SRA BOARD
14 July 2020

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Summary of other issues and recommendations

New proposals in 2020 Consultation Fund reform consultation

Applying a cap to multiple applications

What was the consultation proposal?

1 We consulted on a proposal to introduce a new mechanism to cap payments from the Fund. The cap would apply to payments:

- arising from a single or connected event, and
- which are likely to exceed a specified financial threshold.

2 In applying the cap, we said that we would:

- fix the total level of the cap for each single of connected event at £5m
- decide on a case by case basis, depending on the circumstances, how we apportion the £5m across the multiple applications.

Rationale

3 We wanted to introduce a mechanism that would allow us to manage the potential liability to the Fund presented by high value connected applications such as those related to property and other investment schemes. This in turn would make it easier for us to be consistent in the level of contributions levied each year, providing greater certainty and ability to manage outgoings by those we regulate. We said that the proposed approach would still allow all eligible applicants to receive a reasonable level of redress, that compares favourably to other schemes with capping mechanisms.

4 In arriving at the consultation proposal, the Board considered a more flexible approach, with greater discretion to set the level of cap on a case by case basis. The Board decided that we should consult on a fixed cap to apply to all relevant groups of claims because this would provide transparency and certainty for the public, the profession and the Fund. Several other compensation schemes that have caps set them at a fixed level. We stated in the consultation that we may periodically review the £5m figure based on the changing profile of claims.

5 The £5m threshold was set as a proportionate sum, given the profile of very high value multiple claims that the Fund is currently receiving.

Responses to consultation

6 There was a mixed response about this proposal. The majority agreed that in principle a capping mechanism could be beneficial and necessary. However, several of these respondents also raised concerns around fixing a total amount for any scheme at £5m

to be apportioned between eligible claimants. This was in terms of whether £5m is the right amount, with some highlighting that we had provided limited data to support this figure. Some respondents argued that it would be fairer to adopt a more flexible approach, deciding the limit on a case by case basis. Considerations might include, the level of reserves in the Fund at the time, the impact of the loss, the culpability of the applicant and even the wider economic climate. Some respondents argued that this would maximise the chances that applicants would receive fuller redress and would provide flexibility to address any unintended consequences or unusual situations.

7 Those that disagreed with the proposal in principle were concerned that some consumers would see reductions in redress compared to what they would have been received had there been no connection to other claims, and this may appear unfair. The Legal Services Consumer Panel thought that the application of the cap in some conveyancing and personal injury matters could have unintended consequences. They said that unlike investment schemes the impact of not receiving a full grant available for a single claim might mean that they are made homeless or, in personal injury cases, applicants might not be able to afford personal care for their lifetime.

8 The Law Society suggested that if we introduced a fixed cap: "…*the cap should not apply to all claims relating to the same or connected underlying circumstances, but it should instead apply to all the clients of a particular firm with claims relating to the same or connected underlying circumstances*…". Their rationale was that if we also required the solicitor to inform the potential client approaching them that they might be subject to a multiple application cap for the relevant work that the firm was going to do, they might approach a different solicitor. In turn, this would make it more likely that the dubious nature of the scheme might be exposed if the original solicitor had not realised that it was dubious

Further information

9 We arrived at the £5m as a proportionate threshold by reference to the expected payment for high value schemes we are aware of that are giving, or may give rise, to claims on the Fund and the need to balance contribution levels from the profession. The precise details of claims and potential claims are confidential but had been viewed by the Board in deciding to consult on this figure for the cap.

10 We have reviewed the latest forecasts post consultation. We now think it less likely that the Fund will pay very large sums on one scheme because another regulator's scheme has started to provide redress. However, there are potential liabilities in relation to new schemes where we might expect high value applications to be made. We estimate that the schemes where we are already making payments or where we assess that we are likely to make payments in the future we will see total claim values ranging from £1m to £10m with an average of £5m.

