

This paper will be published

**Post six-year negligence and the Solicitors Indemnity Fund:
policy options for future consumer protection**

<p>Reason for paper</p>	<p>This paper sets out the case for future consumer protection for post six-year negligence and recommends a model for delivering this going forward.</p> <p>In summary, our recommendation is to:</p> <ul style="list-style-type: none"> • Maintain consumer protection for post six-year negligence as a regulatory arrangement with the same level of cover as the SIF. • Provide this via an indemnity scheme operating under the direct control of the SRA, to give us clear oversight of its operations and enable us to realise potential cost efficiencies and keep under review the costs and benefits of this protection. <p>The Board is thus asked to agree formally to dismiss alternative options for delivery of post six year cover, including the current model via the SIF.</p> <p>As a consequence, we would consult on our approach and the detailed rules to implement an SRA-controlled indemnity scheme, and reinstitute the programme of work to explore the wind up of SIFL and arrangements to manage its remaining liabilities.</p>
<p>Decisions</p>	<p>The Board is asked to:</p> <ol style="list-style-type: none"> (1) dismiss the option of a new compensation fund with discretionary criteria for the payment of post six year grants, equivalent to those applied to payments under the existing SRA Compensation Fund (paragraph 14 to 21) (2) dismiss the option of retaining the SIF operated by SIFL as a separate corporate entity. This will entail closing the SIF to notifications of new post six-year claims from 30 September 2023 (paragraph 22 to 33). (3) agree that we establish an indemnity scheme operating under the direct control of the SRA to deliver

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	<p>post six-year consumer protection (paragraph 34 to 48).</p> <p>(4) agree that the consultation paper setting out our approach and the detailed rules for implementing the scheme is signed off by the Chair (paragraph 49).</p>
Previous Board and committee consideration	<p>The Board decided in June 2021 to consult on the future of the SIF.</p> <p>The Board agreed on 5 April 2022 that we should seek a 12 month extension to the September 2022 deadline for notifying post six-year claims to the SIF, to allow further consideration of the issues and evidence raised in the consultation.</p> <p>The Board considered the emerging findings of this further work in an informal workshop session in July 2022.</p>
Next steps	<p>Subject to Board decisions we will publish a consultation paper on our approach and the rules to implement the recommended model.</p>

If you have any questions about this paper please contact: Juliet Oliver, General Counsel, at juliet.oliver@sra.org.uk

Post six-year negligence and the Solicitors Indemnity Fund: policy options for future consumer protection

Summary

- 1 This paper sets out the case for consumer protection for post six-year negligence and considers the options for providing future protection. It recommends that we replace the post six-year cover currently provided by the Solicitors Indemnity Fund administered by SIFL (SIF) with an indemnity arrangement operating under the direct control of the SRA, in order to:
 - allow us to maximise the potential cost savings identified in our recent work and ensure that the overall cost of the scheme is proportionate
 - give us clear oversight of the scheme's operation and enable us to keep under review its costs and benefits as a regulatory arrangement.

Background

- 2 In 2021 we launched a [public consultation](#) on the future of indemnity cover for loss where negligence comes to light more than six years after a firm closes with no successor. We set out our preferred option that the SIF should cease to provide cover for post six-year claims after September 2022, and that our future regulatory arrangements should not include post six-year protection.
- 3 In April 2022 the Board noted that the consultation had generated evidence that removing protection for post six-year negligence could have a greater impact on consumers than was suggested in our initial consultation analysis. It also noted that the legal profession appeared willing to fund the cost of ongoing protection for post six-year negligence via a levy, and did not expect material costs to be passed on to consumers as a result.
- 4 In view of this, the Board wished to explore further the options for proportionate consumer protection for post six-year negligence. The Board therefore [agreed](#) to seek a 12 month extension to the deadline for new claims to be notified to the SIF, to 30 September 2023, and this was approved by the Legal Services Board (LSB) on 1 September 2022. We have agreed to underwrite the potential liabilities of SIF Limited (SIFL) up to £6m to meet any shortfall arising from the extension.
- 5 This paper summarises further analysis we have carried out since April 2022 on the case for ongoing consumer protection for post six-year negligence and the options for delivering appropriate and proportionate protection.
- 6 In July 2022 the Board had an informal discussion about our ongoing work on options for post six-year consumer protection, and agreed to issue a [discussion paper](#) to update stakeholders. We invited feedback on that paper (see annex 1) and have taken it into account in our final recommendations.

