MFL Professional
INSURANCE BROKERS

Risk Update

Welcome to the August edition of Risk Update.

The Gold Rolls Royce - not yet in the scrap yard

A few years ago I chaired a "Round the Table" discussion on behalf of Manchester Law Society (MLS), with the participants including officials and council members of MLS and very senior insurance market representatives who travelled from London to attend.

The scope of the Minimum Terms Cover (MTC) for professional indemnity insurance was a hot topic then, as it continues to be today. One particular comment has stuck in my mind since that day. I had responded to a question along the lines of "Compared to the insurance cover required by other major professional bodies such as the ICAEW, RICS, RIBA etc, the MTC demanded by the legal profession is akin to a gold-plated Rolls Royce, when a standard saloon would have been adequate". This provoked a retort by a senior MLS Council Member, which has stuck in my mind since, to the effect that **"Sorry, Kevin, you are wrong: the MTC are the equivalent of a solid gold Rolls Royce, and will cost the profession big style in the future".**

There we had it. Likening the MTC to a solid gold Rolls Royce that would cost the profession dear proved to be a very perceptive comment, particularly as it was made before the economic crash when the profession had become accustomed to annual premium reductions, not massive increases.

Since then the Roller's been customised a bit. One major modification has been the replacement of the Assigned Risk Pool (ARP) by a specific obligation for insurers to provide run-off cover, whether paid for or not, if the insured has to shut up shop: another one of those "be careful what you wish for" moments for the insurance market.

They say timing is everything. Well, the SRA has gone and done it again: **"SRA Discussion Paper: Protecting Clients Financial Interest, 8 July 2015"** is now with us. After last year's embarrassing fiasco for the SRA, it has demonstrated yet again a complete lack of understanding of how the insurance market works. And this after the SRA promised that the consultation paper would be available to the insurance market by Christmas 2014.

To see the problem that will be created by this timing, you need look no further than the front page article published in The Law Society Gazette of 13 July 2015: **"SRA in renewed call to lower minimum cover for insurance".**

The SRA states in the Discussion Paper:

"We will set out detailed proposals in a further consultation in early 2016. This means that the earliest any major changes can be implemented by is October 2016"

I presume this means that the changes will catch the 85% or so of policies issued to firms of solicitors that still fall due for renewal on the old common renewal date, in September 2016.

I am somewhat bemused by the Discussion Paper, particularly in the light of what was proposed and subsequently rejected by the LSB last year. It asks for feedback on a range of issues, some of the key ones being as follows:

- level of indemnity;
- insurer's obligation to provide run-off cover;
- period of run-off cover;
- consistency of cover for all clients;
- payment of policy excesses, including insurers' obligation to pre-fund the excess payment;
- ability of insurers to deny cover for claims.

The potential outcomes of the above will have an effect on the Solicitors' Compensation Fund, which is of course the province of the profession and not the concern of the insurers.

The SRA has at least learned something following last year's fiasco, even if it's not about the timing. It is seeking information from the insurance market, which it did not do last year and without which it made blind decisions. The SRA does not have credible evidence to support its suggestion that there would be significant premium reductions if, for instance, the minimum limit of indemnity were to be reduced to £500,000. Of course, some firms might benefit financially but there is no proven case that there would be any saving for the majority of eligible firms; in fact the reverse is possible because of the knock-on effect on the cost of top-up cover.

The level of indemnity is a difficult area. The SRA's position is that it is the responsibility of firms to assess what limit of indemnity is appropriate. This is not so easy. For a start, some firms will simply purchase the minimum amount of cover required to satisfy the regulator in order to save premium, without regard for their exposures or the consequences for their clients. Brokers and insurers will provide advice but understandably neither is in a position to recommend a specific figure. The availability of capacity might in some cases be a constraining factor and conversely it does have to be recognised that affordability may be an issue. What I would say is that some of the larger professional indemnity claims we have seen have arisen from seemingly innocuous advice, which quite simply would never have been factored into any consideration of what level of cover is advisable.

I can also state without fear of contradiction that, in the light of claim statistics for all professions over the last 20 years, a limit of £500,000 is not enough for the vast majority of practices. It could leave sole traders and partnerships massively exposed and lead to their financial and reputational ruin.

What does need to be avoided is any knee-jerk reaction to put solicitors' indemnity limits on a par with, say, those of the ICAEW, following the opening up of probate work and any perceived need to level the playing field with respect to insurance limits and costs.

I will not comment in detail on the rest of the SRA's list of topics. The fundamental issue remains the Solid Gold Rolls Royce! The Minimum Terms are too wide and always have been, yet they are now the accepted benchmark for "customer protection" — and firms' protection, of course, albeit at a financial cost to them. Tinkering with the Minimum Terms could reduce the cost, but equally it would correspondingly reduce the protection provided. Little will change unless a calculated gamble is taken and certain types and sizes of firms are allowed to buy cover that is significantly reduced in all aspects, including the element of discrimination against certain classes of client.

I believe that insurers could work with this type of approach, providing that there were safeguards, possibly via the Compensation Fund and/or other levies. But I fear that it would be impossible to get all stakeholders to buy into this, given the many conflicting interests in play.

The imposition of solutions to one or two of the issues being consulted upon might only cause problems in other areas. I suspect this can will be kicked down the road for years to come, without a satisfactory resolution. But a long-term solution does need to be evolved, so as to create a balance of customer and solicitor protection. A one-size approach will not necessarily fit all.

By the time this article is published, I will be in warmer climes and in close proximity to a pool and a bar, as I suspect will be many MLS Members … enjoy your holidays!

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This article does not present a complete or comprehensive statement of the law, nor does it constitute legal advice. It is intended only to highlight issues that may be of interest to MLS members and solicitors. Specialist advice should always be sought in any particular case.

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