Our view

11 There was majority support in principle for a cap where there are high value connected claims for the reasons set out in the consultation. We remain of the view that setting a

fixed level cap is the fairest and most transparent option. This provides the most certainty for clients, the profession and the Fund. This will in turn provide greater flexibility for us to adopt a less conservative reserves approach to cover potential liability, with the associated contribution costs to the profession, which may ultimately be passed to consumers. A more flexible, discretionary limit would not provide certainty and would mean that any decision to limit payments that go below full recompense for an individual may result in challenge.

12 We also think that maintaining the £5m figure is right and is based on what we currently know about high value claims and the potential impact on contributions. We will review this figure periodically in light of claims data and other information.

13 We remain of the view that the cap should apply to payments arising from a single or connected event and not to individual firms, of which there may be several involved in an event.

14 We are also undertaking work to help us better understand the consumers view of the role of solicitors in of high risk investment schemes. This will inform communications to consumers around the risks. We will also do further work to explore ahead of implementation how to best explain to consumers how they are protected by the Fund including the circumstances that may result in the multiple application cap being applied.

Recommendation: to cap multiple claims arising out of a single or connected events above a £5m threshold and note that we will:

- **fix the total level of the cap for each single of connected event at £5m**
- **decide on a case by case basis, depending on the circumstances how we apportion the £5m across the multiple applications.**

Remove any financial or hardship tests and use our residual discretion

What was the consultation proposal?

15 Having regard to the responses received to our first consultation we proposed to remove the "hardship" criteria that currently exists for otherwise eligible applicants. And that we would instead use our residual discretion to refuse or reduce a payment where the impact of loss is disproportionately low, and it would not be appropriate to meet it from a finite fund.

Rationale

16 We explained that we do not have a set threshold for what "hardship" means in practice and that we do not operate any type of "means tested" assessment usually associated with hardship tests. Instead we proposed that we will use our residual discretion to allow us to consider those rare cases in which the impact of loss is disproportionately low, and it would not be appropriate to meet it from a finite fund.

17 We explained that this residual discretion might be used to refuse or reduce a grant where the applicant has already received a appropriate level of compensation from another scheme or from an insurer who has not paid in full. Or for any other reason that would mean that the loss is immaterial when viewed in context of the applicant's wealth or circumstances.

Responses to the consultation

18 There was unanimous support for the removal of hardship tests. The common theme from responses was that any loss of money would have an impact on eligible applicants and that the requirement to demonstrate hardship was unnecessary.

19 The majority of responses agreed with the proposal that we use our residual discretion and that the approach aligned with the statutory purpose of the Fund. The Law Society thought this was not unreasonable especially if guidance as to the factors that might lead to such a decision and explaining in practice how the discretion is likely to be exercised was to be issued.

Our view

20 We are pleased that there was overall support for these proposals. We will continue to work on our draft guidance on factors that might lead to us exercising our residual discretion.

Recommendation: to remove any financial or hardship tests for eligible applicants beyond a discretion to refuse or reduce payments when we consider the loss to be immaterial or substantively compensated elsewhere

Applying the single claims limit

What was the consultation proposal?

21 We consulted on a proposal to apply the single claim limit to each individual applicant receiving payment. Each individual applicant will receive a maximum of £500,000 for the loss arising from a single event or set of circumstances. This would mean for example, where a separating couple that has jointly instructed a solicitor to sell the family home that is worth significantly more than £500,000 and the sale proceeds are stolen, each person could make a claim for up to £500,000.

Rationale

22 In our first consultation we suggested that the general principle should be that where the loss of money relates to single retainer, that should be dealt with as a single claim on the Fund. In light of the responses received we acknowledged that by linking a single claim to a single retainer may lead to an unfair outcome is some circumstances. We agreed that our approach should be flexible enough to reflect factors such as the nature of the relationship between parties to the retainer (or those benefiting from the services provided in the case of beneficiaries).

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Responses to the consultation

23 The Law Society, local law societies and the Legal Ombudsman agreed that this revised approach was fairer than applying the limit to a single retainer which is what had been proposed in our earlier consultation.

Our view

24 There was general support for this proposal and no issues raised that we think require us to amend our revised approach to how we will apply the single application limit.

