compensation Fund is properly maintained, to meet claims without delay.

#### **F. Statement in respect of the Better Regulation Principles**

18. The way in which the Compensation Fund requirement is allocated among the profession was reviewed in 2010. This was, among other things, to improve transparency and accountability. In February 2014, our Board decided to maintain the practising fee and Compensation Fund contributions apportionment structure for two years, pending a wider review.
19. We planned to review the payment structure for the fees we charge and consult with the sector. We have done a significant amount of work on this. However, we have decided that we should not propose changes at this time. This is because many of the relevant processes are likely to change due to our regulatory reform programme and work to modernise our IT. The profession is also being asked to handle a lot of change, including the introduction of the General Data Protection Regulations and the recent anti money laundering regulations. We now anticipate carrying out this review in 2019.

#### **G. Statement in relation to desired outcomes**

20. In increasing the contributions towards the fund, our aim is to make sure it is properly funded and maintained and able to meet claims without delay. The fund is reviewed annually and is also subject to audit. Regular reports on the nature of claims and any trends are made to our senior management team, and the fund's financial status is a key priority for our Finance and Audit Committee.

#### **H. Statement in relation to impact on other approved regulators**

21. There is no impact on other approved regulators. The increase in contribution only applies to individuals and/or firms we regulate.

#### **I. Implementation timetable**

22. The timetable is as follows:
  - Our Board and the Law Society Council finalise the total funding requirements in July and seek LSB approval of the practising fees.
  - During August, final preparations for this year's renewal exercise will be made, and, on 1 October 2018, firms and individuals will be contacted and asked to make the various renewal applications online.
  - Firms and individuals must submit the relevant Compensation Fund contributions and other fees by 31 October 2018.

#### **J. Stakeholder engagement**

23. As is standard practice, a comprehensive communications plan was drawn up to promote the determination of the 2018/19 practising fees, including the proportion of

Compensation Fund contributions. The purpose of the communications plan was to make sure that the regulated community and relevant stakeholders were informed of:

- what their fees pay for
- the availability of the fees calculator to help them
- the level of fees to be collected.

24. The following elements of the communications plan for fees and compensation fund activities have been delivered or are scheduled for delivery:

- 22 March-15 June: We ran a comprehensive consultation which looked at our client financial protection arrangements, including a discussion about the level of cover and cost of the Compensation Fund.
- 24 April: We outlined information about the grants we made from the Compensation Fund in our Annual Review.
- 12 June: – The Law Society Group published its net funding review consultation, which covers the Compensation Fund.
- The consultation was publicised through media releases by both us and the Law Society. We did a separate announcement focussing on the changes to the Compensation Fund.
- Social media posts – including LinkedIn, Facebook and Twitter, also promoted this consultation.
- 13 June: Our senior management team discussed issues around Compensation Fund contributions at a media briefing.
- Further promotion came through the Law Society’s Professional Update weekly newsletter, and our newsletters, SRA Update (10 July) and Compliance News (20 June).
- Compensation Fund statement published in August
- 18 July – SRA Board agrees fee-collection mechanism
- July – large-scale communication will be sent to firms ahead of the renewal period, outlining the level of indicative fees, as well as the contributions we are asking for
- 1<sup>st</sup> August – SRA post board media briefing where issue may potentially be discussed
- Mid August – following LSB decision/approval update of web materials confirming fees
- September – large-scale communications will be sent to firms ahead of the renewal period, outlining the level of fees and contributions we are asking for.

### **Contact for matters relating to this application**

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**Annex A - Basis of recommendation**

**Annex B - Draft Determination of Compensation Fund contributions 2018**

**Annex C - Draft Determination of Compensation Fund contributions for Licensed Bodies 2018**

# Annex A – Basis of recommendation

## Compensation Fund Contribution for 2018/19

### Recommendation

1 The SRA Board recommended that Council sets the contributions to the Compensation Fund (“the Fund”) for 2018/19 at £25.6m resulting in:

- individual contribution     £ 90                    (2017/18 - £40)
- firm contribution             £1,680                    (2017/18 - £778)

### Background

2 The Fund pays discretionary grants to people who have lost money as a result of dishonesty or failure to account by solicitors or law firms. In 2013 the Fund’s jurisdiction was expanded to include the payment of discretionary grants to people who cannot recover damages from a solicitor or law firm because of a failure to obtain indemnity insurance.