The case for consumer protection for post six-year negligence as an SRA regulatory arrangement

- 7 The reasoning underlying our 2021 consultation proposals was that:
- the post six-year cover provided by the SIF delivers relatively little consumer protection at a high operating cost
 - maintaining this protection indefinitely would ultimately require further funding from the profession, and the costs involved could be passed on to consumers generally in the form of higher fees for legal services
 - given the low level and high cost of this protection, it would not be proportionate to make it part of our ongoing regulatory arrangements.
- 8 Since the April 2022 Board meeting we have reviewed this analysis in the light of other available evidence, including further consumer research commissioned by us and others. We have also engaged with bodies whose members work in fields with long-tail risks (such as conveyancing, wills and probates and professional negligence) to assess the impact such risks can have on consumers. This work has confirmed there is evidence that negligence emerging more than six years after a firm closes can cause significant detriment to the small number of consumers affected. The 2021 consultation also confirmed that there is no prospect of a market solution to manage these risks in the foreseeable future.
- 9 We have concluded that there is a stronger argument than we set out in 2021 for an ongoing regulatory arrangement for consumer protection for post six-year negligence. Meanwhile, responses to the 2021 consultation have indicated the profession is willing to provide new levy funding for this protection, and have suggested it is unlikely that a levy would lead to material costs being passed on to consumers generally.
- 10 We therefore consider that the SRA should continue providing post six-year consumer protection if it can be delivered in a way that:
- provides appropriate protection for consumers
 - is appropriately governed and consistent with other regulatory arrangements
 - is cost effective

and is therefore a proportionate regulatory arrangement. The rest of this paper considers options for doing so, and reaches a recommended way forward. If accepted, we propose taking forward a consultation on our approach and the detailed rules governing how this would be implemented.

Delivery options for a regulatory arrangement for post six-year protection

- 11 We have identified four core options to deliver future consumer protection for post six-year negligence as a regulatory arrangement. These could be

established using our statutory powers¹ to set up professional indemnity arrangements and compensation arrangements. The options are:

- A. retain the SIF operated by SIFL as a separate corporate entity, but with changes to reduce its operating costs
 - B. a statutory indemnity scheme operating under the direct control of the SRA, providing the same level of indemnity cover as the SIF, and benefiting from improved transparency and reduced costs through economies of scale
 - C. a new compensation fund within the SRA, using the administrative resources of the current SRA Compensation Fund but ring-fenced, and with different rules providing a level of consumer protection equivalent to the SIF
 - D. a new compensation fund on the same basis as option C, with rules providing additional criteria to apply to the payment of grants, which might include that this should act as a fund of last resort and require claimants to explore other routes before making a claim – as with the current SRA Compensation Fund designed to provide compensation for loss resulting from ethical failures.
- 12 Our initial view, which was informed by independent analysis carried out by WTW consultancy and discussed informally by the Board in July 2022, was that these options were likely to be significantly more cost-effective than SIF in its current form. We and WTW have assessed the options further since the July Board as set out below.
- 13 We outlined possible delivery options in the discussion paper published in August 2022, invited views, and discussed the paper with the Law Society, the Sole Practitioners Group, the Legal Services Consumer Panel (LSCP) and our post six-year virtual reference group. The paper received 116 responses; a high-level summary is at annex 1. The large majority of respondents supported retaining the SIF (with cost savings where feasible), on the basis that it provides appropriate protection for consumers and retired solicitors at a cost the profession is willing to fund, and the status quo is perceived by the profession to work well. Other respondents, including the Law Society, local law societies and the LSCP had no objection in principle to an SRA-run scheme if provides the same level of cover as the SIF.

Consumer protection

- 14 As outlined above, in the light of work since the 2021 consultation we have concluded that there is a stronger argument than we set out in 2021 for an ongoing regulatory arrangement for post six-year consumer protection.

¹ Under s36, 36A and 37 of the [Solicitors Act 1974](#).