25 We will develop guidance to show how the single claim limit will apply to each individual applicant that makes an application (or applications) for the loss incurred by them arising from a single event or set of connected underlying circumstances.

Recommendation: to apply the single claim limit of £500,000 to each individual applicant receiving a payment.

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Our other previous proposals

26 In the second consultation we confirmed that that we would be proceeding with some proposals from our first consultation. Some respondents to the second consultation took the opportunity to comment on these again. For completeness we include a summary of this feedback. We do not think that any new issues have been raised that affects the Board's previous decisions, so we are recommending proceeding with these. Given the significant concerns raised again in relation to the reduction in the single claim limit, the Board had a full discussion on this issue at its 22 June workshop. For this reason, we include more detail about this issue than the others.

Reduction in single claims limit

What was the consultation proposal?

27 We confirmed in the January 2020 consultation that we intended to proceed with our earlier proposal to reduce the single claim limit from £2m to £500,000 (paying a higher amount only in exceptional circumstances).

Rationale set out in the consultation

28 We considered this to be a fair and proportionate maximum payment level, which compares favourably against comparable schemes including those of other legal services regulators and for other professional services. And this would cover the vast majority of claims. We set this out in the evidence and analysis annex that we published with the consultation[1]. We highlighted in the consultation that in the period between 2010 to 2018, this would have seen lower payments for around only 0.4% of applications paid (or where we are reserving a possible payment) but this would amount to £10m less in value. We felt that this was a proportionate position to take.

Responses to the consultation

29 In the first consultation, we received strong opposition to the proposal. This was repeated in the feedback to the second consultation, mainly based on a principled position that we should not be reducing consumer protection.

30 We did not ask a specific question about this change in the second consultation but both the Legal Services Consumer and the Law Society reiterated their strong opposition to this change arguing that given the low numbers of people affected the resulting reduction in the liabilities of the Fund would be limited.

31 Some respondents also raised concerns that the reduced claims limit may have a disproportionate impact on small firms and their clients. This is because sole practitioners and small firms are more likely to have insurance claims refused where there has been dishonesty, on the basis that the sole practitioner or all partners were complicit in the dishonest act. In these circumstances the clients of sole practitioners

[1] https://www.sra.org.uk/globalassets/documents/sra/consultations/supporting-evidence-analysis-comp-fund.pdf?version=48f268

or small firms will only be eligible to claim up to £500,000 from the Fund whereas in larger firms the insurance cover will be a minimum of £2m per claim. The view was that this difference may put people or lenders off using small firms that are already facing difficult market conditions.

Further information

32 We have updated our data on impacts and explored the issue raised about potential impacts on small firms and those that use them. The analysis is set out in more detail in our draft Impact Assessment (attached as Annex 4) but our main findings are:

- the absolute level of protection provided is proportionate and will provide full protection for the overwhelming majority of people: only 32 payments over the period 2004 - 2019 have been above £500,000 which is 0.2% of all payments. For conveyancing and probate the limits cover at 90% and 96% of all transactions respectively

- that characteristically vulnerable (older, lower social grading, BAME, disabled) are less likely to use the types of legal services that give rise to large claims on the Fund (conveyancing and probate). They are also less likely to use a small firm (e.g. 48% of black African/Caribbean people used small firms compared to 78% of white people; and 67% of disabled people who are limited a lot, compared to 77% no disability) [2], and

- the likelihood that small firms will be undertaking work that may involve very large sums of money that would not be covered by the £500,000 limit is low. For example, our data suggests that nearly 9 out of 10 small firms either derive less than 25% of income from conveyancing work or are located outside of property hotspots.

Our view

33 We do not consider that there is significant new evidence that impacts on the Board's rationale for this proposal. We will develop our guidance which sets out the exceptional circumstances in which we might consider making a higher payment.

34 By their nature, exceptional circumstances cannot be comprehensively defined. We would expect that it would be rare for more than £500,000 to be awarded.