3 The SRA Finance and Audit Committee (FAC) and the SRA Board have operated a policy of maintaining a relatively steady level of contributions over the short to medium term where possible – avoiding significant year on year fluctuations. This has been done in order to assist contributors in their financial planning.

4 In addition, until last year, we have been in a period where we have been reducing the level of cash reserves held by the Fund. Cash reserves were increased at a time where we faced high levels of claims for conveyancing matters following the 2008 financial downturn. The great majority of these claims did not result in payments from the Fund which meant that the level of cash reserves held by the Fund were higher than necessary to meet the more normal levels of call on the fund.

5 We have in recent years set contributions at a level which provided income to the Fund lower than cash outflows in order, over a period of time, to bring the Fund’s cash reserves down to what we would calculate to be an appropriate level.

6 The contributions set for 2017/18 increased from the level which had applied for the previous three years. The increase was to provide additional reserves because of the risks posed to the Fund by a small number of very large claims arising from dubious investment cases.

7 The FAC considered the appropriate level of contributions for 2018/19 in detail on two occasions in order to reach the recommendation made to the Board. The key issue for the FAC has been whether

- (a) to maintain the approach of recent years and keep contribution levels at a level which would reduce the level of Fund reserves, or

- (b) given the information available about the potential level and timing of significant claims from investment scheme frauds, to further increase contributions for 2018/19.

8 After careful consideration the FAC decided that the latter approach is necessary, and that decision formed the basis of the recommendation to the Board.

### **Fund Position as at 31 March 2018**

9 Total grant payments for the practice year 2016/17 were £15.2m. The gross value of open claims<sup>1</sup> received as at 31 May 2018 was £94.0m. Total grants paid as at 31 May 2018 are £10.2m and we forecast that in the year 2017/18 we will pay grants of £19.9m.

### **Claims for uninsured loss**

10 These are applications to the Fund (following closure of the Assigned Risks Pool (ARP) at the end of September 2013) for losses suffered as a result of the civil liability of a firm which did not have insurance against which claims could be made. Capita deals with these claims on our behalf because of their close relationship to formal negligence claims which they also dealt with as manager of the ARP.

11 At the end of May 2018 there have been 97 claims, of which 85 have been closed and twelve are currently under investigation with a total claim value of £2.3m.

### **Cost Pressures**

12 In 2016/17 we became aware of a number of significant investment fraud schemes involving solicitors. We issued warning notices about these to the profession and to the public. A number of implications arise from the continued increase in prevalence of these schemes.

13 The contributions set for 2017/18 increased from the level which had been applied for the previous three years when contributions had been deliberately set at a level that would reduce the level of reserves held by the fund. For 2017/18 the Board recommended that contributions needed to increase to provide additional reserves because of the risks posed to the Fund by a small number of very large claims largely arising from dubious investment cases.

14 The Fund has not yet made or approved payments in respect of any of the investment fraud schemes. However, there is now an established trend of increased total payments in respect of “standard” cases which has utilised the increased contribution last year. In addition, the level of payments into the Fund from sources other than contributions has been diminishing.

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<sup>1</sup> The ‘Original Claims Value’ which after analysis is usually reduced to ‘Revised Claims Value’ which represents a more realistic estimate of the correct value of the claim. Claimants often seek much more “compensation” than is actually payable from the Fund.

