

The only Risk Management newsletter published by practising solicitors

Professional indemnity
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 Anti-money laundering
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 Risk Management
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 Partnership
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 Conduct

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Risk management trends: Forecast for 2007

Effective risk management involves not only a review of what has gone right or wrong in the past, to which many law firms limit their focus in our experience, but an assessment of what might go right or wrong in the future.

For us as practising solicitors, this in turn involves an assessment of what is happening in the areas in which we practise – both work type and geographical, and the likely or possible effect of changes in the economy on both the firm and its clients, and changes in the law. These involve recent decisions here and abroad (which may influence thinking here or impact on our potential overseas liabilities) and legislative change, particularly the Legal Services Bill.

Levels of litigation tend to be linked to the state of the economy –

first because people who have lost money are more likely to look for a scapegoat and sue, and secondly because breaches of duty are more likely to be detected. So the fall in the property market in the late 1980s and early 1990s resulted in a large number of property related claims in the United Kingdom. Some involved fraud which in many cases would have gone undetected in a rising market. Problems in the property market in the United States can be expected to result in increased claims there.

For anticipated trends in property related claims see an article by Legal Risk partner Frank Maher in Insurance Times of 7 December 2006 <http://www.claimscouncil.org/news/2006/12/07/calm-before-the-claims-storm>.

Remember - we are not just looking for where next year's *claims* will come from, but the underlying risks, which may not materialise into losses for several years, a point exemplified by the long time lag in pensions and endowment misselling claims which affected several firms.

Anti-Money laundering

Not forgetting Counter-Financing of Terrorism, which is gaining increasing importance – emphasised by the 2006 guidance from the Joint Money Laundering Steering Group. We are seeing signs of an increased police focus on money laundering when in the past they might have focused on other crimes which attracted lesser sentences.

It is nearly three years since wider aspects of legal work became part of the regulated sector and retraining in many firms is long overdue, even before taking account of new recruits, as much has happened in the meantime and attention will almost inevitably have slipped. Draft Regulations implementing the Third Money Laundering Directive are expected in January 2007 and draft revised guidance from the Law Society in the Spring, but they should not be seen as a reason to delay training.

A City of London Report by The British Institute of International and Comparative Law examines the comparative implementation of the EU Second Money Laundering Directive in various EU states.

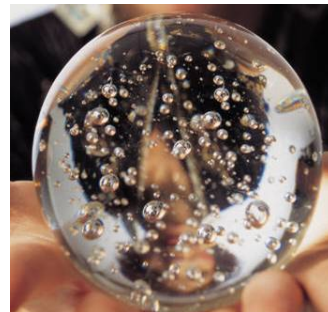
For help with training, and legal advice on policies and procedures, production orders, and privilege issues contact sue.mawdsley@legalrisk.co.uk

Aggressive tax planning

At least one major accountancy firm has had a number of claims following HM Revenue and Customs (HMRC) into investigations into aggressive tax planning schemes. Increased interest in off-shore accounts makes such claims more likely and law firms are unlikely to escape the net. Revenue incentives to tax inspectors to bring in extra cash, reported in The Times of 2 January 2007, may increase their activity.

Code of Conduct for Solicitors

The Code is expected, belatedly, to receive statutory approval in the summer. Rule 5 will require all firms to implement risk management and business continuity. **Read on...**



Looking into a crystal ball for the risks ahead

Continued

Compulsory Risk Management

Will you be able to demonstrate compliance? Do you have procedures, and check they are applied in practice? And just as important, can you prove it? We have been helping numerous firms here and abroad build a risk management strategy. As part of that process, we have used our Desktop web diagnostic tool to test law firm staff in six jurisdictions on their understanding of their firms' procedures with some remarkable findings - problem issues which could result in large liabilities or failings in the firm's strategies, in many cases put right easily and at little or no cost. Desktop provides firms with a record of testing which can form part of the audit trail to demonstrate compliance.