35 Factors that we will consider in making a higher payment will include for example:

- the impact of the loss on the claimant. We are more likely to find exceptional circumstances where the loss has a potentially catastrophic impact on the claimant's quality of life, and
- the likely duration of such an impact and the ability of the applicant to "make up" losses by other means.

[2] https://www.legalservicesconsumerpanel.org.uk/what-we-do/research-and-reports#2019

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Recommendation: to confirm we will proceed with the earlier decision proceed to lower the single claim limit from £2m to £500,000 (paying higher only in exceptional circumstances)

Exclude litigation costs

36 We confirmed that we would proceed to exclude litigation costs other than in exceptional circumstances. This is to prioritise payments that provide redress for direct financial losses and to protect against the risk of being tied to paying for escalating litigation costs.

37 Concerns were raised in the first consultation about the impact on applicants' ability to pursue other avenues of redress. These were repeated in the second consultation with the Law Society arguing that is was unfair on those who may have been entirely reasonable in seeking to recover their losses through litigation which, if successful, might obviate the need to apply to the Fund for part or all of their loses.

As set out in the consultation, our approach to dealing with applications is to factor in an individual applicants' ability to pursue other avenues of redress. Where they do not have this ability, we are more likely to process their claim to the Fund. We do not expect most individuals to pursue for example, litigation where this is likely to have high costs, particularly given that payment from the Fund might be low relative to those costs.

38 We will advise applicants on our expectations in relation to them pursuing other means of redress - proportionate to their circumstances as we process their application.

39 In this context, we reserve the right to pay some costs on an exceptional basis, proportionate to the nature of the application. This might be where we think that the pursuit of another remedy is highly likely to be successful, but the applicant does not otherwise have the financial resources to pursue them.

Recommendation: to confirm we will proceed with the earlier decision to exclude litigation costs and paying them only on an exceptional basis

Our expectation about the conduct and behaviour of applicants

40 We said we would proceed with the proposal to take a more robust approach to how we take into account how an applicant has behaved when applying for a payment or if they failed to take steps that could have mitigated their loss. We also confirmed we would introduce an explicit requirement for full and frank disclosure by an applicant when requesting a payment from the Fund. This would strengthen our ability to get the evidence we need to understand the circumstances leading to the loss.

41 This was accepted as a legitimate approach although clear guidance needed to be provided. No further feedback was provided in the second consultation.

42 We will issue guidance on when the conduct of the applicant may warrant refusal or reduction. We will publish consumer friendly guidance on what is meant by full and frank disclosure

Recommendation: to confirm we will proceed with the earlier decision to clarify our expectations around the conduct and behaviour of applicants and how we take this into account when deciding whether to refuse or reduce a payment

Limit where we will consider a claim where no insurance policy

43 We said that we would proceed with the changes to limit circumstances where the Fund provides a safety net where insurance is not in place. This would mean that we would limit applications to where a firm that is authorised by us had failed to get our required insurance, and we would make it clear that we would not make payments should a PII become insolvent and polices re disclaimed.

44 In their response to the second consultation the Legal Services Consumer Panel thought that economic situation would make it more likely that a PII insurer could fail and that we should maintain protection for consumers in this situation. The Professional Negligence Lawyers Association also thought we should allow payments if an insurer fails, as did the Westminster and Holborn law society who also observed that this was one of the limited benefits that the Fund provided for clients of largest firms.

45 Our view remains that the Fund should not be a last resort for any financial loss suffered by the client of a solicitor. We will continue to discuss with the Financial Conduct Authority whether there may be changes to Financial Services Compensation Scheme for consumers of large law firms to be able to claim on their scheme when an insurer becomes insolvent.

Recommendation: to confirm we will proceed with the earlier decision proceed to limit the circumstances the Fund can make a payment where a firm does not have insurance in place

Exclude barristers and other third-party claims for unpaid fees

46 We said we would proceed to exclude applications from barristers and other third-party experts which relate to their unpaid fees. Where the third party is an expert or a professional themselves, they are more likely to be able to protect themselves in their commercial arrangements with the solicitor. If something does go wrong, they are also likely to have the skills to pursue other routes of redress, such as the debt recovery process.

