

# Risk Update



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Willis Tower, Chicago

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## News from the USA

What happens in the US first often follows in the UK legal market. It can also inform our thinking, in areas such as conflicts, albeit the rules differ materially. In addition, with an increasing number of US firms and insurers as clients, we take a particular interest in developments on the US scene.

Legal Risk LLP partners attended a packed conference in Chicago in March, on law firm liability and risk management. It was noted that the expected credit-crunch claims had largely yet to materialise, much as in the UK, and there has been no discernible rise in the frequency of claims. It was thought this may be in part because potential claimants do not wish to spend the money on legal fees in pursuing claims. We suspect that in the UK the reason may be that the stagnant property market has meant banks cannot sell property and have therefore yet to crystallise their losses; while they could nonetheless pursue claims now, in practice this is unlikely.

There was also the suggestion that current insurance rates are not sustainable and will have to increase. Coverage disputes are far more common in the US, though we detect an increasing number in the UK.

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## Quinn Insurance Limited

On 30 March 2010, following an application by the Irish Financial Regulator, the High Court of Ireland has appointed joint provisional administrators to Quinn Insurance Limited.

The Financial Regulator states that the appointment of joint provisional administrators will allow the firm to remain open for business in the UK, to continue to be run as a going concern under different management and to put the business on a sound commercial and financial footing. The Irish Times reports that the company has an excess of liabilities over assets of €200 million.

According to the Financial Regulator's statement:

"In addition, the Financial Regulator has separately directed Quinn Insurance Limited to cease writing new business in the UK. Existing UK policyholders will not be affected by this decision as existing policies will remain valid. Customers can make claims in the normal way.

The effect of this action is to prevent Quinn Insurance Limited suffering further financial losses on its currently unprofitable UK business."

Quinn Insurance Limited is the company in the Quinn group which is a 'qualifying insurer' for the purposes of the Solicitors' Indemnity Insurance Rules 2009. Quinn underwrote almost 10% of the solicitors' primary market in England and Wales in 2009.

Without suggesting that Quinn is insolvent, in our July 2009 newsletter we outlined the consequences of an insurer becoming insolvent. See [www.legalrisk.co.uk/FileUploads/2009729\\_NewsletterJul09\\_2.pdf](http://www.legalrisk.co.uk/FileUploads/2009729_NewsletterJul09_2.pdf)

## Events: Practice Standards Unit Visits

Legal Risk LLP partners will be speaking at a series of events organised by Aon in conjunction with local law societies. The events carry 3 hours CPD points and are at a variety of locations around the country between 11 May and 8 July 2010. There is no charge for the majority of these (except Newcastle – nominal fee of £25).

To register please go to [www.aon.co.uk/psuseminars](http://www.aon.co.uk/psuseminars)

We have helped a wide variety of firms, including major city and national practices, prepare for regulatory inspections by the Practice Standards Unit of the Solicitors Regulation Authority (SRA).

For assistance in preparing for PSU inspections, contact [info@legalrisk.co.uk](mailto:info@legalrisk.co.uk)

*News from the USA (continued)...*

Hot topics were claims arising from estates and from patent work. Patent related claims particularly involved errors in applications. 26 per cent involved time limits. Other examples included failure to pay fees to maintain a patent, and omission of source code from an application.



On conflicts, ABA Model 1.10 has been revised to permit the use of information barriers to screen lateral hire lawyers – previously this was only permitted in the case of those who came from government. Advance conflicts waivers were discussed, and doubts were expressed about their efficacy, though they may still be useful to open the door to further discussion when issues arise.

Liability to third party beneficiaries is a developing area, which may surprise lawyers in England and Wales where, in broad terms, such liability has long been established.

Communications with in-house counsel may create a conflict, resulting in there being no privilege; instructing an external law firm may be a way round this (a point welcomed by Legal Risk LLP partners!)

Schemes by which fraudsters purport to be potential clients contacting law firms by email and ending with a request for the lawyer to cash cheques have been an increasing problem. Commonly, this is for a purported debt recovery on behalf of an overseas 'client'. This is something we have not seen in the UK, despite the variety of other scams.

Large law firm closures, significant lateral movement and unprecedented redundancies have been a feature of the US market over the past year. There is however still an increase in law firm mergers and acquisitions. There are particular insurance coverage issues when recruiting lateral hire partners from firms which may collapse; we have advised a significant number of UK firms in relation to the implications of lateral hires from collapsed US firms. Lateral hire partners may be exposed to litigation from many sources, which may be a distraction from doing the work of their new firm.

Closure of law firms causes real problems over the cost of file storage, particularly on insolvency – no less a problem this side of the Atlantic.

