

Solicitors Regulation Authority

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Contact: Frank Maher

Our Ref: FRM PSYROC

Your Ref:

Date: 30 August 2022

Dear Sirs

**Next steps on the Solicitors Indemnity Fund (SIF) and consumer protection for negligence claims**

1. This is the response of Legal Risk LLP to the Discussion Paper dated 3 August 2022 (the Discussion Paper).

**Summary of response**

2. It is unlikely that a compensation fund would result in material cost savings.
3. A change to a compensation fund is in the interests of neither (a) consumers nor (b) solicitors and their staff.
4. Abolishing the entitlement of solicitors and their staff to indemnity would in our submission be unlawful, in breach of the SRA's statutory duties and regulatory objectives, and susceptible to judicial review.

**Our experience**

5. Members of the firm have experience of –
  - a) Defending several thousand professional liability claims insured through the Master Policy Scheme, SIF and open market insurers and/or advising on coverage for every year of compulsory insurance since the 1976 year,

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Legal Risk LLP is a limited liability partnership registered in England and Wales, number OC339694. A list of members' names is available for inspection at our registered office: 28 Bixteth Street, Liverpool L3 9UH. We use the word partner to refer to a member of Legal Risk LLP.  
Authorised and regulated by the Solicitors Regulation Authority under number 494979.

- b) Advising solicitors who have found themselves uninsured or potentially uninsured as a result of insurer insolvency, including an application for judicial review of the Financial Services Compensation Scheme,
  - c) Reviewing governance and providing expert evidence for litigation in relation to compulsory Law Society insurance schemes outside the UK,
  - d) Providing legal advice on insurance arrangements to firms and individual solicitors affected by firm closures,
  - e) Providing legal advice to a retired solicitor presently covered by SIF who would potentially be affected by any changes,
  - f) Establishing a law firm captive insurer and being a director of it,
  - g) Conducting litigation relating to insurance coverage disputes, and
  - h) Participating in discussions hosted by the SRA, the Law Society and others in relation to SIF.
6. As practising solicitors, two of our partners being past SIF contribution payers, and as consumers of legal services ourselves, we have a pecuniary interest.

#### **Outcomes of the consultation process to date**

7. *The Request by the Solicitors Regulation Authority (SRA) to the Legal Services Board (LSB) to issue an exemption direction under the Legal Services Act 2007 (LSA) dated 17 August 2022 (the LSB Request)* identified that the consultation process so far had resulted in feedback which included –
- a) Recognition that the potential impact on individual consumers could be significant,
  - b) Law firms' and solicitors' willingness to contribute to the funding of arrangements, and
  - c) The expectation that the cost passed on to consumers would be minimal.

#### **The cost of SIF**

8. The 2020 accounts show a residual surplus of £22.483m. While the solvency position in the LSB Request is noted, the SIF has not required additional funding from the profession in two decades, with the cost of claims for many years, it would appear, being covered by investment income.
9. Any perceived shortage of funds in SIF is attributable to the withdrawal by the Law Society in 2006 of £25m and, we believe, a similar sum the following year making a total of £50m; these sums were applied for a wholly extraneous purpose of paying the Law Society's own

staff, through its pension fund, instead of indemnifying solicitors and their staff against claims.

10. Contributions to SIF were paid by the profession under compulsion of law, enforceable in conduct under the Solicitors Indemnity Rules from year to year and as a debt, and were paid in the legitimate expectation that they would be applied for the purposes set out in those Rules in order to provide indemnity in future years, and that those contributing would not at some future time be put in the position where (a) they had no such protection (even though many had paid for it) and, or alternatively, (b) no such protection could be obtained in the insurance market.
11. While SIF's reserves may not suffice for the future, the likely annual cost of funding which would have to be met by the profession were SIF to continue appears to be low, in the order of £10-15 per practising solicitor, and may be rather less once account is taken of investment income.
12. If that were to change significantly, the situation could be reviewed in the future: it does not warrant a decision to terminate SIF now.

#### **Alternatives to SIF**

13. The Discussion Paper canvasses the alternatives of a new SRA consumer protection arrangement as an indemnity scheme or a compensation fund.
14. There seems little point in setting up a new indemnity scheme when SIF already exists. If there is scope for reducing cost, this can be achieved within the current structure by, for example, outsourcing claims handling or other aspects of management if found cost-effective to do so.
15. A compensation fund would represent a radical change. There are significant obstacles to such a change.
16. Claimants could not be compelled to abandon their entitlement to claim in the usual way. It is suggested that various categories of claimant with turnover, income or assets in excess of £2m might be excluded in any event; in very many cases the description of these as 'large corporate claimants' is a misnomer.
17. The Discussion Paper envisages that such a fund, protecting consumers but not solicitors and their staff, might have subrogated rights of recovery<sup>1</sup> against the latter, who would in any event be unprotected for the reasons identified in paragraph 16.

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<sup>1</sup> Similar to the provisions of rule 17 of the SRA Compensation Fund Rules 2021

