

**FURTHER SUBMISSIONS IN SUPPORT OF THE 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:**

- **CLAUSES 2.10, 6.2 AND 6.11 OF THE QUALIFYING INSURER'S AGREEMENT 2010**
  - **THE SOLICITORS' INDEMNITY INSURANCE RULES 2010**
  - **THE MINIMUM TERMS AND CONDITIONS OF COVER (MTC)**
  - **THE ASSIGNED RISKS POOL POLICY**
1. Following submission of the SRA's application for approval on 9 July 2010 we sought comments on three changes which had not been the subject of formal consultation papers. The three changes are as follows:
    - **Defence Costs** (MTC-Clause 1.2(c)) (see paragraphs 35 to 40 of the application)
    - **Award by Regulatory Authority** (MTC—Clause 1.8) (see paragraphs 41 to 48)
    - **Debts and Trading Liabilities** (MTC—clause 6.6(b)) (see paragraphs 49 and 50).
  2. Four submissions had been received by the deadline of 23 July 2010 as follows:
    - The Law Society
    - The Sole Practitioners Group (SPG)
    - A Qualifying Insurer
    - The Legal Services Consumer Panel.
  3. We have considered the points raised in each of the submissions and assessed whether they provide new information that would cause us to alter our application. This report summarises the comments received and sets out the SRA's position in the light of those comments.

**Defence Costs (MTC – Clause 1.2(c))**

**Comments received**

4. Comments were received from The Law Society, the SPG and the Qualifying Insurer. Both the Law Society and the SPG argue against the proposal to remove cover for defence costs in respect of disciplinary proceedings arising from any claim. The Law Society understands the thinking behind the proposal as it is a provision that on the face of it provides protection for solicitors rather than their clients but makes the point that the cover has been

part of the Minimum Terms and Conditions (MTC) since 2000. Both the Law Society and the SPG are concerned at the lack of proper consultation and are of the view that the change should be deferred to allow full consultation. There is clearly a feeling that the cost to insurers of providing the cover is very small so little is to be gained by its removal. The Law Society recognise the need to avoid delay in settling the MTC and have suggested that the LSB require the SRA to consult properly on the defence costs issue over the coming months before coming to a final decision on the matter, and to require the SRA to reinstate the provision of defence costs for disciplinary proceedings for the purposes of the 2010/11 renewal.

5. The Qualifying Insurer respondent states that *“solicitors are not a special case and have a worse record than many other professionals in terms of frequency of claims. Outside solicitors PI very few PI policies compel insurers to cover disciplinary - it is usually optional. Costs can be very substantial and tend to exaggerate losses on firms which already have a problem with issues like mortgage fraud followed by disciplinary.”*

### **SRA position**

6. For the reasons set out in our application, the SRA Board believes that it is right in principle that cover for defence costs related to disciplinary proceedings should not be part of the compulsory MTC. The Law Society does not argue against the principle but along with the SPG expresses concern at the lack of full consultation and we accept that there were deficiencies in the consultation process this year regarding some of the proposed changes to the Rules and MTC.
7. Costs can be very substantial and can act as an unnecessary disincentive for insurers either to continue in the market or to provide individual firms with terms. It is difficult to get precise figures for the cost of providing this cover as insurers do not separately record defence costs related to disciplinary proceedings. Indications are that typically defence costs for disciplinary proceedings are of the order of £30,000. This is about the same as an average personal injury failed litigation claim (£28,000) or a matrimonial claim (£34,000). However they tend to be in the 1-5 partner area and for firms paying less than £10,000 in premium. The costs can be substantially higher and two cases that have come to our attention recently involved insurers paying defence costs for disciplinary proceedings of £900,000 and £250,000 respectively.
8. It is fair to say that the absence of approved MTC for 2010 is already causing problems as insurers appear to be holding back on providing quotes until they are clear as to the final MTC. The Law Society is fully alert to the problems associated with further delays. We have considered the suggestion that the provision regarding defence costs is reinstated to allow us time to consult more fully before coming to a final decision regarding 2010/11. We do not support this approach as it would not provide the necessary timely certainty as regards the 2010/11 MTC.
9. We also do not support the suggestion that we abandon the proposed change until October 2011, at the earliest. We anticipate that this year's renewal will be the most difficult yet for the profession. Reinstating defence cost at the last minute could further destabilise an already fragile market and we believe

would not be in the interests of either the public or the profession. The proposed change is right in principle and will, we believe, ease some of the stress that has built up in the market. Notwithstanding the deficiencies in the consultation process we still believe that the change approved by the SRA Board strikes the right balance between scope of cover, public protection and the need for a viable market for solicitors' compulsory professional indemnity insurance.

