

*In this issue ...*

- Compliance with Rule 5 of the Solicitors' Code of Conduct
- Top 100 Professional Indemnity and Risk Management Survey 2009
- Lessons from the USA
- Liability of Professional Indemnity Partner to co-partners
- Publication: Risk Management in the Legal Profession
- Referral self-audit for compliance



Report from the Legal Malpractice & Risk Management Conference 2009 held in Chicago.

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## Compliance with Rule 5 of the Solicitors' Code of Conduct

Readers may have seen the article by Peter Williamson, chairman of the Solicitors Regulation Authority, in the Gazette of 12 March 2009 warning solicitors against reducing their compliance and supervision during the recession. <http://www.lawgazette.co.uk/opinion/by-the-book/compliance-must-not-be-ignored-when-tackling-recession>

We have however already encountered evidence of firms reducing the size of their risk management teams. We comment further on the size of risk teams below.

A key focus of the SRA's attention is compliance with rule 5 of the Solicitors' Code of Conduct 2007, which exposes the principals in a law firm to disciplinary action, if they fail to implement systems for the supervision and management of their practice.

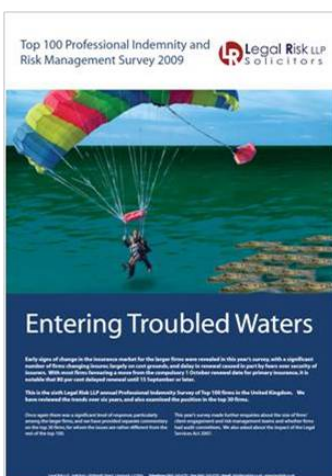
Legal Risk LLP have produced 'A Practical Guide to Rule 5 (Business Management) of the Solicitors' Code of Conduct 2007' to help firms with their compliance (price £10). There has been a marked increase in firms asking for help in preparing for SRA inspections (both routine and otherwise), compliance checks on other areas such as referral arrangements, and advice on conflicts issues.



**For legal advice on compliance, or to order a copy of the publication, contact [info@legalrisk.co.uk](mailto:info@legalrisk.co.uk)**

## Top 100 Professional Indemnity and Risk Management Survey

Legal Risk LLP has released its sixth annual survey on top law firms' professional indemnity and risk management. The response equalled last year's record with 64 firms replying, including 22 of the top 30.



Concerns over security of insurers delayed renewals for 16 per cent of firms and 20 per cent of the top 30, and a large number of firms changed insurer – 14 per cent of the 64 respondents, equalling the previous 2003 record, and a remarkable 23 per cent of the top 30.

Professional people need to appreciate that it is not only the security of insurers at the time of renewal which is a concern, but long into the future when claims under the current policy may fall to be paid. The writer defended a top firm on a multimillion pound claim where one of the relevant excess layer insurers was Independent, following the insurer's collapse; this is therefore a very real concern, and a reason to review terms limiting liability and policies in applying them to maximise the prospects of being able to rely on them.

We have advised many firms of all sizes on limiting liability, including ten of the top 100, overseas firms, and firms specialising in high net worth clients and other high value work, and Legal Risk LLP partner Frank Maher has provided an expert report for use in High Court proceedings on the nature and extent of large firms' terms limiting liability.

*Continued ....*

**Top 100 Professional Indemnity and Risk Management Survey (continued)...**

Liability caps are not the only issue – time limits for claims are another aspect to consider. So too is the avoidance of responsibility for the proportion of any claim due to the fault of other potential defendants, particularly when their insurance may also be in doubt, may not be as wide as yours, and may be for far less than solicitors are accustomed to buying – counsel in particular have relatively low limits in practice in most cases.

Our survey shows that top firms have little appetite for the Legal Services Act reforms allowing non-lawyer partners in Legal Disciplinary Practices from 31 March 2009. This presents opportunity and risk for multinational firms – the danger of imperiling their status in some jurisdictions, against promotion to partnership for other specialists such as patent attorneys or tax specialists who may be allowed partnership status in other jurisdictions.

77 per cent of the respondents have now converted to Limited Liability Partnership (LLP) and only a dwindling minority of 9 per cent have no present intention to do so. Perhaps driven by conversion to Limited Liability Partnership, focusing minds more on risk and governance issues, 51 per cent of firms have an audit committee, and 60 per cent of the top 30. Audit committees' terms of reference will vary from firm to firm, but essentially they review the firm's financial reporting, internal control and risk management, and internal and external audit.

