# Annex 1 to summary of responses

July 2020

# Our other previous proposals

1. Respondents to the consultation took the opportunity to comment on several areas that relate to our earlier consultation. These points together with our response are discussed here.

***Barristers and experts***

2. Some respondents took the opportunity to repeat concerns that our proposal in the first consultation to exclude payments to barristers and experts would undermine trust in the profession. They disagreed with our view that barristers and experts necessarily had expertise to protect own interests and they may be inclined to stop working for instructing solicitors because of fears of not getting paid.

3. Leicestershire Law Society also said that the exclusion of barristers/experts from making a claim on the fund could impact on small firms and sole practitioners as barristers and experts might choose to work for larger firms from who they will seek greater certainty that they will be paid. The Law Society made a similar point and suggesting that this may negatively impact on access to justice.

*Our response*

4. We remain of the view that we should exclude application from barristers and experts. Our rationale remains that the fund should not be used as a substitute for debt recovery or claim for breach of contract processes There is a contractual relationship between barristers and experts working with instructing solicitors and usual commercial practices can be adopted.

***Exclusion of large businesses, charities and trusts from eligibility***

5. We did not ask a specific question about our current exclusion for large businesses. However, the Law Society's response raised concerns about the existing use of hardwired eligibility criteria linked to the wealth of businesses. Its view was that businesses with an income of over £2m should be eligible if they could prove that a non-payment of their claim would result in hardship and that in some instances the business would not be sophisticated enough to look after themselves in the event of that they lose money as a result of their solicitor's actions.

6. It also expressed concerns that we said we were proceeding with our proposal to extend this exclusion to large charities and trusts. In its response, it stated that charities cannot hold substantial reserves so that while they might have income of more than £2m, (as a result of large donations) this did not necessarily mean they had assets to cover the losses caused by a solicitor or be in a position to mitigate the impact of a loss. Its view was that as a result,

ultimate beneficiaries of charities could be disadvantaged and given the work charities do it was likely that a large proportion of their beneficiaries could have protected characteristics. This change could, therefore, have unintended consequences for those beneficiaries of charities if a grant was not made and especially so where the beneficiaries were protected under the Equality Act.

*Our response*

7. The decision to exclude large businesses from eligibility was made in 2015. We remain of the view that when buying legal services, they are in a position to make informed decisions, understand the risks involved and therefore better able be able to put safeguards and controls in place. They should also be able to bear the impact of a loss better than individual consumers or small businesses. We do not consider it should be a priority of the fund to protect them.

8. Larger charities with incomes of more than £2m are likely to have a structured governance regime and will most likely be registered as a company or at least operate like one[1]. Many large charities will have trading arms set up to carry on discrete work or projects and will have large and sophisticated marketing operations. Like businesses, some will compete against similar bodies. Many charities will enter into commercial partnerships to raise funds and profile.

9. Large charities and trusts, like businesses will often face complex legal problems. Charities, for example, may seek advice on drawing up contracts, reviewing a trust deed or being involved in a commercial dispute. When deciding to instruct an external lawyer, the charity is likely to have in-house lawyers. The Charity Commission has provided guidance on what charity trustees need to know when thinking about taking or defending legal action generally, and when the Charity Commission needs to be involved[2]. Trustees of a large or complex trust are also likely to seek professional advice on how they should comply with their obligations and how the trust should be managed.

10. Charities will often be left gifts or legacies in a person's will. Unlike when purchasing legal services, the charity will have limited, or no, influence over the choice or actions of the probate solicitor. This puts them in a different position than when purchasing a legal service. There is a particular risk where the solicitor is the sole executor and there are no other executors that could have influenced how the matter was handled. Our data shows that we have made payments to large charities such as Cancer Research and the NSPCC for

[1] The guidance for charities with a gross income exceeding £1m confirms that an annual return, trustees' annual report and audited accounts must be filed with the Charity Commission
[2] https://www.gov.uk/government/publications/charities-and-litigation-a-guide-for-trustees-cc38

missing legacies when they have made a claim to the fund as the 'residual' beneficiary of the estate. These payments have been as high as £146,000.[3]

11. This risk and potential impact of lost legacies on the financial position of the charity is one of many factors that will need to be considered as part of the financial management of the charity and their reserves policy. There is no requirement for, or restriction on, a charity to have a particular level of reserves. In their guidance[4], the Charity Commission suggests that each charity should assess this after considering its income, outgoings and risk so any target level of reserves should depend on individual circumstances. Trustees of large charities are often experienced professionals who oversee their charity's reserves policy.

12. We therefore remain of the view that large charities and trusts should be subject to the same eligibility criteria as large businesses. A large charity is likely to possess the expertise necessary to put in place, monitor and review a reserve policy that builds the financial resilience to manage the risk and or impact of missing legacy donations and have the resources and know how to seek to recover these losses in other ways where possible.