Outsourcing is also a significant issue in the US, where firms (or perhaps their clients) are probably some way ahead of the UK. This is expected to provide new challenges for professional liability. Particular issues arise where clients instruct more than one firm to deal with separate aspects of the same matter, and this is especially significant where there is litigation and e-discovery (disclosure) is outsourced to save cost, potentially exposing the firm on the court record to breaches of its duties to the court.

Attorney-client privilege was considered in the context of changes in clients' corporate structures and ownership through asset sale, merger or takeover, following some recent decisions. It was recommended that the issue be addressed in the deal documents.

Suing for fees which in turn provokes a counterclaim for professional liability is as much a problem in the US as in the UK. Interestingly, one large international firm requires the practice area to instruct an outside law firm to act for it on fee recovery claims, paid for out of its own budget.

Most state bars accept that it is ethical for law firms' terms of business to provide at the outset that all disputes will be decided by arbitration. Despite arbitration meaning there would be no jury trial, opinion was divided on the benefit overall.

Is the billable hour dead? Not yet, it seems, but it will not be the default mode going forwards. Discussion focused on outcomes and what constitutes delivering value – which might, for example, be settling a dispute by Friday, or preventing the CEO having to give evidence. It was noted however that clients often fail to reward firms proposing value-based arrangements, perhaps not trusting the alternative to be good for them. Alternatives considered included the expected - volume and discounted fees, blended hourly rates, contingency fees, fixed fees, capped fees, success or incentive fees – and, less predictably, reverse contingencies (paying the firm a percentage of avoided loss) and retrospective assessment based on value, the last of these being heavily reliant on mutual trust.

Our clients include numerous US and overseas firms, either for compliance, professional indemnity and risk management in their UK offices, or risk management in their overseas offices. For services to US and overseas law firms contact [frank.maher@legalrisk.co.uk](mailto:frank.maher@legalrisk.co.uk)

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## Council swaps

A note of caution for those who advise on public sector contracts. In our May 2008 Risk Update, we issued a reminder that the doctrine of ultra vires is alive and well, even if emasculated in relation to companies, following the decision in **Risk Management Partners Ltd v London Borough of Brent** [2008] EWHC 692 (Admin). An appeal was dismissed - [2009] EWCA Civ 490.

Many readers will recall from the 1990s the problems of complex financial instruments in local authority finance, found to be ultra vires the authorities – see in particular, **R v Hammersmith & Fulham London Borough Council** [1992] 2 AC 1. These continue to cause problems, with a recent £28 million judgment against a leading Scandinavian law firm – see **Haugesund Kommune v Depfa Acs Bank and Another** [2010] EWHC 227 (Comm) [www.bailii.org/ew/cases/EWHC/Comm/2010/227.html](http://www.bailii.org/ew/cases/EWHC/Comm/2010/227.html).

Further problems have arisen, as appears from news reports that four banks have been charged with fraud in relation to derivatives covering €1.7 billion of borrowings for Milan.

## Legal Services Act

The Legal Services Board has announced that the provisions enabling Alternative Business Structures, which will permit outside ownership of, and investment in, law firms will come into force on 6 October 2011 - [www.legalservicesboard.org.uk](http://www.legalservicesboard.org.uk)

We will report further in future editions.

For advice on compliance and regulatory issues, contact [francis.dingwall@legalrisk.co.uk](mailto:francis.dingwall@legalrisk.co.uk)

## New Code of Conduct - Outcomes focused regulation

In the last issue of Risk Update we mentioned that The Solicitors Regulation Authority had announced a consultation on Outcomes Focused Regulation (OFR), which will be a risk-based regulatory regime based on core principles and the high-level outcomes firms must achieve. The SRA have now announced their programme *Freedom in Practice: Better Outcomes for Consumers*, which will be centred on a series of consultations. The first, to take place in late April, will look at the broad context of OFR and regulatory practice. The second will be on the new draft regulatory handbook, including licensing rules for ABSs and the new Code of Conduct. This document will be published on 28 May 2010.

## Conflict rule changes – or not

The SRA is not pursuing the proposed changes to rule 3 which were the subject of its recent consultation, for the moment at least. This appears to be a by-product of the wide-ranging review of the rules now underway. The SRA had previously decided in principle to amend rules 3 (conflicts) and 4 (confidentiality) to allow waivers for 'sophisticated clients', as reported in the January 2010 edition of this newsletter. The changes to rule 4 await approval.