## **Award by Regulatory Authority (MTC - Clause 1.8)**

### **Comments received**

10. Comments were received from the Legal Services Consumer Panel (the Panel) and the Qualifying Insurer. The Panel does not support the SRA's decision not to require insurers to provide cover for the 'return of fees' element of any award by the Legal Ombudsman. The Panel does not agree with the SRA's reasoning *"on the simple grounds that there is little point in giving consumers rights they cannot enforce. Consumers have a reasonable expectation that all remedies awarded by the Legal Ombudsman will be honoured, including through the solicitor's insurance policy as a last resort. Not only is the SRA's policy unfair to consumers who have been let down by their solicitor, it also undermines the authority of the Legal Ombudsman, potentially sowing a seed of doubt in the minds of all consumers about the prospects of securing redress."*
11. The Panel also made the point that the Association of British Insurers did not appear to be aware that this was an issue for its members.
12. The Qualifying Insurer argued that the change did not go far enough and that all Legal Ombudsman awards should be excluded from the compulsory MTC as follows:

*"We do not consider that these [awards by regulatory authorities] should be covered at all. Non-negligent poor service has been an issue that has dogged the profession and has driven some of the changes to the SRA and Law Society. Insurance is not the answer to this issue and never has been as it defeats the intention to drive best practice....."*

*Treating IPS awards as insured compensation widens losses and again the firms that do not pay tend to have had negligence claims as well, or go into run-off without paying the premium. The maximum IPS award limits are expected to increase....."*

*Widening scope increases further the risk of major losses and discourages insurers from underwriting small firms, because they are often under-capitalised. In the long term scarcity of insurance will prevent new practices starting up. This issue is demonstrative of a misunderstanding of the role of normal insurance:*

*In a worsening loss climate insurers usually restrict cover, here the cover has widened over time, and in a worsening loss climate....."*

*This is a classic moral hazard situation - an insured should not be covered for treating a customer poorly - e.g. being rude or not replying to letters*

*Covering this loss is more in the interest of solicitors than in the interest of the public - these losses should fall to the Compensation Fund if not paid*

### **SRA position**

13. The SRA's position encompasses three elements.
14. First, it is a moral issue. It seems fundamentally wrong that a solicitor who has been ordered to return fees which it has been determined he was never entitled to charge should be financially unaffected by such an order.
15. If the MTC covered such cases, a solicitor who had overcharged, or charged for work done badly, and who had been ordered to refund all or part of the fee would suffer no loss, since he would be indemnified by his insurer. An order for the refund of fees is intended not merely to compensate the injured client but to express the adjudicator's disapproval of the solicitor's conduct. If the solicitor in fact suffers no financial loss, it is a toothless punishment.
16. Second, it is a market issue. Most insurers are strongly of the view that for the reasons outlined above refund of fees should not be covered by PI policies, are not in fact covered, and accordingly resist payment of such claims. As all are aware, the market is currently in a fragile condition. The SRA considered that at the present moment the time was not ripe to confront the market on this point, when the market faces so many other challenges.
17. Third, it is a legal issue. Under many professional indemnity policies an insured firm must establish that it has suffered a loss as a result of the claim. The MTC wording provides cover in respect of civil liability arising from private legal practice. There is a respectable argument that the refund of fees is already covered by the current (2009-10) MTC, whether ordered by a Court or by the Legal Complaints Service. However, this argument has not been tested, and there are arguments to the contrary. This lack of clarity as to the legal position has led to the variation in approach by the market.
18. Having considered the points raised by the Panel we remain of the view that the proposed coverage for awards by the Legal Ombudsman is both reasonable and proportionate.

### **Debts and Trading Liabilities (MTC - clause 6.6(b))**

#### **Comments received**

19. The only comment received was from the Qualifying Insurer as follows:

*"Widening the scope of the cover when the market as a whole is running at over 100% loss ratio (i.e. the total premium collected does not cover the total claims) is always going to reduce competition as it demonstrates the regulator will not take into account insurers concerns.*

*The trading debt exclusion is one of the few exclusions in the policy and is being watered down to potentially cover solicitors for things like infecting the Land Registry system with a virus. This is in solicitor interests but does not*

*affect the public. Covering network liabilities to providers is not a standard element of PI insurance outside solicitors cover and there is no special case to be made.”*

### **SRA position**

20. We are not persuaded by the arguments put forward by the Qualifying Insurer. As stated in the application the purpose of the change is to preserve, rather than to enhance, cover. The carve out from the exclusion will ensure that if a firm enters a Land Registry Network Access Agreement it will not take away professional indemnity cover that the firm had before entering into the contract. The change is intended to preserve client financial protection and the protection of firms.

### **SRA CONTACT FOR MATTERS RELATING TO THIS FURTHER SUBMISSION**

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Date: 27 July 2010

Version 1