- 15 The combined impact of these issues is that, although no payments have been made in respect of “exceptional” cases the Fund will not be carrying a level of reserves above the minimum level as expected at the end of the year.
- 16 The FAC noted the information on the predicted level of interventions and “standard” claims in 2018/19 and considered that the impact of these was addressed through the application of the usual forecasting calculation. There was nothing exceptional apparent that required a variation in the application of that calculation.
- 17 The Committee considered in detail, and discussed, all of the information available to it about exceptional cases where claims had either been made to the Fund or were expected. Many of these cases arise from solicitor involvement in dubious investment schemes. The Committee had been kept informed of the development of these cases through regular reports from the Executive throughout the year.
- 18 There are three cases deemed to be of medium or high risk with significant potential losses and are expecting to pay grants in the next year or so on these cases although it may take some time before the claims are received. The risk to the Compensation Fund is extremely difficult to predict but could be very serious if it does crystallise.
- 19 The high value exceptional matters relate mainly to investment fraud matters which, by their nature are very complex. Accordingly, the lead time for potential payments being made from the Compensation Fund can be quite lengthy so it is likely to take a matter of time before significant payments are made. Therefore, the imminent risk of very high payments remains relatively low, but some cases may change quickly. The highest risk is a sudden need to deal with multiple claims that cumulatively total a large amount.
- 20 The Committee considered and discussed whether any changes resulting from the current consultation that is proposing reforms to PII and the Compensation Fund will impact on the Fund in 2018/19. It decided that they would not change the position of the existing high value exceptional matters and have therefore not been considered in the recommendation for the level of contribution in 2018/19. Any changes from the reforms will not be implemented imminently and are unlikely to be applied retrospectively.
- 21 The Committee accepted the executive’s recommendation that the total level of funding for 2018/19 to be collected through contributions should be based on the well-established forecast calculation but with the minimum level or reserve increased by £10m because of the risks posed by the number, value and current status of the exceptional claims and potential claims. This is consistent with the approach taken by the Board to contribution setting for 2017/18.
- 22 On the basis of the review of the high value exceptional cases, the FAC advised the Board that the reserves should be increased to a level of £10m above that indicated by the established calculation.
- 23 The required contribution is £25.6m, which is £14.5m higher than last year (£11.1m in 2017/18). The significant increase over 2017/18 (even though the same approach is being taken) arises primarily because of the recent trend of

increased payments in respect of “standard” cases and reduced recoveries (see paragraphs 14-16 above). The impact of this is that the base level calculation of the funding required to maintain a minimum level of reserve results in a need for increased contributions and the funds necessary to place the Fund £10m above the minimum level needs to be collected afresh.

- 24 For the purposes of calculating an individual and firm contribution it has been assumed that there will be the equivalent of 142,000 individuals paying a fee and approximately 7,620 firms paying a contribution.
- 25 Based on these figures, a collection of £25.6m would result in an individual contribution of £90 and a firm contribution of £1,680. The Committee recognised that this was a significant increase year on year but one that was necessary, on the best information available, to meet the Board’s obligations to manage the Fund on a sound financial basis.

### Calculation of Recommended Contribution for 2018/19

- 26 As in previous years, the recommended contribution has been calculated by considering the opening balance of money held in the Fund and then taking account of:
- calculation of the appropriate reserve required (see paragraphs 28 to 29)
  - forecast cash outflows (i.e. grants and costs – see paragraphs 30 to 32)
  - cost paid from the compensation fund (see paragraphs 33 to 34)
  - forecast cash inflows (excluding the contribution – see paragraphs 35 to 37).
- 27 This leads to the required contribution being identified as a balancing figure with value incorporated for the high value exceptional cases in addition to the established calculation. This approach was taken in 2013/14 when the mortgage fraud cases project was established.

### Appropriate Reserve

- 28 We have increased the calculation of the appropriate reserve to take account of the medium to high risk high value exceptional cases.
- 29 Based on the intelligence we have about the investment scheme fraud claims we have made a best estimate of when they could be paid. This position will continue to change over the coming months as we investigate further.
- 30 The calculation used for the appropriate reserve produces the following figure for 2017/18:

- (1.5 x weighted average grants in previous 7 years) + (3 months’ costs)  
Being: £24.4m (1.5 x £16.3m) + (£2.7m) £27.2m  
Plus potential grants on Exceptional Cases £10.0m  
**Total Appropriate Reserve £37.2m**

### Future Claims and Costs

- 31 The main factors in forecasting grants are the numbers of current claims and expected future claims. The latter is determined by the expected number of interventions.
- 32 For the purpose of this calculation, we have assumed that there will be 40 interventions in this and subsequent practising years. We have seen a decrease in the number of larger interventions in the first seven months of this financial year (Nov 17 – May 18) however given the unpredictable volatility of the number of interventions year on year an assumption of 40 interventions for this year and next has been made.
- 33 Interventions account for the bulk of the costs paid by the Fund. We liaise closely across several internal departments on potential interventions to help forecast future intervention costs more accurately (as well as to prepare operationally). Forecasting intervention numbers beyond that is very difficult.