13. Where there are other individual executors of an estate, or other beneficiaries, they will continue to be eligible to make an application to the fund and they could make a payment to the charity or trust on receipt of a payment. We do not have data on how may claims we receive from individual estates where probate money includes legacy donations.

14. The charity or trust will also be able to take legal action themselves to recover any missing legacies from the defaulting solicitor or firm.

15. This view also applies to large trusts that are more likely to operate through structured governance and controls in respect of decisions that it makes including when to engage the services of a professional adviser to help on matters affecting the trust and when seeking to recover any lost monies.

***Reduction in the maximum payment from £2m to £500,000***

16. Some respondents when responding to how we should apply the single claim limit took the opportunity to comment on the proposal we said we would proceed with to reduce the maximum grant from £2m to £500,000 and only make a higher payment in exceptional circumstances. In the first consultation,

[3] Income received from legacies will form part of the £2m cut off for eligibility to claim from the Fund. Lost legacies, without other redress, will not usually count towards the income calculation

[4] Charities reserves: building resilience (CC19) https://www.gov.uk/government/publications/charities-and-reserves-cc19/charities-and-reserves

we received strong opposition to the proposal. This was repeated in the feedback to the second consultation, mainly based on a principled position that we should not be reducing consumer protection.

17. Both the Legal Services Consumer Panel (LSCP) and the Law Society reiterated their strong opposition to this change arguing that given the low numbers of people affected the resulting reduction in the liabilities of the fund would be limited.

18. Some respondents also raised concerns that the reduced claims limit may have a disproportionate impact on small firms and their clients. This is because sole practitioners and small firms are more likely to have insurance claims refused where there has been dishonesty, on the basis that the sole practitioner or all partners were complicit in the dishonest act. In these circumstances the clients of sole practitioners or small firms will only be eligible to claim up to £500,000 from the Fund whereas in larger firms the insurance cover will be a minimum of £2m per claim. The view was that this difference may put people or lenders off using small firms that are already facing difficult market conditions.

19. The Law Society said that if the £500,000 limit was an unavoidable necessity, then there should be a generous interpretation of 'exceptional circumstances' when deciding whether to pay more than the limit in any particular case.

20. The Association of Professional Injury Lawyers reiterated its concerns that the reduction from £2m to £500,000 would mean that many severely injured clients could be left without adequate compensation.

21. The Ecohouse Creditors Representative also raised concerns about the reduction in the maximum grant.

*Our response*

22. In response to comments received about the reduction in the maximum grant payable, we have updated our data on impacts and explored the issue raised about potential impacts on small firms and those that use them.

23. Our updated information provides us with comfort that:

- the absolute level of protection provided is proportionate and will provide full protection for the overwhelming majority of people: only 32 payments over the period 2004 - 2019 have been above £500,000 which is 0.2% of all payments. For conveyancing and probate the limits cover at 90% and 96% of all transactions respectively

- that characteristically vulnerable (older, lower social grading, BAME, disabled) are less likely to use the types of legal services that give rise to large claims on the fund (conveyancing and probate). They are also

less likely to use a small firm (eg 48% of black African/Caribbean people used small firms compared to 78% of white people; and 67% of disabled people who are limited a lot, compared to 77% no disability) [1], and

- the likelihood that small firms will be undertaking work that may involve very large sums of money that would not be covered by the £500,000 limit is low. For example, our data suggests that nearly 9 out of 10 small firms either derive less than 25% of income from conveyancing work or are located outside of property hotspots.

24. We do not consider there to be any significant new evidence that impacts on our original rationale for this proposal. We considered this to be a fair and proportionate maximum payment level, which compares favourably against comparable schemes including those of other legal services regulators and for other professional services. And this would cover the vast majority of claims

25. We will publish guidance which sets out the exceptional circumstances in which we think a higher grant should be made. By their nature, exceptional circumstances cannot be comprehensively defined. We would expect that it would be rare for more than £500,000 to be awarded. We will bear in mind that the intention of the rule is to limit the vast majority of claims to that amount or below.

26. Factors that we will consider will include:

    - The impact of the loss on the claimant. We are more likely to find exceptional circumstances where the loss has a potentially catastrophic impact on the claimant's quality of life.

    - The likely duration of such an impact and the ability of the applicant to "make up" losses by other means.

    - The extent to which the wider public confidence in the administration of justice is impacted by the loss.

***Application costs***

27. We said in the second consultation that we would proceed with the proposal to exclude payments associated with the cost of making an application to the fund.

