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Problem renewals?

Visit the dedicated page on our website at www.path.to/Solicitors2009

We provide legal advice to help obtain cover for solicitors.

- Claims problems
- Coverage disputes
- Dishonesty claims
- Laundry listing
- Lender claims
- Run-off cover
- SRA investigations
- Successor practices

Visit www.path.to/Solicitors2009 or contact Frank.Maher@legalrisk.co.uk



Solicitors' Renewal 2009

The renewal season is underway. The consensus appears to be that premiums may rise by about ten per cent. In real terms, even a 0% increase would be significant, because the turnover in many firms will have fallen. Premiums are likely to be computed by reference to the turnover in the last 2-3 years, because it is the level of activity in those years which will determine the level of claims emerging now, not just this year's depleted income.

Some firms may struggle to obtain any cover at all from qualifying insurers, forcing them to apply to the Assigned Risks Pool for cover at penalty premium rates which will eliminate any hope of profit for most of them. We believe that there could be as many as 500 firms in the Assigned Risks Pool this October.

We are already many seeing firms and insurers come to us for advice on successor practice issues, as well as many fraud claims and a number of sham partnership cases.

We have dedicated a page on our website to the Solicitors Renewal www.path.to/solicitors2009 which aims to help solicitors and their brokers to obtain cover and save money. We provide advice and links on:

- Adverse claims history;
- Current year notifications/laundry listing;
- Dishonesty issues;
- Extent of duty of disclosure;
- Insurer insolvency.
- Mortgage fraud/lender claims;
- Perceived exposure to future claims;
- Risk management;
- Sham partnerships;
- SRA investigations and inspections;
- Successor practices.

For those firms fortunate enough to have a real choice on renewal, remember it is not just about price, or even security. A significant part of what you are buying is the claims handling. Will the claims handling on offer continue to meet your expectations? Larger firms may have more say in who handles their claims. Smaller firms may be less fortunate. Consider also what the prospects are of the insurer being in the solicitor market for the long term; while nobody can be certain, some are far more likely long term prospects than others.

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Insurer insolvency

Legal Risk LLP's Top 100 Law Firm Professional Indemnity and Risk Management Survey 2009 www.legalrisk.co.uk/FileUploads/200956_LegalRiskLLP_Top100_2009.pdf found that concerns over the security of insurers delayed renewals for 16% of respondents and 30% of top 30 firms. This may have reflected the extraordinary events unfolding in the financial world last September, but we are not out of the woods yet.

Smaller insurers might not receive the same support that the world's largest insurer required. Being a 'qualifying insurer' under the Qualifying Insurers Agreement <http://www.sra.org.uk/documents/rules/Indemnity-Qualifying-Insurers-Agreement-08.pdf> does not imply any approval by the SRA or the Law Society; they have not vetted the 'qualifying insurers'.

What happens if an insurer becomes insolvent? The scheme under the Policyholders Protection Act 1975 was replaced by rules made under Part XV of the Financial Services and Markets Act 2000.

The rules are somewhat byzantine. We had a Kafka-esque experience when we made 'mystery shopper' calls to the relevant bodies. When we phoned the Financial Services Compensation Scheme (FSCS), they told us to speak to the Financial Services Authority (FSA). When we phoned the FSA, they told us to speak to the FSCS.

In very broad terms, the position appears to be that a small firm (i.e. a firm with a turnover of less than £1 million) or a sole practitioner, will receive an indemnity in respect of any claim or circumstance validly notified to the insurer before it closed down. However they would be unwise to choose their insurer on the strength of this, as there may be other obstacles to a peaceful night's sleep. We doubt the FSCS has significant experience of defending professional liability claims, and there is also a requirement for the FSCS to set a 'quantification date' for assessing claims, and it occurs to us that this might operate to deny firms a full indemnity for matters which have been notified as circumstances but have not yet turned into claims.