### Costs paid from the Compensation Fund

- 34 The amount forecast to be paid from the Fund for 2017/18 is £11.9m based on the intervention costs included in the SRA budget.
- 35 For 2018/19 the predicted recharge is £11.0m. This is made up of £7.0m intervention costs and the remainder is other staff related costs and shared service contribution. It is assumed that rates of recovery from existing and future statutory trust accounts will not differ significantly from previous years.

### Cash Inflows

- 36 The main cash inflows to the Fund (excluding contributions) are transfers from Statutory Trust Accounts (STAs) through rights of subrogation and the transfer of residual balances.
- 37 Based on evidence of previously closed STAs and the ongoing work on live accounts, subrogated and residual funds are expected to total £10.6m in this year and £10.3m next year.
- 38 Money is also recovered from intervened solicitors or through claims against the indemnity insurer of an intervened firm. Recoveries are expected to be £1.6m in 2017/18 and are forecast at £1.7m in 2018/19, increasing to £1.8m from 2019/20 onwards.

### **Recommended 2018/19 contribution**

- 39 The required contribution is £25.6m, which is £14.5m higher than last year's requirement (£11.1m in 2017/18).
- 40 The table below shows the expected cash inflows and outflows to the Fund. Indicative figures are shown covering the current and next three practising years. The level of contributions is set each year to ensure that reserves are maintained at the appropriate level.

41 The main driver of the increase in fees this year is the increase in the level of the appropriate reserve to take into account the high value cases in relation to investment scheme fraud.

42 The table below shows the expected position at the end of the 2018/19 financial year including the impact of payment of claims in respect of exceptional investment scheme cases.

	2017-18	2018-19
<b>Income</b>		
Compensation Fund contributions	3,200*	25,640
Subrogated claims	9,557	9,575
Compensation Fund recoveries	1,615	1,700
Residual balances from STAs	1,061	760
Bank & investment income	177	176
<b>Total income</b>	<b>15,610</b>	<b>37,852</b>
<b>Expenditure</b>		
Compensation Fund Grants	19,889	14,658
Fees, tax and other costs	51	60
SRA support costs recharged	11,917	10,994
<b>Total expenditure</b>	<b>31,857</b>	<b>25,712</b>
<b>Surplus / (deficit)</b>	<b>(16,247)</b>	<b>12,140</b>
<b>Opening balance</b>	<b>41,302</b>	<b>25,055</b>
<b>Closing balance</b>	<b>25,055</b>	<b>37,195</b>

\* As the majority of contributions are paid in advance of the practising year the actual contributions collected in relation to the 2017/18 practising year was in excess of £11m with the majority of the cash recognised in the previous practising year. Although £25.6m collection for 2018/19 is shown in that year, in actuality a proportion of the cash will be collected during October 2018 and the actual year-end balance will be higher as a result.

43 Given the uncertainty over the extent and timing of these claims any future forecasts are highly uncertain and therefore have not been included. The forecasts are based on the currently available information and may change as we move through the next financial year.

44 We continue to closely monitor the development of these cases and as the position becomes clearer on each we will review and update future forecasts. At the most extreme position, should all of the current cases where there are potential claims result in payment then there would necessarily be future increases in contribution levels. However, as we have explained we are simply not in a position to make this definitive judgment at this stage.

- 45 For the purposes of calculating individual and firm contributions it has been assumed that there will be the equivalent of 142,000 individuals paying a fee and approximately 7,620 firms paying a contribution. There is an increase in individuals and the number of firms from last year. The table below compares fee levels in 2016/17 and those recommended for 2017/18.
- 46 A collection of £25.6m would therefore result in an individual contribution of £90 and a firm contribution of £1,680 with 50% of the contribution collected from individuals and 50% from firms.

### **Next steps**

- 47 The fees are significantly increasing following the increase for the first time in three years last year. We therefore conducted a wider communication plan than usual explaining the impact of the high value exceptional cases. A full briefing note is attached at Appendix 1.

### **Supporting information**

#### **Links to the Strategic Plan and / or Business Plan**

- 48 This proposal relates to our strategic objective to “improve our operational performance and make fair and justifiable decisions promptly, effectively and efficiently” in the context of ensuring client protection through an effective and efficient Compensation Fund.

#### **How the issues support the regulatory objectives and best regulatory practice**

- 49 A properly run Compensation Fund provides transparency and accountability.