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- 15 The post six-year cover currently provided by the SIF reflects the terms of the run-off insurance cover provided to closed firms under our Indemnity Insurance Rules. If a client has a valid claim it will be paid by the SIF, and the solicitor will not be personally exposed.
- 16 Of the options we have considered, A and B would provide the same level of indemnity cover as the SIF currently does, subject to some questions of detail discussed below. Option C would also be designed to make payments on terms that provide an equivalent level of consumer protection but through the vehicle of a compensation fund.
- 17 Option D would provide a significantly lower level of consumer protection than the other options. However, our analysis indicates that option D would not offer material cost savings over the other options (except reduced claims costs, which would merely reflect the reduced level of consumer protection). Some of the principles of the current Compensation Fund, such as providing consumer protection on a 'last resort' basis, are likely to be significantly less useful or relevant in the context of post six-year negligence, where the firm has closed long before the claim comes to light and individual solicitors may be deceased or hard to track down.
- 18 The August 2022 discussion paper invited views on three further specific areas in which the scope of the consumer protection provided by the Compensation Fund differs from the cover provided by the SIF. These relate to protection for large corporate claimants, the treatment of claimant costs, and the recovery of claim payments.
- 19 In the light of further analysis of these issues and stakeholder feedback on the discussion paper, we recommend that future consumer protection for post six-year negligence should follow the approach of the SIF on each of these issues. This is because the criteria designed for the Compensation Fund relate to ethical failures rather than negligence, and adopting them for post six-year negligence protection would reduce the scope of consumer protection in this area, while offering no material cost savings other than those arising from reduced consumer protection. The issues are discussed further at annex 2 to this paper.
- 20 Option D would also face higher long-term funding costs than the other options, since it would not be likely to benefit from access to the SIF residual assets, which have an important part to play in enabling cost savings as discussed under 'proportionality' below. That is because whilst we are able to apply the residual assets to an alternative indemnity arrangement, these would otherwise be returned to the Law Society, which would not be required to provide them to us to fund any alternative non-indemnity scheme. (The same consideration applies to option C, as discussed below).
- 21 Given that option D would provide significantly less consumer protection than other options with no material cost savings, we recommend the Board agrees to dismiss option D.

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Recommendation: the Board is asked to dismiss the option of a new compensation fund with discretionary criteria for the payment of post six year grants, equivalent to those applied to payments under the existing SRA Compensation Fund

Governance and consistency with our other regulatory arrangements

- 22 The SIF is an independent entity with its own infrastructure and governance costs, reflecting its past role as the provider of professional indemnity insurance to the whole profession until 2000. However, the SIF is now in run-off and delivers only a small niche function, handling only (i) claims relating to firms that closed before 2000 and (ii) post six-year claims. Consequently the SIF in its current form is not cost-effective as an open-ended consumer protection vehicle for post six-year negligence.
- 23 If we were to retain SIFL as a separate corporate entity, we would seek to streamline its governance: SIFL has a Board with an independent Chair and independent non-executive member, together with further non-executives members representing both the SRA and the Law Society. These arrangements reflect the SIF's wider pre-2000 functions and are not needed for a narrower post six-year consumer protection arrangement.
- 24 The SIF's limited operational requirements and systems also mean that it collects and reports only a limited range of data about the claims it receives. For example, there is little information available about the problems that give rise to post six-year negligence claims or the characteristics of the consumers who suffer losses. This makes it difficult to assess in a detailed way and fully understand the regulatory costs and benefits of the consumer protection the SIF provides.
- 25 We propose that any future SRA regulatory arrangement for post six-year consumer protection should be set up and governed in a way that delivers the same protection as the SIF, while also:
- providing us with clear oversight of the arrangement's operating costs and risk management decisions, and access to relevant management information about operations and claims²
 - enabling us to report transparently on, and keep under regular review, the costs and benefits of post six-year consumer protection
 - ensuring this is delivered in a way that is consistent with and works in parallel with our other consumer protection arrangements.

² As with the SRA Compensation Fund, we would need to manage the handling of events that may lead both to disciplinary action against a solicitor or firm, and a post six-year negligence claim.