A firm with a turnover of more than £1 million, will have no recourse to the FSCS for claims or circumstances notified, though it may receive a dividend in the liquidation of the insolvent insurer. The Claimant will have a right to payment by the firm, not the insurer.

Quite apart from notified claims, a firm insured by an insolvent insurer will have to obtain new cover part way through the policy period, at its own expense. In other words, the firm will have to pay its premium a second time. And if an insurer did become insolvent, that would probably trigger a dramatic hardening of the market, so the cover would be expensive if it were available at all.

Single renewal date

All firms are required to renew their compulsory cover on 1 October each year. The Law Society has launched an online survey www.lawsociety.org.uk/survey.law?poll=representation!pii_renewal and published advice from actuaries on this from actuaries Lane Clarke Peacock www.lawsociety.org.uk/new/documents/2009/pii_insurance_laneclarkepeacock.pdf and brokers Marsh www.lawsociety.org.uk/new/documents/2009/pii_insurance_marsh.pdf.

We believe the discussion to date has focused too heavily on price. Most significantly, and the survey and all discussion overlooks this, is the risk of an insurer becoming insolvent in the run up to renewal. This must be more than a hypothetical risk (evidenced by the fact that the Law Society has prepared a draft Practice Note to deal with the possibility of insurer insolvency).

There is also more than adequate evidence of the risk at this time of year from the events after September 11 (which was before the renewal date was moved from 1 September to 1 October), the collapse of Independent, and concerns at the time of last year's renewal. This could exacerbate the problem for, say, 10% of the profession because by then no market would exist among other insurers focused on the single renewal date. It is a risk management issue for the Law Society, the SRA and the profession. The problem would be severe at any time of year, but we believe it would be far more acute in the run up to the single renewal date.

The SRA: inspections of City firms

It has been suggested that Practice Standards will not inspect large City firms for the time being. This suggestion follows a comment by a senior representative of the SRA following publication of the Smedley report in March 2009, that the old style of visit would not continue for City firms. He has subsequently confirmed to us that the emphasis is on the words 'old style'. What will change in the short term is the frequency and tailoring of the visits.

It has also been suggested that the SRA's resources are exhausted by the dramatic increase in interventions, leaving it without the manpower to visit City firms.

We are aware that the Practice Standards team is in fact continuing to make inspections of City firms. The only change is that the SRA communicates the reasons for investigations in accordance with its 'Transparency, Protecting the Public, and Reasons for Investigations' policy www.sra.org.uk/solicitors/enforcement/we-are-investigating-you/transparency-public-protection-and-reasons-for-investigations.page

We have helped a wide cross-section of firms prepare for inspections, from major city practices to small firms. Contact frank.maher@legalrisk.co.uk

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Anti-money laundering: examples from life

Fee-earners might be forgiven for believing 'it could never happen to me'. Some real-life examples we have come across may help to cure them:

- The solicitor was instructed on the purchase of a flat for £2,450,000 in Canary Wharf. The client was a hedge fund manager. He asked for the client's original passport or a certified copy. The client faxed an uncertified photocopy. The solicitor also asked for £200 to cover a search fee. The client sent £5,000. The transaction was then aborted.

Four years later, the solicitor read an article in the newspaper, reporting the client's conviction for a string of frauds to the tune of £15 million. He had changed his name prior to instructing the solicitor, following earlier fraud convictions in Switzerland. The solicitor was still holding the £4,800. On the file checklist, there was a tick against 'ID information'.

- The solicitor was instructed on the purchase of a flat for £200,000 in South West London. The flat was for a South African, but the purchaser was a company registered in the British Virgin Islands. The only information provided for the company, was that its director was a second BVI company, a trust company. The managing director of the second BVI company, the trust company, was a professional trustee based in Geneva. The funds came from a Swiss bank account.

The source of the funds was therefore totally unfathomable. The solicitor went ahead with the transaction, because he had dealt with the professional trustee several times over the previous five years, and had a copy of his passport.