For advice on conflict issues, contact [francis.dingwall@legalrisk.co.uk](mailto:francis.dingwall@legalrisk.co.uk)

## Anti-Money Laundering

The Court of Appeal decision in **Shah v HSBC Private Bank (UK) Limited** [2010] EWCA Civ 31 [www.bailii.org/ew/cases/EWCA/Civ/2010/31.html](http://www.bailii.org/ew/cases/EWCA/Civ/2010/31.html) raised the spectre of negligence claims against solicitors and other professionals who report money laundering suspicions. The case will now go for trial. The decision demonstrates the need for solicitors to keep records of their thinking when considering suspicion – but they need to do this for their own protection in any event, as otherwise it is easy to assume that subsequently discovered facts were known to them at the time. More concerning however is the prospect of one's decision making process and internal private discussions being picked over in court. Taking independent advice may assist in mitigating the risks.

Bribery investigations and prosecutions have been in the press a number of times. The Bribery Bill was referred by the House of Commons to a Public Bill Committee on 16, 18 and 23 March 2010. It has some prospect of becoming law before the General Election. See [services.parliament.uk/bills/2009-10/bribery.html](http://services.parliament.uk/bills/2009-10/bribery.html) to monitor progress. For the most recent draft see [www.publications.parliament.uk/pa/cm200910/cmbills/095/10095.i-ii.html](http://www.publications.parliament.uk/pa/cm200910/cmbills/095/10095.i-ii.html). If passed, firms will need to implement procedures to prevent bribery. They should be particularly alert to risk in public sector work and construction in our view.

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### *Anti-money laundering (continued)...*

Insider dealing investigations and prosecutions by the Financial Services Authority are also featuring highly in the press and could also give rise to significant anti-money laundering issues.

Legal Risk partner Sue Mawdsley will be presenting several anti-money laundering seminars for the Law Society. Details, along with other events at which Legal Risk LLP partners are speaking in the UK and overseas, can be found on the Events page of our website, [www.legalrisk.co.uk/Pages/EventCalendar.aspx?id=249](http://www.legalrisk.co.uk/Pages/EventCalendar.aspx?id=249)

For advice on anti-money laundering, including reporting issues, production orders, systems and training contact [sue.mawdsley@legalrisk.co.uk](mailto:sue.mawdsley@legalrisk.co.uk)

## Sale and leaseback

Our May 2008 Risk Update warned (under the heading Equity release – or not) of the dangers of sale and leaseback schemes under which homeowners, usually in debt, sell their homes. The Solicitors' Financial Services (Scope) Rules 2001 were amended with effect from 20 January 2010 so as to restrict solicitors' activities in relation to advising on and administering these products in a number of ways, where they rely on regulation by the Law Society/SRA as an Exempt Professional Body.

For advice on equity release and other compliance issues contact [frank.maher@legalrisk.co.uk](mailto:frank.maher@legalrisk.co.uk)

## Limiting liability

Legal Risk LLP's Top 100 Surveys on Law Firm Professional Indemnity and Risk Management have shown that limiting liability is now commonplace. Our 2010 survey is in course of preparation and will be published shortly. We have advised on the terms of ten of the top 100 UK firms, including large city firms, and some overseas and offshore practices.

Elsewhere around the world, while the USA remains resistant to allowing liability caps, Irish law firms may limit liability to €1.5 million, and rules have been passed in Australia permitting liability caps - \$1.5 million in Queensland and \$2 million in Victoria.

However limitation of liability is not just about capping. Other issues include time limits, sharing liability with other defendants, and excluding liability of individuals.

For advice on limitation of liability contact [frank.maher@legalrisk.co.uk](mailto:frank.maher@legalrisk.co.uk)

## Assigned Risks Pool consultation

Our November 2009 Risk Update mentioned the SRA's consultation on the future of the Assigned Risks Pool (ARP) – particularly pertinent for two reasons. First, the Irish Law Society scrapped its ARP the following month under pressure from insurers. Secondly, claims against the (English) ARP are reported to amount to £33 million, though many suspect the true exposure is higher, and the premiums are only £5.5 million, with £3.5 million unpaid.

The consultation has concluded, and the SRA has resolved to maintain the ARP but with a maximum period of 12 months cover, rather than 24 months as at present, and a bar on new firms joining.

## Successor practice consultation

The SRA's consultation on this has resulted in a decision to allow firms which are closing to elect to pay for run-off insurance, as an alternative to there being a successor in the manner currently prescribed. For advice on structuring or avoiding successor practice cover, and in relation to claims problems, contact [frank.maher@legalrisk.co.uk](mailto:frank.maher@legalrisk.co.uk)

### *And finally...*

Whilst it has never been a risk management strategy, immunity for lawyers against suit has been an important defence in a small number of claims over the years, albeit more for the bar than solicitors in the UK. Its erosion in the UK by the decision in **Arthur J S Hall v Simons [2002] 1 AC 615 HL** has now been followed in Malaysia, in the case of **Sri Alam Sdn Bhd v Tetuan Radzuan Ibrahim & Co [2010] 1 MLJ 284**.

(With acknowledgements to Ramrais & Partners for drawing this to our attention.)

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