Proportionality

- 26 As discussed above, we would want the operating costs of a new arrangement for post six-year protection to be materially lower than those of the SIF in order to be proportionate to the consumer benefit the arrangement will provide.
- 27 Responses to the 2021 consultation argued that given the expected low cost of any new levy funding for post six-year protection (discussed further below), a levy will not result in material costs being passed on to consumers generally. The Law Society has said to us that competition in long-tail areas of law such as conveyancing and wills is currently keeping fees stable despite substantial recent increases in PII premiums, and a post six-year levy is not likely to have any impact on fees.
- 28 However, market conditions can change and at least some of the costs of post six-year protection may be passed on to consumers in future, particularly if the cost of the protection rises significantly. It is therefore important that the new arrangement is as cost-effective as possible.
- 29 We have therefore worked with WTW, SIFL and others to assess the potential cost of new arrangements under delivery options A, B and C – that is, retaining and streamlining the SIF, or setting up an indemnity scheme or compensation fund providing equivalent protection, operating under our control. We have concluded that all three options offer scope for significant savings through (i) reducing the costs of claims handling, infrastructure and governance (including by outsourcing claims handling, as we already do for the Assigned Risks Pool and uninsured loss claims to the Compensation Fund), and (ii) optimising asset and liability management to make the best use of the SIF residual assets and future levy income.
- 30 However, the WTW analysis (see annex 3) indicates that maintaining an indemnity fund through an independent entity offers less scope for cost savings than the SRA-controlled options; option B is substantially more cost-efficient than option A in terms of both claims handling costs and infrastructure costs.. This would be the case even after streamlining its governance and reviewing its approach to claims handling. Maintaining an independent body would also offer less opportunity to optimise the cost-effectiveness of its asset and liability management. In summary, their work highlights that:
- The potential claims handling cost saving for Option B compared to the current SIF model is £300,000 to £400,000, and for Option C is £50,000 to £200,000
 - Even with fully modernised claims handling (which would be likely to take time to implement), option A can only generate £100,000 to £175,000 of claims savings
 - Option A also retains separate infrastructure, with maximum savings of £48,000 on related costs while options B and C offer savings of £120,000 plus

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- 31 Respondents to the August 2022 discussion paper raised concerns over the potentially significant cost of establishing a new arrangement to replace the SIF. Since an SRA-controlled arrangement would be delivered through SRA staff (using outsourced expertise as appropriate) and infrastructure, we do not expect these transitional costs to be significant, nor much if at all greater than the cost of modernising the SIF by updating its governance and systems and improving the cost-effectiveness of its operations.
- 32 Respondents to the discussion paper also expressed concern that the SIF's residual assets could be diverted to other purposes if transferred to a new arrangement under our control. However, if we close the SIF and introduce a new indemnity arrangement, all SIF's residual assets would be put towards the new scheme and could not be applied to wider non-indemnity regulatory purposes.
- 33 Given the analysis discussed above, we recommend that both for reasons of governance and proportionality, any indemnity arrangement should be operated under the direct control of the SRA as part of our wider set of consumer protection arrangements, and accordingly that the Board agrees to dismiss option A.

Recommendation: the Board is asked to dismiss the option of retaining the SIF operated by SIFL as a separate corporate entity. This will entail closing the SIF to notifications of new post six-year claims from 30 September 2023.

Preferred option to deliver post six-year consumer protection

- 34 Given our overall assessment of proportionality above, we consider that either of the other delivery options would be a proportionate regulatory arrangement. The comparative estimated costs and other implications of the two options are discussed further below, and a summary of WTW's analysis of the key points is at annex 3.
- 35 Therefore, this section of the paper considers the pros and cons of delivering post six-year protection via (i) option B, an indemnity scheme under our control, and (ii) option C, a new compensation fund. It covers the mechanics of each arrangement, their comparative cost implications, and the question of whether an indemnity or compensation arrangement is more appropriate in principle for the purpose of providing post six-year consumer protection.

Scheme mechanics

- 36 We have statutory powers to set up and deliver both professional indemnity arrangements and compensation funds. An indemnity provides security for loss arising from negligence and is automatically triggered when a solicitor (or the scheme on their behalf) receives a valid claim (being one that (i) meets the terms and condition of the scheme, (ii) is not excluded, and (iii) there are funds available to make the payment). The scheme essentially steps into the shoes of the solicitor reviewing the claim against the terms of cover under our MTCs

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and deciding whether to accept the claim, to seek to negotiate an early settlement for less than the full value of the claim, or to contest the claim, potentially through litigation. This approach to consumer protection is founded on the existence of a claim which could always potentially be determined in court.

