CLC consultation on new arrangements for PII

The Law Society's response

May 2016

Introduction

1. The Council for Licensed Conveyancers (CLC) is consulting on new arrangements for professional indemnity insurance (PII). While the CLC invites answers to specific questions, it also welcomes comments on the proposals as a whole.

2. The Law Society (the 'Society') notes the interaction between this consultation and the current SRA consultation 'Removing Barriers to switching regulators'. SRA participating insurers are obliged to provide six years' run off cover to firms closing down or switching to become regulated by another 'Approved Regulator'[1]. The SRA believes that the considerable cost of run off cover[2] acts as a barrier to firms who wish to leave SRA regulation. It therefore proposes to waive the run off cover requirement for firms transferring to another Approved Regulator. The CLC's proposed arrangements for PII dovetail with the SRA's consultation in that they would facilitate the ability for firms to choose the most appropriate regulator. The Society will be responding to both consultations.

3. A significant characteristic of the CLC's proposals is that a firm switching to CLC regulation would be able to purchase PII from a CLC Participating Insurer, inclusive of six years' run off cover at no additional cost at the point of closure. There is no reason in principle why CLC Participating Insurers should not provide insurance to firms carrying out conveyancing and/or probate work that were previously regulated by another Approved Regulator. However, we would not support a system that allows SRA-regulated firms to switch regulator where the result is a dilution in the financial protections afforded to clients of the SRA-regulated firm. In particular, the high level of consumer protection provided by the SRA run off requirements is not reflected in the PII arrangements of other Approved Regulators. For example, if the CLC's proposed PII arrangements are approved, there is a potentially negative impact on clients who make a claim that would have been covered under SRA-mandated run off cover but is not covered under CLC-mandated run off cover. We will be raising the issue of consumer protections in our response to the SRA's consultation.

Responses to specific questions

(**A**) **Do you agree with the proposal for the CLC to permit insurers who sign up to its Participating Insurers Agreement to provide professional indemnity insurance for CLC practices incorporating the CLC PII Policy Wording at Annex 3?**

4. The Law Society has no particular view on the move from the Master Policy arrangement to a Participating Insurers Agreement. However, in finalising the new arrangements, the CLC may wish to consider the following:

- The CLC states that it will seek to identify at an early stage practices that may not be able to afford PII from a participating insurer. The CLC has not addressed in the consultation paper how it will respond to

[1] As defined under the Legal Services Act 2007.
[2] The Law Society's 2015-16 PII survey found the median cost of run-off cover to be 300% of annual premium.

situations where firms have no PII cover but are closing down. This could be of immediate concern in light of the timetable for introducing the Participating Insurers Agreement.

- Where claims in the run off period exceed £2 million in aggregate, clients may apply for a grant out of the CLC's Compensation Fund. The CLC will need to consider the level of funding that the Compensation Fund will require in order to cover such claims. We note that the Compensation Fund has been subject to successful challenges in recent years.[3]

- CLC participating insurers must have a financial standing rating of 'A' or above, and notify the CLC if their rating falls below this level. The CLC will have to consider what action it will take in these circumstances.

5. The Law Society's comments in relation to Annex 3 clauses 8.10 (Run-off Cover) and 8.11 (Scope of Run-off Cover) are included in response to (B) below.

(B) Do you agree the proposal for run off cover to be provided to practices which close at no additional cost to those practices when they close?

Run off cover provided at no additional cost

6. Although six year run off cover would be provided at no additional cost to practices at the point of closure, it is to be expected that the premiums paid by CLC-regulated firms would be higher than they currently experience, in order to reflect the included cost of run off cover. This arrangement could be beneficial to some firms, in spreading the cost over a period of time rather than requiring a substantial one-off payment at the point of closure (as is the current process). However, a firm that continues to trade for a long time could end up paying substantially more than the market cost of the run off cover.

7. If the SRA's proposals are enacted, firms switching from SRA to CLC regulation may not find any saving. An underwriter would price the insurance premium for the first year in the knowledge that it would have to cover six years' worth of run off claims at some point in the future. The exception may be that, theoretically, a regulated firm wishing to close could simply switch to CLC regulation for its final year in practice and avoid the run off premium set by the SRA insurer. CLC participating insurers would not know how for how long the entity intended to continue to practice and could therefore have difficulty setting an appropriate premium. Indeed, an insurer knowing that it has to potentially provide seven years' cover for one year's premium may be more likely to offer cover at substantially higher cost than the market rate or decline cover, particularly for smaller firms.

[3] *Queen on the application of Nigel Coatman and Andrew Golub v Council for Licensed Conveyancers* [2012] EWHC 1648 (Admin)

Scope of cover

8. The risk that regulated firms wishing to close could switch to CLC regulation in order to avoid a run-off premium is significant. The CLC can have little indication of to what extent this might occur, and what liabilities previously regulated firms may bring. Conveyancing is one of the work areas of highest risk and can give rise to high value claims. It therefore imperative that consumers are adequately protected by way of an appropriate level of insurance cover if something goes wrong. For this reason, the lack of equivalence of SRA and proposed CLC MTC PII cover is a cause for concern.

9. There are a number of differences between the proposed CLC minimum terms and conditions (MTCs) and the existing SRA MTCs.

    - While both sets of MTCs require insurers to provide £2 million in compulsory cover for any one claim, the SRA requires ABSs, limited companies and LLPs to have £3 million of cover. There is no such requirement in the CLC's proposals for CLC-regulated ABSs, limited companies and LLPs.

    In relation to run off cover:

    - The SRA MTCs prescribe a £2 million limit on individual claims during the run off period, whereas the proposed CLC MTCs require a £2 million limit on claims in aggregate. If the SRA's proposals are enacted, clients of previously SRA-regulated firms could be left exposed as a result of the reduced level of run off cover under the CLC PII arrangements. This is a significant risk, given that conveyancing is typically one of the highest risk areas of work and could produce high value claims, easily exceeding liabilities in excess of £2 million over six years. While the CLC notes that 'since 2011 the aggregate claims in run off have not exceeded £100,000'[4], this is an incomplete figure. This figure would appear to relate to their current market and makes no attempt to forecast the market should solicitors' firms switch. In addition, although the book for the year 2011 is quite mature, it still has another year to run in which claims may surface. By contrast, the claims year 2015 is very immature in run off terms, and the full extent of claims will not be known until 2021. Indeed, bearing in mind that the market in the last four years has been characterised by low interest rates[5] and low claims, there is insufficient basis for extrapolating the £100,000 figure. Rather, it is possible that the number and value of claims will rise to the extent that a £2 million limit on claims in aggregate over six years will not be sufficient. Solicitors' clients should not receive a lower level of cover because their provider has switched regulator. In response to the SRA's consultation, we will argue that clients should be afforded equivalent SRA MTC run off cover if the firm switches to another Approved Regulator.

[4] Paragraph 25

[5] In any settlement of a successful claim, the insurer will have to take into account interest on the amount payable over the years of detriment suffered at the prevailing rates. A few years of interests rates at 6%, for example, would increase the level of damages significantly.

(C) Do you agree the proposed amendments to the CLC's Professional Indemnity Code and Guidance and to the CLC's Professional Indemnity Insurance Framework at Annex 1 and 2 respectively?

The Law Society has no comments.