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CONSULTATION ANALYSIS – To make interim amendments to the CILEx Regulation Compensation Arrangements Rules

The consultation proposing interim amendments to the CILEX Compensation Arrangements ran from 16 July 2021 to 13 August 2021 and was covered in the CILEX Member Newsletter on 22 July and 27 July. We advised all CILEX Authorised Entities on 19 July by email. The Consultation was advertised on social media on 16 July, 27 July and 12 August.

The Senior Management Team, including the Board Chair designate made direct contact with two key stakeholders:

- Competition and Markets Authority (CMA)
- Legal Services Consumer Panel (LSCP)

We received responses from:

1. The LSCP, and
2. A CILEX member

The CMA thanked us for drawing the consultation to their attention but made the decision not to respond, beyond sympathising with the sudden withdrawal of cover.

The Chair of the LSCP and the Chair elect of the CILEx Regulation Board have had a discussion in relation to the proposals in addition to their formal response which we have responded to in detail below.

The CILEX member sought clarifications in relation to the effect of the withdrawal of insurance cover and interim proposals on their firm.

General themes raised by the responders.

1. The CILEX member asked why the insurance company had withdrawn their cover when it seemed that no claims have ever been made. They also sought clarification that CILEx Regulation was able to secure the level of cover, which is currently being proposed, and whether this would make any difference to the annual compensation fund fee, including any potential refund when the level of cover changes.

CILEx Regulation response:

We advised that the insurance company had made a commercial decision to withdraw from this market and we believed that other regulators may also be impacted. As we had only learned this once the renewal process was commenced by our brokers, we were having to react swiftly; we confirmed that the claims history has been very good.

We advised we were looking at the options as to how the proposed new arrangements are underwritten going forward but again, subject to the consultation responses and LSB approval, we need these to be in place very soon.

Lastly, we confirmed that the fee that a firm pays, is a contribution to the fund and not a contribution to the payment of the insurance premium.

2. The LSCP recognised the need for CILEx Regulation to introduce changes at short notice to address the non-renewal of the insurance policy underwriting the CILEX Compensation Arrangements. However, they raised a number of issues and we have responded to each of these in turn:

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- a. Data transparency: the LSCP noted that the CILEX fund has not had any claims but noted that a review of claims from other regulators would have been helpful, including any data sets used by the actuary in his analysis.

CILEx Regulation response:

In the short timeframe available, CILEx Regulation managed to meet with other legal regulators, however although they are willing to share data on their claims' histories, the timeframe precluded inclusion of this to support this application. The actuary was however provided with data which is in the public domain from the SRA compensation fund to support his calculations and risk assessment.

For our longer-term review, which will take place over the next 12 months, we will seek this additional data to support any changes to our approach. As these data sets belong to 3rd parties, CILEx Regulation may not be able to share these publicly and a similar issue arises in relation to data which CILEx Regulation provided to the actuary in relation to our law firms. This data is likely to be commercially sensitive and could identify individual firms given the small numbers that CILEx Regulation currently regulates. CILEx Regulation is committed to being transparent and will publish all data that we are able to do to support our future applications.

- b. Actuary's opinion: the LSCP queried whether the actuary had fully considered all aspects of the compensation scheme, given the opinion letter only referenced dishonest misappropriation and dishonest failure to account.

CILEx Regulation response:

The full actuarial report extended to 14 pages and did include the wider civil liability element of the compensation arrangements. However, disclosure in relation to the document was restricted owing to the confidential and sensitive information contained within it (it contains data in relation to third parties and opinion in relation to other issues). Disclosure of the full document has been made to the LSB as part of the application.

- c. The potential to revert to the scheme in operation prior to 2017

CILEx Regulation response:

There are two reasons why CILEx Regulation could not revert to the previous scheme. Firstly, we have, through our broker, sought alternative insurance policies, both at current and lower levels of cover, but have so far been entirely unsuccessful. Therefore, the insurance element of the earlier scheme would not be possible at present.

Secondly, the scheme was changed to ensure that there was a balance between the provision of adequate consumer protection on the one hand against affordability to the CILEX Group on the other.

Our proposal seeks to ensure that the scheme can continue to provide consumer protection whilst maintaining the viability of CILEX and CILEx Regulation as an entity regulator. In reaching this decision we have relied on the independent view of the actuary that we engaged, i.e., that in his opinion, the risk of a claim on the fund at all is remote and that based on data published by the SRA average claims for conveyancing are in the region of £230,000 - £260,000. It should also be noted that we have increased the claim and fund size from the actuary's minimum viable recommendation of £250,000 to £500,000, which is the same as our current maximum discretionary grant. This we consider balances the ongoing consumer protection requirements with affordability to the profession. We are however

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committed to continue to seek alternative cover which would enable us to increase the size of the fund. We will also be working with the actuary over the next 12-month period to determine the minimum viable arrangements for the CILEX compensation arrangements for the long term.

Responses to the questions

Q1. Do you agree with the approach that CILEx Regulation has taken to ensure there is ongoing consumer protection for the clients of firms regulated by CILEx Regulation?

Yes/No? Please provide comments:

The LSCP responded to this question. They did not however support or otherwise the approach CILEx Regulation has taken. They do support the maintenance of the maximum discretionary grant amount at £500,000 but highlight the limitations of total fund being set at the level of one maximum claim. They also note that there is insufficient data for them to fully assess the proposal (this is addressed above). On the whole, the LSCP acknowledges that in the timeframe available there was no other viable option for CILEx Regulation to consider, but that in the next 12 months, CILEx Regulation should take into account the risk of consumer detriment if the fund is extinguished.

CILEx Regulation response:

We acknowledge that there is a remote risk that the fund will be exhausted within the 12-month interim period, however we have used the actuarial analysis of the CILEX authorised entities to determine that the risk is very small. At the same time, we acknowledge that we need to undertake further analysis and consider a range of options and we undertake to carry out this work over the next 12 months.

Q2. CILEx Regulation has set out this approach to cover the next 12 months, do you have any views on the longer-term approach that CILEx Regulation may take to ensuring the protection of clients of CILEx Regulation firms?

Yes/No? Please provide comments:

The LSCP has provided a series of helpful comments in relation to the development of a longer term, sustainable solution to the compensation arrangements for CILEX entities.

CILEx Regulation response:

We will take these on board as part of our research and development of new proposals during the interim period.