- 37 In the case of a compensation fund for loss caused by negligence, the consumer applies to the fund for a grant to compensate for an alleged loss. A grant is by its nature discretionary. The fund must decide (i) whether a negligence-related loss has arisen, and (ii) whether the application fits the criteria of the fund and if so a grant should be paid. Unlike an indemnity scheme, the fund cannot usually negotiate a part-payment to settle the case. The process is quite separate from any legal claim that the consumer may have against the solicitor. As respondents to the August 2022 discussion paper have noted, a compensation fund cannot compel a consumer to use that fund, rather than a legal claim, to seek redress.
- 38 Board members have asked whether an indemnity scheme might provide support for a solicitor facing a claim arising from their own dishonesty. It would not, because our MTCs³ provide for an exclusion for claims arising from a solicitor's dishonesty or fraud.
- 39 An analysis of existing consumer protection arrangements we have carried out with WTW indicates that an indemnity scheme mechanism can have cost advantages over a compensation fund. This is because the indemnity involves fewer decision-making steps, and also allows scope for early negotiated settlement of claims (which can benefit both the fund and the claimant). This is reflected in the cost assessment below.

Cost implications

- 40 As noted above (paragraph 30), we expect that outsourcing claims handling could provide cost savings for either option in comparison to the current SIF model. However, the estimated claims handling saving available under an indemnity scheme (£300,000 - £400,000) is significantly higher than under a compensation fund (£50,000 - £200,000). Both models are expected to offer similar savings on infrastructure costs such as staff, premises and systems.
- 41 There are further cost considerations relating to the choice between these options. One is that in the event of the SIF being replaced by a SRA controlled indemnity scheme, its residual assets (net of any required to handle SIF's ongoing residual liabilities) would automatically pass to the new scheme, whereas if the SIF is replaced by a non-indemnity scheme, the residual assets must be returned to the Law Society to be used for the benefit of the profession.

³ See paragraph 6.8 of the MTCs, in Annex 1 to the [Indemnity Insurance Rules](#).

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- 42 In that event we would ask the Law Society to make those assets available for a compensation fund, on the basis that it would provide benefit to solicitors albeit indirectly. However, the Law Society would not be bound to agree. If a new compensation fund could not access all or part of the residual SIF assets, it would be less able to realise cost savings via asset and liability management, and would require more levy funding – potentially increasing the risk of costs being passed to consumers.
- 43 A further consideration is that in the event of the SIF closing, its live claims (including those relating to firms that closed before 2000 and those post six-year claims notified up to 30 September 2023) will need to transfer to another handler. If the SIF is replaced by a new indemnity scheme this would give us the option of arranging for the new scheme to handle these claims under rules mirroring those of the SIF, should this be considered the most appropriate way forward. If we use a compensation fund, we will need either to make arrangements for the fund to handle a small number of indemnity claims itself, or seek an alternative handler such as an insurer, which is likely to carry additional costs.

Principles

- 44 Beyond the mechanics and costs of the delivery options, there are broader questions about whether the type of vehicle we use is appropriate in principle, and whether stakeholders (including consumers, solicitors and the public) can readily understand its purpose and function. Relevant considerations here include:
- the arrangement is intended to provide protection on terms equivalent to the insurance protection provided under our MTCs, and it is simpler and more transparent to continue to deliver this via an indemnity scheme, rather than engineering a compensation fund to work in a similar way to an indemnity, which may result in confusion for consumers
 - indemnity provision is by its nature non-discretionary, whereas a compensation fund will retain at least a notional discretion to refuse claims, which may cause concerns that it provides a lower level of protection than an indemnity
 - a compensation fund providing quasi-indemnity cover is a less natural fit with both our existing compensation and insurance arrangements than an indemnity scheme would be.