- It is also instructive to read **SOCA v Matthews and others** [2009] EWHC 1544, for an illustration of circumstances where the proceeds of drug-dealing were laundered by investment in the purchase of building plots. The fact that proceedings were necessary demonstrated that the money was washed fairly thoroughly.

Mr Matthews was not a drug-dealer, but he knew someone who was – the aptly-named Mr Crook. Mr Crook put money in Mr Matthews' bank account, and Mr Matthews used it to buy a plot of land. Mr Matthews also obtained a mortgage: Mr Crook very generously completed the application form on his behalf. Using the proceeds of drug-dealing, the gang built a house on the plot, and sold it for a profit. The investment was rolled over: the proceeds were used to buy a further plot and a house, again with the help of mortgages. The second plot was being built on, when Mr Crook was arrested.

Link for Lawtel subscribers www.lawtel.com/content/display.asp?ID=AC9501676&HL=Y&BK=Y&ResultID=27805175

Finally on this topic, even money launderers are suffering in the recession. We came across an example of a serial mortgage fraudster seeking to expand his estate with yet another mortgage fraud-fuelled purchase, only to find he had bought off an identity fraudster who did not own the property he was selling!

We advise many leading law firms and smaller practices on money laundering problems, such as production orders, as well as helping devise and implement policies and procedures, audit and training. Contact sue.mawdsley@legalrisk.co.uk

Departing staff - tenders and other risks

Although an architect's claim, the next case is relevant to lawyers too in the current economic environment. In **Fitzroy Robinson Ltd v Mentmore Towers Ltd** [2009] EWHC 1552 (TCC) www.bailii.org/ew/cases/EWHC/TCC/2009/1552.html, a firm was found liable for fraudulent misrepresentation by failing to inform its proposed client that the nominated project leader for the contract had resigned. The court found that the firm knew of the importance of the project leader's involvement to the client and that had the client known this it might have considered other firms.

Staff leaving, by redundancy or otherwise, may give rise to other issues. Low morale in a firm often appears to filter through into a significant deterioration claims experience. It may affect those who remain as well as those who are leaving. Personal pressures may also result in a deterioration of standards. Will you be able to secure their co-operation in dealing with claims or complaints arising from their work? Will you be able to contact them if they have decided to take time out in the Australian outback?

Stanley v Capital Law LLP [2009] UKEAT/0417/08 www.bailii.org/uk/cases/UKEAT/2009/0417_08_0304.html, an Employment Appeal Tribunal case, involved a claim by a law firm against a negligent ex-employee. An employment solicitor had been dismissed and negotiated a compromise agreement. The firm then discovered he had missed a time limit in a client matter, failed to report circumstances to the firm, and the firm claimed against him for misrepresentation in the compromise agreement.

Tenders and confidential information

We have already dealt with one risk issue relating to tenders, which involved departing staff. A reminder of another risk is in **Baker Tilly v Makar** [2009] EWHC 1715 (QB), that firms tendering for work but who are unsuccessful may receive confidential information which creates a conflict issue in relation to another client, although in this case the judge found that the firm had no confidential information. www.lawtel.com/content/display.asp?Context=585c1f24488e4f8f90f321615f604820&ID=AC0121592 (Lawtel subscribers only)

Continued ...

Engagement letters and non-engagement letters

Firms are rightly increasing their focus on the requirement for client care letters and rule 2 of the Solicitors' Code of Conduct 2007 www.sra.org.uk/rule2, and we have assisted many firms with their rule 2 letters and terms, including limitation of liability.

