Indemnity Insurance and the Regulatory Revolution

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The SRA Handbook came into force on 6 October 2011, introducing a new Code of Conduct that was in part prompted by the advent of alternative business structures, and the desire of the SRA to open up the legal market in the wider public interest. That drive to keep pace with the changing consumption of legal services will, with effect from 25 November 2019, give rise to the new and more streamlined SRA 'Standards and Regulations', and the creation of two codes of conduct for firms and solicitors.

The latest reforms followed the SRA's March 2018 consultation paper which proposed significant revisions to the Minimum Terms & Conditions ("MTCs"), to include dramatically reducing the minimum limit of indemnity, as well as an overhaul of the operation of the Compensation Fund. Amidst much opposition, in late 2018 the SRA decided to park the issue of changes to PII cover, but to focus on plans to liberalise the market, and effectively to change the way that solicitors are regulated.

The aims of the SRA as part of its 'Looking to the Future' programme are to focus upon what is deemed most important; maintaining high professional standards (and the protection of client money) and making it easier to both access legal services and for firms and solicitors to perform those functions. A major part of this involves the rise of the 'freelance solicitor' and the ability for 'non-reserved' legal work to be conducted from outside regulated firms.

According to SRA statistics, almost one quarter of firms are sole practitioners. Balanced with the pressures of ensuring there is a sufficient work stream, it can provide greater flexibility to fit around changing lifestyles and, ultimately, more control. The scope to be able to provide reserved legal activities as a freelance solicitor is an extension of this, without needing to be a formally recognised sole practitioner and with a reduced regulatory burden.

To be 'freelance', the SRA's 'Authorisation of Individuals Regulations' sets out a series of preconditions. The solicitor will be more than three years qualified, self-employed and practising in their own name rather than through a trading name or company. They will be instructed directly by their clients, and be paid directly for the services. They will not employ anybody and not be able to hold client money (other than for disbursements which have not yet been paid).

However, it then becomes far more vague around the professional indemnity insurance requirements. If the freelance solicitor is carrying out purely non-reserved legal activities, they can do so without any form of PII. This includes Will writing and employment advice, both of which are fertile areas for negligence claims.

As for reserved legal activities, the freelance solicitor only has to take out and maintain "adequate and appropriate cover" for the services provided, taking into account any alternative arrangements that either the solicitor or client may have made. "Adequate and appropriate" as a concept remains undefined, but the basic standard of protection afforded by the MTCs falls away. More significantly from the perspective of the client, if the solicitor has failed to put appropriate insurance in place, there will be no right of recourse by the client to the Compensation Fund. It necessarily increases the potential risks to the client unless wholly satisfied that there is suitable insurance in place, and that the policy will respond to the specific reserved activity.

It remains to be seen how this will operate in practice, whether Insurers will have the appetite to write cover that will be acceptable to the SRA as 'adequate and appropriate', how those policies will be priced, and if clients will be happy to relinquish the security of the MTCs in favour of greater flexibility and freedom of choice in representation. Having witnessed what can go wrong on seemingly the simplest of matters, the consequences of inadequate or no insurance could be devastating, which clients will need to appreciate before embracing the changing models of legal representation.

Equally, and with only three months to go, far greater clarification will have to follow from the SRA before it can be

expected that there will be any significant adoption of these new methods, and whether the reforms have in turn achieved the desired aims of improving access to justice, promoting competition, and helping to increase consumer protection. Without careful control and guidance, the potential variations in quality of cover have the danger of confusing consumers and leaving them exposed in the unfortunate event that something goes wrong.

Post six year run-off cover

Whilst considering the forthcoming changing insurance landscape for solicitors, it is worthwhile revisiting another imminent deadline: the 2020 closure of the Solicitors Indemnity Fund, which will finally bring an end to the post-six year run-off cover extension for firms that have closed without a successor practice.

As it stands, on closure of a practice the former clients are currently protected by six years of run-off cover, either pre-arranged by the retiring partners, or else provided by the last Insurer on risk in accordance with the MTCs. However, with PII policies operating on a 'claims made' basis, many professional negligence claims do not emerge until some years later and so would potentially fall between the (i) end of the six year run-off period and (ii) the 15 year long stop date under s.14B of the Limitation Act 1980. The additional cover afforded by SIF helped to bridge this gap.

In 2016, and despite its own research suggesting that 11% of claims arose 15 years or more after a firm's closure, the SRA confirmed that there would be no extension to the arrangements for providing cover beyond the run-off period, and similarly declined to extend the SIF deadline for a further three years, until 2023. The SIF will run down its existing book of claims, but will not then be accepting any new notifications.

All of this means that partners and employees of firms that closed without a successor practice should give careful thought to obtaining post six-year run-off cover after 2020, to avoid the danger of being held personally liable for any historical claims. We are aware of at least two Insurers having expressed an interest in providing such cover, although the actual products have not yet been developed and will likely only emerge once they are needed next year.

It is not clear what they will look like or how they will be priced, but policies are predicted to be underwritten on an individual basis with a careful consideration of the risk, and the ability to refuse to quote. This dictates that a detailed record should be preserved of the closed firm's historical data and claims history, to present to underwriters. It is also anticipated that, unlike under the constraints of the MTCs, the premium will have to be paid before cover is confirmed, hence an additional expense that it would be prudent to budget for as part of the closure process.

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