Conclusion and recommendation

- 45 Taking all these points into account, we recommend that the Board agrees that we adopt option B – an indemnity scheme operating under our control – as the option to deliver consumer protection for post six-year negligence.
- 46 The WTW report published alongside our 2021 consultation (produced by its actuarial arm) referred to a potential levy of around £240 per firm being needed to maintain the SIF. Responses to that consultation suggested that new levy

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funding for post six-year consumer protection would not represent a material cost to consumers generally. The analysis now prepared by WTW's consulting arm, of the costs of a new arrangement, indicates that any future levy requirement should be no higher than – and potentially lower than this figure.

47 This is because the £240 estimate was based on assumptions which do not all read across to a new arrangement. This includes that any new arrangement should reserve for the value of any potential claims for firms that have ceased before the existing SIF arrangement closes. This would require considerably higher provision requirement than is likely to be needed for the options now under consideration. Further it did not take into account the use of investment income from the SIF's residual assets and as noted above our work has identified potential cost savings for a new scheme by optimising asset and liability management. Furthermore, the £240 assumes that the claims handling, operational and infrastructure costs of ongoing PSYROC would be the same as the existing SIF costs. The latest WTW analysis has shown that significant savings can be made in these areas.

48 A key operational issue for the new scheme will be how to balance the use of residual assets, investment income and new levy funding to cover operating and claims costs. If the Board agrees to consult on the basis set out above these decisions will be for the SRA Board. We do not currently expect that we would raise a levy on implementation of the new scheme, and would need to consider a number of variables which might lead to us deciding not to do so for some time. We will not therefore set out the potential amount of a future levy in the next consultation. However, as explained above we can confidently say that any levy will be less than the £240 set out in the report supporting our previous consultation. In the event that we decide to impose a levy to fund post six-year protection via an SRA-run scheme, we will consult at the appropriate time on the structure and value of the levy, as we do when setting levies for the SRA Compensation Fund.

Recommendation: the Board is asked to agree that we establish an indemnity scheme operating under the direct control of the SRA to deliver post six-year consumer protection.

Next steps

49 Following the Board's decision we propose to consult for 12 weeks on our approach and the draft rules for a new indemnity scheme, so the consultation would run until the end of 2022. We will then return to the Board in early 2023 to confirm the final rules before submitting them to the LSB for approval. We propose that sign-off of the consultation document is delegated to the Chair.

Recommendation: the Board is asked to agree that the consultation paper setting out our approach and the detailed rules for implementing the scheme is signed off by the Chair.

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Supporting information

Links to the Corporate Strategy and/or Business Plan and impact on strategic and mid-tier risks

- 50 This paper relates to objective 1 in the corporate strategy: *We will set and maintain high professional standards for solicitors and law firms as the public would expect and ensure we provide an equally high level of operational service.*

How the issues support the regulatory objectives and best regulatory practice

- 51 This paper discusses the provision of consumer protection against losses caused by solicitors' negligence. This engages regulatory objectives including protecting and promoting the interests of consumers, protecting the public interest and promoting competition. The paper recommends an option for delivering this protection based on analysis of the case for consumer protection and the options for a proportionate regulatory response, in line with the principles of better regulation.

Public/Consumer impact

- 52 The paper follows a 2021 consultation which invited views on draft regulatory and equality impact assessments. It sets out our view of the need for additional consumer protection and proposes a further public consultation on delivering the recommended option for providing this protection, which will include consideration of the impact of our proposals on the public and consumers.

What engagement approach has been used to inform the work and what further communication and engagement is needed?

- 53 The paper reflects a high level of stakeholder feedback to the 2021 consultation and a further discussion paper published in August 2022. The paper proposes a further public consultation which will include proactive engagement with bodies representing consumers of legal services, solicitors and other stakeholders.

What equality and diversity considerations relate to this issue?

- 54 The 2021 consultation invited views on a draft equality impact assessment, which will be revised and subject to further consultation.

How the work will be evaluated

- 55 The paper describes planned work led by the Legal Services Board to review consumer protection arrangements across the legal services sector, in which we will participate.

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Annexes

- Annex 1** **Summary of feedback on August 2022 discussion paper**
- Annex 2** **Detailed issues relating to the future scope of cover**
- Annex 3** **Key extracts from WTW analysis**

NB: the annexes to this paper will not be published as they relate to emerging strategy or policy