Brexit: a risky business?

What does Brexit mean for law firm risk, asks Frank Maher

Already there are press reports that some leading law firms are battening down the hatches in anticipation of either a full recession, or at least a downturn in activity in particular sectors such as real estate, following the UK's referendum decision on 23 June 2016 to leave the European Union.

The risks to business and the wider economy have been widely explored in the press, and law firms can expect, to some extent, to follow the fortunes of their clients, but what are the professional liability risks which law firms may face? As we enter uncharted waters, this article attempts to explore some preliminary thoughts on where those risks may lie.

Cream of the crop

Many of the lawyers advising on Brexit issues will be among the cream of the profession and will doubtless have a thorough grounding in the area of law in which they practise. Errors of law were an infrequent source of claims in the past, but this is an area where insurers have seen change, particularly in highly technical areas of law such as pensions. That said, the writer's instinct is that errors of law will not feature highly in the Brexit-related claims statistics of the future.

More likely in the writer's view are the following scenarios. A depressed economy can normally be expected to fuel professional liability claims, based on past experience from the 90s, which impacted heavily on the Solicitors Indemnity Fund, and the post-Lehman period when insurers' loss ratios were impacted heavily, particularly in 2009.

Ratings

Ratings downgrades may give rise to unforeseen margin calls spreading pressure more widely. Valuation evidence may be affected by the passage of time, whether actuarial advice on a pension fund in an M&A context, property valuation or accountancy advice, and lawyers will not only need to be alert to the need for it to be updated but will also need to consider the exclusion from their retainers of advice on commercial aspects of transactions.

There is much speculation that there will be heavy demand for advice on Brexit issues, and this may lead to law firm resources being stretched. It is always easy for clients to say with hindsight that if something had been done slightly quicker, this would have enabled them to exploit some opportunity, or have avoided some loss. The writer has seen a claim arising from a fall in exchange rates over a few days where it was alleged that the law firm had adopted the wrong currency for receipt of money.

In the context of Brexit claims, delay may cause loss in several ways. There may be funding opportunities which are missed, and exchange rate differences give clients a fertile opportunity for one-way bets – if the pound goes up during a period of delay, they lose nothing, but if it goes down, they have a claim. Depending on the detail of future negotiated arrangements, there may also be missed opportunities for visas and residency rights.

Should clients be establishing European entities, whether a societas Europaea or locally incorporated company, and European operations as part of their planning? They may take time to establish and seek necessary authorisations and recruit staff to be operational in time. Delay may impact on the clients' business.

While intellectual property rights may not be greatly impacted by Brexit, the loss of protection of the EU trademark could give rise to client losses and claims – perhaps more through lawyers' failure adequately to define their retainer, or to ensure that they have effectively concluded an earlier retainer.

Jurisdiction

Choice of law and choice of jurisdiction in contracts could give rise to issues, as Rome I and Rome II would no longer apply to the UK, and this may be relevant to existing and future pre-Brexit contracts.

Depending on the result of the Brexit negotiations, withholding taxes may become more of an issue and there is a possibility of client losses, if only the inconvenience of having to seek tax refunds in another country, if contracts do not anticipate the risk of this in the meantime.

Assuming VAT continues to apply in the UK, or something very similar to it, it will remain to be seen how it operates between the UK and EU. There may be unforeseen consequences which in turn may be laid at the door of law firms if they have not excluded tax from their retainers.

While it is unlikely that there will be any radical difference between the UK and the EU in data protection laws post-Brexit, thought will have to be given to data transfer issues, whether by relying on model clauses or binding corporate rules, with interruption to business and possible sanctions in the meantime if the need is not anticipated and adequately addressed.

Biggest risk

Perhaps the biggest risk is less overtly Brexit-related, and that is partners hungry for work seeking opportunities in new and emerging markets with higher risks which are not matched by the firm's experience. The recent case of *Agouman v Leigh Day* [2016] EWHC 1324 (QB), [2016] All ER (D) 172 (Jun) provides an illustration of the potential for such claims: the defendant firm allowed clients' damages to be paid in a single tranche into a bank account in the Ivory Coast, where, it is said, it was vulnerable to dishonest claims, including claims enforced by a corrupt judiciary in the Ivory Coast.

Too often, however, the writer's firm sees examples of law firms' client and matter opening procedures including some form of risk assessment which fails to lead on to appropriate measures being taken. This either happens because the partners or fee earners designate all matters as "medium risk", when some clearly are not, or because they rightly designate some matters as "high risk", but then fail to implement any further measures in consequence. Such measures might include further due diligence, ongoing monitoring, supervision and second opinions.

Overall, a flood of Brexit-related claims seems unlikely, but thought should be given to ensuring that clients know if past retainers are at an end, the careful definition of future retainers, detailed assessment of the risks of unfamiliar jurisdictions – and taking appropriate measures in the light of that risk assessment. NLJ

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