47 The Law Society took the opportunity to repeat concerns that this would undermine trust in the profession. They disagreed that that barristers and experts necessarily had expertise to protect own interests and they may be inclined to stop working for instructing solicitors because of fears of not getting paid.

48 The rationale remains that the Fund should not be used as a substitute for debt recovery or claim for breach of contract processes.

Recommendation: to confirm we will proceed with the earlier decision to exclude barristers and other third-party claims for unpaid fees

New suggestions received

Introducing a minimum payment level

49 We received a new suggestion from the Law Society that we consider introducing a "de minimis" payment level which we will not pay out below. They suggested that then different minimum thresholds for different classes of applicants could be set (e.g. individuals, SMEs, charities and large businesses) that could be based on factors like income, wealth, or turnover. The Law Society did acknowledge that the proposal would introduce a new layer of administrative complexity. It is notable also that the suggestion would 'reintroduce' eligibility for large businesses.

50 The table below shows the number of cases in the last two years where payments from the Fund have been made of £50 or less, £100 or less, £325 or less and £500 or less respectively and the total amounts paid.

Payment value	Number of payments	Total paid
£50 or less	12	£464
£100 or less	16	£1,869
£325 or less	159	£31,683
£500 or less	321	£99,413

51 To make any difference to the volumes of claims administered the de minimis will have to be set at relatively high amount compared to amount that people save. To reduce volumes by around 10% and 20% the level would need to be set at £325 and £500 respectively. These are relatively large sums for many applicants. According to a 2020 survey conducted by the Royal Society of Arts/Populus, 32% of workers in the UK have savings of less than £600. Research in 2016 by the Money Advice Service found the figures to be even lower, with 40% of the working population having less than £100 in savings.

Our view

52 In order to reach the volume of claims that would have a material impact on the administration cost of the Fund the level of the minimum payment would be need to be set at a level that people that claim on the Fund cannot afford to lose. The creation of different minimum thresholds for different classes of applicants would also introduce the kind of wealth- based judgements that respondents to the fist consultation were keen to avoid. This would also introduce additional complexity to the claims process as well as impacting on our control of costs. For these reasons we do not think we should introduce a minimum payment level or levels

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Other issues raised in responses

Intervention and operational costs

53 The Law Society and the Legal Services Consumer Panel responses questioned the recovery of intervention costs through the Fund and what they saw as escalating costs. They questioned whether it was right that these costs should come from the Fund. And if it was, whether focusing on reducing these costs might reduce the need to introduce measures to better prioritise direct grants. The cost of interventions and whether they should be paid from the Fund was not something we discussed in this second consultation.

54 The Law Society also commented on the costs of administrating applications and that more should be done to reduce these if they are increasing.

Our view

55 The Solicitors Act 1974 provides that the cost of interventions may be paid from the Fund. The Board confirmed in 2013 that they considered that that it was proportionate and appropriate to do so. The alternative is to fund through the practising certificate, which is still a cost to the profession. The Board felt that the Fund does carry reserves that allows it to better deal with the unpredicted costs of interventions and the connected payment of grants, which could not be accommodated within the SRA budget in the same way as other operational activities.

56 We intervene in firms to protect the public interest on the grounds set out in legislation. We cannot control the instances where this threshold is met, and this varies year on year. We make every effort to work with firms to avoid the need for an intervention. And we are publishing new guidance to highlight our work in this area and encourage early discussion with firms where they are in difficulties.

57 The cost of an intervention will depend on the scale of work involved in closing the solicitor's practice and the amount of work that is involved in sorting through what could be a very poorly managed firm. In all cases we aim to allocate our resources efficiently so that the cost of any intervention is proportionate. Where possible, we will always look to the intervened firm and culpable individuals to recover the costs incurred. The total recovered over the past three financial years was circa £8.7m. This is made up of both intervention costs and grant recoveries. This figure does not however, include any subrogation back to the Fund from the statutory trust.