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SRA CONSULTATION ON FINANCIAL PROTECTION RESPONSE FROM CLLS PROFESSIONAL RULES AND REGULATION COMMITTEE

The City of London Law Society ("CLLS") represents approximately 14,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 18 specialist committees. This response in respect of the SRA financial protection review has been prepared by the CLLS Professional Rules & Regulation Committee.

Question 1 – Do you have any comments on the SRA's decisions, set out in the policy statement, which form the basis for the changes which we are now consulting on?

Following the previous consultation, and the decisions that have now been taken, our only comments are:

1. It was clear that the Assigned Risks Pool could not continue in its present form, particularly in light of comments from the qualifying insurers.

2. We could see the practical difficulties that there would have been introducing a replacement for the ARP before 30 September 2013, and see the reasons for the reduction on the cover provided by the ARP to six months from October 2011.

3. It seems a fair proposal that the insurer of the expiring policy must provide a further 90 days' cover if the insured does not obtain a new policy. Balancing the public interest with that of insurers, as well as the profession, it is appropriate that the exposure for that 90 day extension be borne by the insurer of the expiring policy. That insurer decided to accept the risk in the previous year and, by definition, has been unwilling or unable to agree terms with the insured for a further year.

4. Although the ARP has to date been provided by the qualifying insurers, that cost has been passed on to the profession through higher premiums, which will have included not only Insurance Premium Tax but also additional costs. The profession will now bear the costs of uninsured claims directly through the Compensation Fund after 1 October 2013, which may result in some savings.

5. The proposed funding for the ARP in 2012/13 seems an acceptable balance between the qualifying insurers and the profession, with the first contribution consisting of the sums left in the Solicitors Indemnity Fund.

Question 2 – Do you have any comments on changes proposed to the Qualifying Insurers' Agreement and the SRA Indemnity Insurance Rules?

We have considered the drafting changes proposed for the QIA and SIIR and agree that they will introduce the changes required by the decisions made by the SRA announced in April 2011. On a point of detail, the page numbering for Appendix 2 in the contents page of the SIIR is incorrect. Appendix 2 now starts at page 78, with consequential changes on following pages.

Question 3 – Do you have any comments on the changes proposed to the SRA Authorisation Rules?

We have reviewed the proposed changes and have no comments on them.

Question 4 – Do you have any questions on the changes proposed to the SRA Compensation Fund Rules?

We have reviewed the proposed changes and have no comments on them.

Question 5 – Credit Ratings of qualifying insurers

We agree that it is not for the SRA to require qualifying insurers to possess an independent credit rating and that that is a matter for the Financial Services Authority, in addition to the fact that the SRA does not have the necessary powers or experience. Such a requirement could also be a barrier to entry and therefore reduce competition in the market. However, we agree that the provision of better information by insurers to firms would be likely to reduce risk without damaging competition. We therefore support the amendment proposed to the Qualifying Insurers' Agreement which will require insurers to confirm their credit and/or insurer financial strength rating (if any), or to state that it has none, and to give the identity of the rating agency that has provided the rating.

The proposed drafting, which requires insurers to give such details in the "Details of the Insurer" section, achieves this aim. It also follows, as is proposed, that there should be a requirement to update such information in clause 6.5 of the QIA, where the qualifying insurer must give information about any change in its status within five business days.

Question 6

6.1 – Acceptance periods

We agree that it is not conducive to the proper operation of the market for insurers to leave quotations open for only a very short period. We would therefore favour the inclusion in the QIA of a requirement that quotations should be kept open for a minimum number of working days and would favour ten as that minimum.

6.2 – Policy cancellation for non-payment of premium or misrepresentation

We are asked to consider again the question whether the policies should be cancellable for non-payment of premium or for misrepresentation in proposal forms. This is against the background of the SRA having decided in April this year not to change the current arrangements but to reconsider the matter in due course, particularly in the context of the new arrangements being introduced in 2012/2013, including the end of the Assigned Risks Pool. It involves balancing the public interest in having solicitors insured with the interest of the insurers

themselves in being paid the premium and in having accurate information given to them, as well as the interest of the profession.

Those two interests of insurers can be differentiated and, in our view, that fact points towards different consequences for the different failures by the insured.

The fact that a firm has not paid its insurance premium will be known by the insurers as soon as the due date has passed. Either then, or after a suitable further period, the insured could be told that in accordance with the policy terms, the policy was cancelled for non-payment of the premium. It would follow that (unless other insurance was obtained) the practice would have to cease operation and it might be that run-off cover would be provided under the terms of the previous policy for the short period of the new year before the default in premium payment (It is not clear whether this is contemplated in the proposals).

The fact that there could be no argument about whether the premium had been paid or not and the unfairness of insurers having to carry a risk when they have not received a premium points towards a rule that the policy should be cancellable for non-payment of premium. As an alternative, insurers might insist that the premium should all have been paid before the inception date of the policy. Nevertheless, we do have a concern that to make even one of these changes to the Minimum Terms could open the door to a broader revision of those terms which would be undesirable given the benefits that they confer on both the public and the profession. We would therefore leave it to the discretion of the SRA whether it is worthwhile to pursue this point.

With misrepresentation in the proposal by the insured, the situation is altogether less clear. Such misrepresentation may only become known long after it was made. Indeed it may never become known. When it does become known there is the issue whether it was innocent or otherwise, and the application of the complexities of the law of the duty of good faith and avoidance.

The scope for argument on these issues and the uncertainty caused by it, as well as the drastic consequences for the solicitors, point towards retaining the present situation where the insurers may not cancel the policy for misrepresentation, innocent or otherwise.

John Trotter

6 December 2011

THE CITY OF LONDON LAW SOCIETY
PROFESSIONAL RULES AND REGULATION COMMITTEE

Individuals and firms represented on this Committee are as follows:

Chris Perrin (Clifford Chance LLP) (Chair)

R. Butterworth (Bird & Bird LLP)

R. Cohen (Linklaters LLP)

Ms S. deGay (Slaughter and May)

Ms A. Jucker (Pinsent Masons LLP)

J. Kembery (Freshfields Bruckhaus Deringer LLP)

Ms H. McCallum (Allen and Overy LLP)

Ms J. Palca (Olswang LLP)

M. Pretty (DLA Piper UK LLP)

J. Trotter (Hogan Lovells International LLP)

Ms C. Wilson (Herbert Smith LLP)