#### **Impact of the proposed reform of the Compensation Fund**

- 50 In April 2018, we published proposals that reform the Compensation Fund and designed to make sure users of legal services get the appropriate level of protection and to make sure financial support is focussed on those in most need of help. The proposals were developed in light of the potential confusion around the purpose of the Fund and changing risks and higher value claims.
- 51 If implemented, the changes are likely to come into effect in Spring/Summer 2019 and will not impact on the contribution setting for 2018/19.

#### **What equality and diversity considerations relate to this issue**

- 52 The increase of the contribution to the Compensation Fund is likely to have a greater impact on sole practitioners and firms with 2 - 4 partners and therefore indirectly for BAME solicitors who are disproportionately represented in this cohort. Unlike the firm Practising Certificate fee which is calculated by turnover.
- 53 The increase in the contribution to the Compensation Fund is significantly higher than last year which was the first increase in three years. The impact is not mitigated by considerations of ‘ability to pay’ however the significant value and level of risk associated with the high value contentious cases, we are

asking for level of contribution that will enable the fund to meet the potential increase in claims over a three-year period. The increase is therefore proportionate and meets a legitimate aim to compensate claimants.

- 54 We provide reasonable adjustments for older solicitors who are unable to close their firm at retirement due to high levels of insurance costs. The SRA supports older solicitors through this process.

## **Appendix 1 - Compensation Fund contributions communications approach**

### **Communications approach**

Any increase in Compensation Fund contributions is unlikely to be welcomed by the profession. Our communications approach will aim to offer reassurance to the profession that:

- the increase is necessary, because of changes in the market. Analysis shows that there are likely to be more high value exceptional claims on the fund
- it is in the interests of the public and the profession that the fund can provide compensation for claims that meet the criteria
- we are managing the compensation fund efficiently and effectively, and will make sure the profession pays no more than they need to
- we always notify contribution levels well in advance to help firms to plan ahead.

In order to manage the communications risks, we plan to take a proactive approach, with a focus on making sure our messages reach legal professionals. We aim primarily to do this through the legal trade press and direct correspondence with law firms of all sizes.

### **Key messages**

#### **Compensation Fund is essential to protect public and maintain trust in profession**

- The Compensation Fund is essential if we are to protect the public, and maintain trust in the profession.
- People can be confident that if they use a regulated solicitor, they have the protection of professional indemnity insurance, with a further backstop of the compensation fund for cases, for instance, that involve dishonesty.

#### **Increase needed – following on from the increase last year which was the first in three years – to make sure sufficient funds to cover claims**

- We need to make sure that there is sufficient funding, including reserves, available to cover valid claims, so we plan to increase contributions for a second year to £26.5m, which includes an additional £10m reserve to meet potential future claims relating to the high value contentious matters with the highest risk where there is a possibility that the Fund may pay circa £30m during the next three years.
- This reflects our assessment of the level of risk related to current and potential cases. The evidence suggests we will see an increase in high value exceptional claims. The increase in contribution in 2017/18 was utilised by an increase in grant payments overall rather than on the previously identified high value contentious cases.
- We continue to see investment scams involving solicitors with consumers continuing to lose significant amounts. Every case will not result in successful claims, but we need to make sure we have appropriate funding available.

**We are committed to making sure we use the profession's money effectively. We will continue to monitor this issue**

- As well as maintaining trust in the profession, we are committed to making sure we use the profession's money efficiently and effectively.
- We will continue to monitor this issue, so that we can make sure compensation fund contributions are set at an appropriate level.

**Background:**

On the basis proposed, the contribution for 2018/19 would total £26.5m with individual and firm contributions increasing for the first time in three years to:

- Individual contribution           £90 (2017/18 - £40)
- Firm contribution                   £1,680 (2017/18 - £778).

**Core activities**

- 31 May: Warm-up communications around compensation fund financial statements for last year, communicated through press release and briefing at 31 May Board
- Detail on Compensation fund activity in new Annual Review, to be published in June
- Mid June: Announcement to coincide with The Law Society Group consultation on practising fees. This will include:
  - press release highlighting the consultation, as well as the changes in the compensation fund contributions. Release will go to trade press on an embargoed basis with background briefing. Update web materials - and fees calculator - to reflect new information and key messages around compensation fund.
  - Include core messages in next editions of our professional newsletters, SRA Update and Compliance News.
- September onwards: reference in PCRE warm-up communications and subsequent communications.
- August: following LSB approval, update web materials confirming final fees.