Practice varies as to whether firms require clients to sign letters of engagement. Some say it is practically impossible, while others achieve 100 per cent compliance, even for volume high street work. Some firms' terms state that continuance of instructions is deemed to constitute acceptance. And some do neither. A reminder of the desirability of requiring clients to sign letters of engagement is in the case of **Baker Tilly v Makar** [2009] EWHC 1715 (QB) mentioned above. Baker Tilly were successful in their claim for recovery of fees for expert witness work, but it is worth noting that the judge found they had proceeded on terms dictated by their instructing solicitors, rather than their own terms which were sent out later but were signed by neither the instructing solicitors nor the client. www.lawtel.com/content/display.asp?Context=585c1f24488e4f8f90f321615f604820&ID=AC0121592 (Lawtel subscribers only).

Practitioners should also not overlook the desirability of non-engagement letters where the firm declines to act. Although not a recent case, it is worth noting by way of example the US case of **Togstad v Veseley, Otto, Miller & Keef**, 291 N.W.2d 686 (Minn. 1980), where the Plaintiff consulted with the lawyer for an hour over a medical malpractice case. The lawyer decided not to take on the case. The lawyer did not mention the imminent expiry of the limitation period, and the non-client missed it. The non-client successfully sued the lawyer, and the Minnesota Supreme Court upheld the decision. It is sensible in these circumstances to send a 'non-engagement' letter after any consultation with a non-client which involves (or risks being construed as involving) the giving of any sort of opinion whatsoever.

A successful challenge to the pre-pack sale of a law firm LLP in administration was the subject of a decision in **Clydesdale Financial Services Ltd & ORS v Smailes** [2009] EWHC 1745 (Ch). An order had been made for inspection of files by third party funders, which 'proved ineffective because it appears that clients were not required by the firm or LLP to sign client care letters evidencing their consent to inspection of their files by funders.' However, the Law Society (pre-SRA) has reserved its position as to appropriateness of obtaining general consent to such disclosure in terms of business. See **Mendelson** (Solicitors Disciplinary Tribunal, 9212-2005). It is an issue which we have also found when reviewing firms' referral arrangements.

A representative of one provider of After the Event insurance, Focus, 'produced consents obtained from three clients on which he relied for an order for inspection of their files. He also relied on the witness statement of ... the compliance officer at the firm until the 8th April 2008, who gave evidence that clients of the firm signed a proposal form for ATE insurance with unnamed insurers in terms which contained a consent to inspection of their files by the insurer. He further referred to the terms of the ATE policies issued by Focus which contain a right for Focus to inspect the files... One or more of the three clients have subsequently withdrawn their consent. I would not be prepared to make an order for inspection on the basis of these recent consents unless given following legal advice.'

Link for Lawtel subscribers - <http://www.lawtel.com/content/display.asp?ID=AC9200875&HL=Y&BK=Y&ResultID=27808525>.

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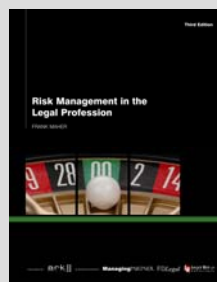
Prohibition on ATE commissions

The **Clydesdale** decision above is also a timely reminder about the prohibition on receiving commissions for ATE policies which we believe is overlooked by many personal injury firms, and may render policies unenforceable as well as resulting in the commission of a criminal offence. (See paragraphs 43-45 of the judgment.) The £20 de minimis provision in rule 2.06 of the Solicitors' Code of Conduct 2007 does not apply.

Swine flu pandemic

Others specialising in business continuity are better qualified to comment on preparation for this. However the risk of staff being off at short notice in large numbers emphasises the need to address delegated access to emails, central diary systems (particularly for key dates), and any increased borrowing requirements to allow for clients being too ill to instruct the firm and staff being unfit to do the work.

Risk Management in Law Firms (Third edition)



This comprehensive guide by Frank Maher, extensively revised and substantially revised to address credit crunch issues, has already sold worldwide in places as far afield as Austria, Bermuda, Finland, New Zealand, and United Arab Emirates to name but a few. It is a practical guide to implementing risk management processes in

law firms, covering a host of topics such as people, clients, finance, protecting partner assets, file audit and insurance. Further details from info@legalrisk.co.uk

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