28. The objective of this proposal was to target the operation of the fund on its core purpose of making good the direct financial loss caused by the actions of the solicitor or law firm. We stated that it was our view that it should not be necessary for an applicant to seek professional help to make an application to the fund. We said that we would make sure the application process is made as

simple as possible and that we have appropriate support available to help applicants through the application process

*Summary of responses*

29. The LSCP repeated concerns that this proposal would negatively affect vulnerable consumers. Their view was that some consumers will need independent and paid for support, especially at a time when free advice services and support is dwindling and overstretched. The Law Society also felt that the proposal might discourage applications from consumers who for reasons of poverty, lack of ability or literacy skills, or because of a vulnerability of some other kind, would be unable to make an application without proper assistance.

*Our response*

30. Our approach will be to help the applicant to present the facts that we need to make a fair and robust decision.

31. We are reviewing our online guidance to make sure it clearly sets out: who is able to claim, what types of claim we will consider, what information we will need, how to complete the application form, top tips for common issues.

32. Through our modernising IT work, work is underway to simplify the application form and provide assistance to applicants as they fill out the form. This work also includes simplifying the process for applicants to submit their form and how we communicate with them at different stages of the process.

33. We are developing new guidance and training for staff around supporting the applicant through the process and advising them on the information needed to help establish the facts of a case and ways to obtain that information. We may also seek further information ourselves, including from the relevant solicitor or firm to inform our decision making. It is for us to make a judgement based on the facts, not for the applicant to “prove” that we must grant the application.

34. Updated guidance and training will also make sure teams have the appropriate tools to help for example, those applicants with disabilities and where reasonable adjustments might be needed.

35. We also plan to continue to explore with charities and other organisations people may turn to for advice when they suffer a loss at the hands of a solicitor and how we can provide guidance and support to help them.

36. The applicant will also have the option of challenging any decisions that we may reach on the merits of a case. We will advise them of their options in relation to this, including seeking independent legal advice and different funding arrangements that may be available e.g. contingency fee arrangements.

37. Historically, most applicants do not instruct professionals to assist them in making their claim. We intend to undertake some consumer research with some that have so that their insights may inform our work programme.

38. We remain of the view that the fund should be focused on providing redress for direct financial losses and it should not be necessary to seek professional help to apply to the fund. We are confident that the work programme set out above will make the process as straightforward as possible and will support applicants, and particularly, vulnerable applicants.

***Litigation costs***

39. We also confirmed we would proceed to exclude litigation costs other than in exceptional circumstances. This is to prioritise payments that provide redress for direct financial losses and to protect against the risk of being tied to paying for escalating litigation costs.

*Summary of responses*

40. Concerns were raised in the first consultation about the impact on applicants' ability to pursue other avenues of redress. These were repeated in the second consultation with the Law Society arguing that is was unfair on those who may have been entirely reasonable in seeking to recover their losses through litigation which, if successful, might obviate the need to apply to the fund for part or all of their loses.

*Our response*

41. As set out in our earlier response our approach is to factor individual applicants' ability to pursue other avenues of redress in deciding whether this is realistic for them or we should proceed to process their claim. We do not expect most individuals to pursue other redress which have high costs. particularly given that payment from the fund might be low relative to those costs.

42. In this context, we reserve the right to pay some costs on an exceptional basis, proportionate to the nature of the application.

43. We will publish guidance and case studies to explain what we mean by exceptional circumstances.

***Insolvent insurers***

44. We confirmed that we would adopt our first consultation position to limit applications to the fund relating to a firm having failed to get the required insurance, to firms that were authorised by us. We also set out that we will not make grants arising from an insurer's insolvency, for example where run-off policies have been disclaimed by a liquidator as part of the winding-up process.

*Summary of responses*

45. The Law Society raised its objections stating that the proposal would see the removal of a significant element of client protection. Its view was that if neither compensation nor insurance are available, then consumers could be left exposed to losses without any avenue for redress. The Westminster and Holborn Law Society was also concerned about this and that the insolvency of an insurer can affect a firm of any size. Its view was that if we proceeded with this proposal then the fund was of no conceivable benefit to large firms or to their clients.

46. The LSCP stated that at the time of drafting and the publication of our consultation there was no doubt that the circumstances of insurer insolvency had been and would be rare. It stated that the situation created by Covid-19, however, might make this less rare and we needed to reconsider the proposal. The PNLA also felt that it was not right to exclude claims that arose out of an insurer's insolvency especially so because the law firm had obtained the required PII cover but through no fault of the firm, the insurer failed to pay. Its view was that if the fund did not pick up these claims it could leave consumers "…*out of pocket potentially for many years whilst coverage and insolvency procedures are followed*…".

*Our response*

47. Where an insurer has become insolvent we have worked closely with its regulator and the appointed insolvency practitioners to make sure that information is provided effectively to persons with a claim against the firm and how future claims are likely to be dealt with.

48. Our view remains that the fund should not be a last resort for any financial loss suffered by the client of a solicitor. We will continue to discuss with the Financial Conduct Authority whether there may be changes to Financial Services Compensation Scheme for consumers of large law firms to be able to claim on their scheme when an insurer becomes insolvent.