The survey also contains information on the size of firms' client engagement and risk management teams which averaged five and three respectively. Further details appear in the survey.

53 per cent of firms responding take out Directors' and Officers' liability cover. This raises interesting issues, because external appointments can pose particular risks. A member of our practice advised insurers on a claim against a lawyer in another jurisdiction who was a director of a bank which collapsed. Clients who invested in the bank alleged that he was in breach of duty in failing to advise them to put their money elsewhere, putting him in conflict with his duty as director.

It can often be difficult to separate the advice as director from advice as a lawyer, and it is essential that controls are put in place, covering acceptance of appointments, and how the advice is provided. It is easy for non-lawyers on boards to assume that the lawyer in their midst is expert in all areas of law. Further comment on conflicts appears below.

36 per cent of top 30 firms, and 16 per cent of top 100 firms, have management liability insurance. We comment further on this later in this issue.

As the Law Society and SRA consider whether the compulsory insurance renewal date of 1 October should remain, a significant proportion of firms – 77 per cent and 81 per cent of the top 30 – favour a choice of date.

The full survey is available for downloading [here](#) and includes six years' data on firms' choice of insurers and brokers.

***For legal advice on limiting liability and terms of business contact [info@legalrisk.co.uk](mailto:info@legalrisk.co.uk)***



## **Lessons from the USA**

Legal Risk LLP partners attended a packed law firm risk management conference in Chicago. The following are some of the key issues which may interest a wider audience.

### **The future shape of law firms**

The traditional leveraged model of law firms with large numbers of associates was under attack from clients' general counsel, one commenting that partner: associate ratios of 1:1 delivered better results than 2 or 3:1 – 'the shape of the successful law firm is not a pyramid'. We know UK firms with corporate practices are increasingly under pressure to service in-house legal teams with specialist advice rather than do whole transactions – as one risk management partner put it succinctly, firms are being asked to take 10 per cent of the fees and 90 per cent of the risk.

*Continued ...*

### ***Lessons from the USA (continued)...***

Interestingly, the Legal Services Act opportunities for external investment in law firms were perceived as giving rise to a competitive advantage for UK firms over US firms; lack of interest to date from the larger UK firms would suggest this may not be an issue. We have advised a number of insurers' in-house legal departments and law firms on structural issues arising from the introduction of Legal Disciplinary Practices on 31 March 2009 and, further down the line, Alternative Business Structures. The latter are expected to be in place in 2011 or 2012 and permit outside ownership.

It was said that the cost of services to large corporations in the past ten years has risen 20 per cent, but law firm fees increased by 75 per cent - perhaps a blunt and distorting use of statistics which may be influenced in part by the increase in regulation, but one can understand the sentiment behind it.

Firms under pressure on fees from defendant insurance clients might be interested in a case where an insured defended a professional conduct complaint without notice to the insurer; one of the insurer's grounds for disputing liability for the costs was that the fees were \$200 per hour rather than the panel firm's \$115 per hour - even with the battered pound, the figures sound remarkably low to UK lawyers who thought they were poorly paid for this type of work.

### **Insurance predictions**

Insurers have recorded an increase in circumstances but not in paid claims. They are under pressure from low rates and almost non-existent investment income. Fears were expected over claims arising from high profile corporate collapses, fraud and corruption, and failed law firms. Rate increases over the next 12 months were predicted. We have been asked about insurers seeking policy exclusions for claims relating to claims arising from Madoff and Stanford.

### **Client insolvency**

An increasing concern is the risk of being caught up in bankruptcy (including corporate insolvency) proceedings, which can result in wide disclosure obligations, and being prejudiced by the findings of an 'examiner'; the telling comment was made that 'the examiner is not your friend'. Claims for fees against the insolvent company constitute a waiver of the bankruptcy court's jurisdiction, which those with international practices might usefully note; it also has the effect of denying the opportunity of a civil jury trial, practically unknown in our jurisdiction, but the loss of it is perceived as a disadvantage by the Americans.