## **Grounds for objection to a compensation fund**

### *A compensation fund may not result in significant cost savings*

18. The present SRA Compensation Fund (SCF) deals with liquidated claims for money which may be reduced by a cap and/or the exercise of discretion. In contrast, SIF operates on a basis of legal liability and it would be wrong in principle to dilute that.
19. Liability claims involve far more complex issues such as negligence and standard of care, whether a duty exists, the scope of duty, breach of trust, causation, quantum and, of particular significance in this context, limitation. The lapse of time since the accrual of causes of action in our experience makes it likely that there will be further complications – claimants under a disability through age or mental capacity, vulnerable claimants, loss of documents, more complex facts requiring investigation, and particularly difficult issues arising in long-running breach of trust cases. Files will inevitably have been destroyed with the passage of time in many cases.
20. There would therefore be many cases where it would be difficult for unrepresented claimants properly and fairly to pursue their claims. In those cases, in order to achieve fairness, it might be necessary for a compensation fund to pay claimants' costs whereas that is not currently the norm for the SCF.
21. We understand that a large proportion of claims against SIF are, unsurprisingly, statute barred, meaning that there are many claims where there is no payment in any event apart from defence costs. We also understand that a disproportionate number of claims are advanced by litigants in person and in these cases the majority of the cost of investigation falls to SIF. In these cases in particular, it is unlikely that there would be any significant saving if there were a compensation fund instead of SIF.
22. It is too simplistic to measure the success of a scheme by reference to the proportion of claims costs to total costs: that could in theory be addressed by simply paying all claims in full, but it would be inappropriate to do so for many reasons, and if a compensation fund were to pay claims in that way and seek recovery from retired solicitors and their staff, it could expect to face significant legal challenges adding further cost.

### *Breach of the SRA's statutory duties and regulatory objectives*

23. As SIF was funded by the profession under compulsion of law and for the purposes of providing indemnity as set out in paragraph 10, for the SRA to withdraw cover and apply the remaining sums in a manner which does not provide indemnity for solicitors and their staff (while also protecting consumers) would, in our submission, be irrational, *Wednesbury*<sup>2</sup>

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<sup>2</sup> *Associated Provincial Picture Houses Ltd v Wednesbury Corporation* [1947] EWCA Civ 1

unreasonable (being a decision which no reasonable person could have made), unlawful, and susceptible to judicial review.

24. Pursuit of subrogated rights vested in a compensation fund would in our submission also breach the SRA's obligations under section 28 of the LSA which requires that the SRA act in a manner which is 'transparent, accountable, proportionate...and targeted only at cases in which action is needed'.

25. The reasons are –

- a) Section 37 of the Solicitors Act 1974<sup>3</sup> provides, in summary, for the provision of *indemnity* for solicitors and their employees through an indemnity fund, authorised [participating] insurers or a master policy. It was for these purposes that the sums currently held by SIF and the £50m previously appropriated to the Law Society's Pension Fund were procured by exercise of statutory powers under section 37. A compensation fund under section 36 of the Act<sup>4</sup> as envisaged in the Discussion Paper would not provide indemnity. Contributions were paid under compulsion of law for the purpose of providing *indemnity*, not for a compensation fund which provided no benefit to those paying for it;
- b) Solicitors contributed to SIF in the reasonable expectation that the money they had contributed would be used to continue to provide cover, and the funds which are still adequate to cover many years' claims should not be taken for any other purpose but must be applied strictly in accordance with rule 21 of the SRA Indemnity Rules 2012, which requires that it no longer be 'necessary or appropriate' that SIF be maintained – but the current claims experience shows that it *is* still needed;
- c) The purpose for which SIF was established was not only to protect consumers but also solicitors and their staff;<sup>5</sup>
- d) Insurance is not generally available in the open market, as the SRA has had to concede;
- e) Even if insurance were generally available, solicitors should not have to pay a second time for what many have already paid, particularly having regard to the reason for any perceived shortfall identified in paragraph 9, namely the appropriation of a substantial portion of SIF's resources towards the Law Society's Pension Fund;

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<sup>3</sup> And, in relation to licensed bodies, paragraph 19 of Schedule 11 to the Legal Services Act 2007

<sup>4</sup> And other statutory powers as set out in the Supplemental Notes to the SRA Compensation Fund Rules 2021

<sup>5</sup> *Swain v The Law Society* [1983] 1 A.C. 598, per Lord Brightman at page 618 B-C

- f) Solicitors are exposed to liabilities which are a direct consequence of the SRA's regulatory arrangements, restricting their ability to limit liability contractually<sup>6</sup> even where their insurance may be inadequate (either because the £1m SIF limit is substantially lower than the £2/3m limit under the Minimum Terms and Conditions applying at the time of the engagement, or capped through the aggregation clause);
  - g) A subrogated claim against a solicitor or staff member in these circumstances is conceptually far removed from the existing SCF recovering money from someone who has stolen or failed to account for client money;
  - h) As any material costs saving is unlikely for the reasons identified above, change would be neither proportionate nor targeted;
  - i) Further, when the evidence so far available indicates that the profession is willing to pay for SIF in its present form, even though the estimates may have been overstated by omission of investment income, to replace it with something providing less protection would be perverse;
  - j) Removal of the remaining indemnity provided by SIF, after the previous appropriation of £50m for extraneous purposes, would undermine the trust of the profession, who funded it, in the regulatory regime.
26. Change should not in any event be implemented without a thorough understanding of the claims on SIF. The analysis in the Willis report is purely numeric, and does not identify types of claimants (for example, lenders, large corporates, small companies, wealthy individuals, under-compensated and disadvantaged brain damaged children), causes of claims, reasons for the lapse of time since the alleged act, the period of time from discovery of circumstances to the claim, and the period of time from practice closure to the claim. The complicating factors identified in paragraphs 19 and 20 above also need to be considered. Such analysis is a necessary precondition to change, if change is lawful at all.
27. Three questions should be asked before implementing change –
- a) Is it in the interests of consumers?
  - b) Is it in the interests of solicitors and their staff?
  - c) Is it lawful?
28. In the case of a compensation fund, the answer to each is a resounding 'No'.

## Conclusion

29. Our response is summarised in paragraphs 2 to 4.

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<sup>6</sup> Rule 3.2, SRA Indemnity Insurance Rules 2019

Yours faithfully

A handwritten signature in black ink, appearing to read 'Frank Maher', is written above a horizontal line that starts under the signature and extends to the left.

**FRANK MAHER**  
Partner  
For Legal Risk LLP