We will also develop reactive lines, for use with media, stakeholders and on social media, so we are in a position to respond quickly to queries and challenges of our approach. This will include lines about how we make sure we manage the compensation fund in an efficient and effective way.

## Annex B - Draft Determination of Compensation Fund contributions 2018

This determination is made by the Solicitors Regulation Authority Board under rule 2.3 of the SRA Compensation Fund Rules 2011, with the approval of the Legal Services Board under paragraph 19 of Schedule 4 to the Legal Services Act 2007.

- (1) Every person who applies for a practising certificate to commence on or after 1 November 2018, or who applies for initial registration or renewal of registration as a registered European lawyer or registered foreign lawyer to commence on or after 1 November 2018, shall pay with the fee payable in respect of that application, a contribution of £90 to the Fund.
- (2) Every recognised body or recognised sole practice that has held or received client money (as defined in the SRA Accounts Rules 2011) during the period 1 November 2017 to 31 October 2018, shall pay with the annual periodical fee, a contribution of £1680 to the Fund.
- (3) Every person that:
  - (a) applies for initial recognition as a recognised body or initial recognition as a recognised sole practice to commence during the period 1 November 2018 to 31 October 2019; and
  - (b) intends to hold or receive client money (as defined in the SRA Accounts Rules 2011) at any time during the period 1 November 2018 to 31 October 2019.

shall pay with the fee payable in respect of that application, a contribution to the Fund as follows:

- i. £1,680 on applying for initial recognition to commence in the period 1 November 2018 to 31 December 2018;
  - ii. £1,260 on applying for initial recognition to commence in the period 1 January 2019 to 31 March 2019;
  - iii. £840 on applying for initial recognition to commence in the period 1 April 2019 to 30 June 2019;
  - iv. £420 on applying for initial recognition to commence in the period 1 July 2019 to 31 October 2019.
- (4) The SRA may waive the contribution payable under paragraph (3) above in circumstances where the initial application is made by a body which is changing its legal status or is succeeding to the practice of another authorised body and the predecessor body or practitioner has already paid a contribution to the Fund.
  - (5) In this determination:

**Fund** means the Solicitors' Compensation Fund established and maintained under rule 2.1 of the SRA Compensation Fund Rules 2011;

All other terms are to be interpreted in accordance with the Practising Certificate Fee Determination 2018.

- (6) This determination shall come into force on 1 November 2018.

## Annex C - Draft Determination of Compensation Fund contributions for Licensed Bodies 2018

This determination is made by the Solicitors Regulation Authority Board under rule 2.3 of the SRA Compensation Fund Rules 2011, with the approval of the Legal Services Board under paragraph 19 of Schedule 4 to the Legal Services Act 2007.

- (1) Every licensed body that held or received client money (as defined in the SRA Accounts Rules 2011) at any time during the period 1 November 2017 to 31 October 2018, shall pay, with the annual periodical fee, a contribution of £1,680 to the Fund.
- (2) Every licensed body that intends to hold or receive client money (as defined in the SRA Accounts Rules 2011) at any time from the date on which the body is authorised to 31 October 2019, shall pay, with the initial periodical fee, a contribution to the Fund as follows:
  - i. £1,680 on applying for initial recognition to commence in the period 1 November 2018 to 31 December 2018;
  - ii. £1,260 on applying for initial recognition to commence in the period 1 January 2019 to 31 March 2019;
  - iii. £840 on applying for initial recognition to commence in the period 1 April 2019 to 30 June 2019;
  - iv. £420 on applying for initial recognition to commence in the period 1 July 2019 to 31 October 2019.
- (3) The SRA may waive the contribution payable under paragraph (2) above in circumstances where the initial application is made by a body which is changing its legal status or is succeeding to the practice of a recognised body or recognised sole practitioner and the predecessor body or practitioner has already paid a contribution to the Fund.
- (4) In this determination:

**Fund** means the Solicitors' Compensation Fund established and maintained under rule 2.1 of the SRA Compensation Fund Rules 2011; and

All other terms are to be interpreted in accordance with the Licensed Body Fee Determination 2018.
- (5) This determination shall come into force on 1 November 2018.