The British Standards Institute is developing a Code of Practice on Risk Management. **For help with compliance and web-based testing of staff and for training on the Code of Conduct by practising solicitors who understand firms like yours contact info@legalrisk.co.uk**

Business Continuity Planning

This too becomes compulsory, and will become a requirement of Lexcel from March 2007. The British Standards Institute has established a code of practice BS 25999-1:2006. (This replaces PAS 56.) Business continuity is not just about disaster recovery: it may cover matters as mundane as telephone failures, power cuts and police cordons preventing access to your building. If you have a plan – do your staff know about it and have you tested it? A recent survey by the National Emergency Response and Rescue Training Center in the United States found that most companies there had formed a plan but one in four had not tested them or trained staff. Increasingly firms are seeking alternative office facilities for use in the event of emergency. **For further information on planning and available facilities contact frank.maher@legalrisk.co.uk**

Cross-border risk: Litigation futures

The spectre of hedge funds investing in litigation in Australia raised its head in a brief comment in The Times of 28 December 2006. While this may not yet be possible in the United Kingdom it may be of concern to those with cross-border practices and to our many overseas readers, as one can well foresee this being of possible interest in cases involving collapse of major financial institutions. The report follows a decision in **Fostif Pty Ltd v Cash & Carry Pty Ltd** [2005] NSWCA 83, in which the Court of Appeal of New South Wales held that champerty was not in itself an abuse of process.

Legal Services Bill

A new complaints regime will affect all firms as we warned in our October 2006 newsletter. It is not just a question of how you do the work in the first place - we can expect an increasing number of awards against firms who have done nothing wrong in dealing with the work but whose complaints procedures are found inadequate. Couple that with an increase in limits for inadequate professional service awards, with current predictions up to £100,000, reduced opportunity to take technical defences such as limitation, and law firms and their insurers may be in for some heavy expenditure. Law firms should be ensuring that their complaints procedures and client engagement have been revised in accordance with the Law Society's May 2006 guidance. Insurers' proposal forms should check that firms have done so. **For help with complaints procedures, complaints handling, engagement letters and terms contact info@legalrisk.co.uk.**

Claims by non-clients

We commented in our October 2006 issue that increasing trends for these have been noted by insurers across the world and referred to recent American authority. In the past, the risk may have focused primarily on disappointed beneficiaries under wills, breach of warranty of authority in conveyancing resulting in claims by lenders and other parties, and claims assigned in insolvency.

Investors worldwide are increasingly flexing their muscles following corporate collapses however. Vendor due diligence is moving up the risk management agenda, and a number of high profile failures of companies listed on the Alternative Investment Market are a cause of concern: 'light touch regulation' may be synonymous with insufficient regulation. See also *Cross-border risk: Litigation futures* above.

Directors of company clients, partners and partnerships, trusts and trustees – not clarifying who you are acting for – are all risk issues.

Age discrimination

This has attracted much comment elsewhere. Have you updated your partnership agreement? **For advice on partnership agreements and litigation contact frank.maher@legalrisk.co.uk**

Equity release – both lenders and borrowers at risk

We warned of this in our January 2004 edition. It will take some years for claims to filter through but the concerns are real. Similar schemes are also causing concern in Australia. Supposedly 'safe' schemes with no-negative equity guarantees may have induced complacency, but even these involve risk to both lenders and borrowers. Space does not permit more detail. Legal Risk partner Frank Maher acted for defendants in the group litigation in the 1990s. Although the Law Society of England and Wales has issued guidance, we do not believe that it will prove sufficient to help firms avoid claims. **For advice contact frank.maher@legalrisk.co.uk**

Mergers, acquisitions, lateral hires and dissolutions

We frequently see partnership merger and dissolution agreements which show fundamental misunderstandings of how professional indemnity policies work and the liabilities which may not be covered, and ignore opportunities for significant cost savings and offloading of risk. Particular problems arise because of the 'successor practice' provisions in the Law Society's Minimum Terms and Conditions of insurance, but that is merely the beginning of the matter. Merging law firms are making regular gratuitous donations to the insurance industry.

Our recent engagements include advising law firms on lateral hires in the UK, Europe and Asia. Insurance issues are important but there are many other considerations. We can provide a checklist specifically focused on lateral hiring. **For advice on these issues contact frank.maher@legalrisk.co.uk**

Continued ...