### **Problems in Intellectual Property practice**

Patent lawyers were very much in the spotlight for liability claims. Diary problems which prevail in professional liability claims around the world are exacerbated by issues particular to US law on when time starts running. Of wider interest to our readers practising in this area is the fear of insurers over international intellectual property advice and documenting the division of responsibility between US and overseas firms, such as the need for overseas firms to provide adequate notice to US firms where time limits are due to expire.

There has been an increase in claims against US firms for intellectual property work done by overseas firms. These may give rise to shared liability and is also a concern for the firms outside the US, particularly if they may be subject to American jurisdiction. Concern was also expressed about general commercial practice firms taking on intellectual property teams 'as a fashion statement'.

Defence costs on intellectual property claims may run to tens of millions of dollars.

### **Law firm mergers and acquisitions**

Acceptance of liability for firms on merger is a significant problem on which we are frequently consulted by UK and overseas firms, exacerbated in the England and Wales by compulsory wording, though we have engineered strategies for dealing with this in a number of cases; we have been instructed in situations arising from the collapse of four US firms. Whether to include cover for acquired practices is optional in the USA, and the desirability of doing so was put seriously in question with one speaker highlighting an instance of this with a particularly adverse outcome.

### **Conflicts**

Conflicts were identified as a particular problem for US firms with lateral hiring of patent lawyers, including problems in addressing conflict checks, and what interests might be construed as adverse. Changes in New York and American Bar Association conflicts rules were also discussed. We advise many firms on conflict and confidentiality issues, and Legal Risk LLP partners Frank Maher and Francis Dingwall presented a Conflicts Masterclass at The Lawyer Strategic Risk Management conference earlier this month.

***Extensive conflicts resources covering over a dozen jurisdictions can be found on our website [www.legalrisk.co.uk](http://www.legalrisk.co.uk).***

***For legal advice on law firm insurance coverage and merger issues, or on conflicts contact [info@legalrisk.co.uk](mailto:info@legalrisk.co.uk)***

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## Liability of Professional Indemnity partner to co-partners

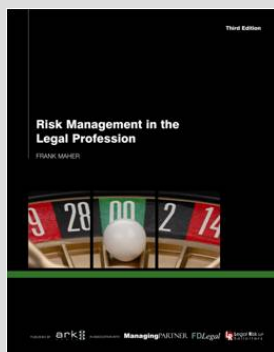
Meanwhile back in England, in **Tann v Hetherington** [2009] EWHC 445 (Ch) an architect and a surveyor were partners. The architect had responsibility for professional indemnity but failed to notify a claim to insurers because he believed it was spurious and thought it would go away, which it did not. The architect was found liable to the surveyor when insurers declined cover. Although the compulsory insurance for solicitors in England and Wales prevents insurers declining cover for a claim, they can – and do – seek reimbursement for prejudice caused by delay in notification, and in some circumstances this can be for the full cost of the claim.

This was a small firm example, but fears of claims against law firm management in larger practices are on the increase, as revealed by Legal Risk LLP's Top 100 Professional Indemnity and Risk Management Survey (see page 1).

Case report link for Lawtel subscribers - <http://www.lawtel.com/content/display.asp?ID=AC0120235>

**For legal advice on coverage disputes with insurers, including representation in litigation or arbitration, contact [info@legalrisk.co.uk](mailto:info@legalrisk.co.uk)**

## Risk Management in the Legal Profession



Now in a new third edition, with the previous edition having sold widely in 29 countries as far apart as Australia, China, Lithuania, South Africa and Canada, the text has substantially increased to cover credit crunch related issues – dealing with practical matters which, if addressed properly, can help save significant cost.

**For further information contact [info@legalrisk.co.uk](mailto:info@legalrisk.co.uk)**

## Referral self-audit for compliance

Referral rules affect even the largest firms – those who think they have none have probably not spotted those they have. While the main battleground of enforcement may have been on the high street, others cannot afford to be complacent. The SRA has found high levels of non-compliance, and this is an issue which is reviewed when the SRA conducts routine Practice Standards Unit monitoring inspections.

It is not only paid-for referrals which are covered by the rule.

Desktop, our online self-audit risk management diagnostic tool, provides a solution for firms wishing to check their own compliance cost-effectively. The cost is £350 plus VAT. Terms apply.

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