Risk transfer: insurance

Professional indemnity cover is only the start. Our forthcoming Top 100 Law Firm Professional Indemnity Survey, to be published early in February, will include information on the extent to which firms are taking out management liability cover (similar to Directors and Officers cover) and 'Lifeboat' policies, which cover residual personal liability for which incorporation as a Limited Liability Partnership (or otherwise) may offer no protection. **We are recommended by Legal 500 for professional indemnity. For advice on professional indemnity issues, including claims, coverage and litigation contact frank.maher@legalrisk.co.uk**

Referral fees

A programme for tough enforcement of the rules on referral arrangements has been agreed by the Solicitors Regulation Authority – the new body that regulates the profession in England and Wales. Checking that solicitors are following the rules and principles will become a priority for the investigation teams of the SRA. The SRA has also threatened to seek criminal sanctions for non-compliance with the rules.

Its predecessor, The Law Society's Practice Standards Unit, found that only six per cent of firms were compliant. We have been helping a number of firms with their compliance in advance of SRA inspections. **For a fixed price health check contact frank.maher@legalrisk.co.uk**

Top 100 Professional Indemnity and Risk Management Survey

This will be published early in February. Last year's survey attracted considerable press interest. In addition to the hard copy circulation, 1183 copies were downloaded from our website with a further 367 copies of a reprint published in Australia. We have had a large number of replies including an increased number of the larger firms. If you are a Top 100 firm and have not yet responded there are still a few days left to do so.

2007 Events

Legal Risk partners Frank Maher and Sue Mawdsley will be speaking at several events including

- **Milan** (14 March),
- **London** – Workshop: Conducting a Risk Audit for Law Firms (21 March),
- **Munich** - International Bar Association (28 September), and
- **Paris** - Queensland Law Society, Australia (18 October).

For further information contact info@legalrisk.co.uk

www.legalrisk.co.uk - Record Hits

Our website attracted a record number of hits in 2006 - nearly 20,000 - a 34 per cent increase on last year. A staggering 26,596 documents were downloaded. There were many visitors from overseas, including large numbers from the USA, Australia, Brazil, Russia, India, China, South Africa, Singapore and Malaysia to name but a few.

Popular downloads included 1817 copies of three articles on mergers and lateral hires, on which we have advised many firms on risk and insurance aspects both here and abroad. There were also 1226 downloads of articles and information packs on successor practice issues under the Law Society's Minimum Terms and Conditions. 4723 copies of back issues of newsletters were also downloaded. Our Partner Asset Protection Plan information attracted 404 downloads and an article on the subject 780, in addition to those following the link to Legal Week.

And finally... one unidentified visitor found our website by asking a search engine 'Does fraud stop you working as a solicitor in the UK!' We hope so - we have helped many firms with 'rogue partner' issues.

About Legal Risk

We are a law firm. We act for many leading UK and overseas law firms and their insurers, as well as many smaller firms and members of other professions. We specialise in risk management, professional indemnity, partnership agreements and litigation, anti-money laundering, compliance and disciplinary. Recent and current engagements include -

- Multi-million pound claims for insurers
- Advice to law firms on The Accident Group issues
- Money laundering - production orders
- Risk assessment of overseas, offshore and UK law firms
- Advice on managing cross-border risk issues
- Terms limiting liability

For further information see our website www.legalrisk.co.uk or contact info@legalrisk.co.uk.

THIS NEWSLETTER IS A GENERAL GUIDE. IT IS NOT A SUBSTITUTE FOR PROFESSIONAL ADVICE WHICH TAKES ACCOUNT OF YOUR SPECIFIC CIRCUMSTANCES AND ANY CHANGES IN THE LAW AND PRACTICE. SUBJECTS COVERED CHANGE CONSTANTLY AND DEVELOP. NO RESPONSIBILITY CAN BE ACCEPTED BY THE FIRM OR THE AUTHOR FOR ANY LOSS OCCASIONED BY ANY PERSON ACTING OR REFRAINING FROM ACTING ON THE BASIS OF THIS.

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Regulated by the Law Society

The firm is not authorised under the Financial Services and Markets Act 2000 but we are able in certain circumstances to offer a limited range of investment services to clients because we are members of the Law Society. We can provide these investment services if they are an incidental part of the professional services we have engaged to provide.